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**ECONOMIC REVIEW****Naira: A new equilibrium**

The Naira hit a new low against the U.S. dollar in January. The official rate went as high as N150; inter-bank rates went up to N162, while the rate in the parallel market peaked at N170 per US dollar. The devaluation pressure from the dollar was so intense in the month that activity in the Inter-bank foreign exchange market was halted in some sessions and trading hours was revised in more than one occasion. The recent downtrend has been developing since early December when the effect of tightening foreign credit and a slowdown in foreign direct investments flows began to show. As a result, there were frantic calls for the Central Bank of Nigeria (CBN) to take decisive action to stabilize the Nigerian currency.

To ensure a more orderly devaluation of the naira, the CBN announced sweeping measures to curb the volatility in the foreign exchange market. These measures include the return to the Retail Dutch Auction system (RDAS); reduction in bank's open position limit from 10% to 5% of shareholder's funds and the narrowing of Bureau de change bid and ask spreads around the CBN rate to between plus and minus 2%. According to the monetary authority, the move from a wholesale auction system to a retail auction system was to stem the tide of speculation on the naira. In the current system, banks can only submit bids on behalf of clients with certified letters of credit. As a result of these measures, calm has been restored to the nation's FX markets; the naira now trades between N144 and N149 per US dollar.

**Inflation: still in double digits territory**

Inflation figures for the month of December were released by the Nigerian National Bureau of Statistic (NBS) this month. The consumer price index, a proxy for inflation inched up marginally from November's figure by .3%. On a month-on-month basis the index was up .78% in December compared to .54% for the same period in 2007. The year-on-year inflation figure now stands at **15.1%** while core inflation (All items less farm produce) is now at **10.4%** compared to 9.3% last month.

The climb in December's figures was spurred by a .63% rise in the prices of Food and Non-Alcoholic beverages, 3.16% increase in the cost of education, and a 2.01% appreciation in the cost of healthcare in the month. Also, transportation cost inched up by 1.87%, Housing and energy cost moved up by 1.61%, clothing and footwear cost was up by 1.07%. The cost of recreation and Furnishing & other household materials were the only items exerting a downward pressure on the index.

On a twelve month basis, the cost of living in Nigeria appreciated in 2008 compared to 2007. The year-on-year average for the CPI in 2008 was **11.52%** compared to 5.41% in 2007. This jump in the cost of living was largely driven by the hike in food prices. Food, a volatile component of the CPI rose on average from 1.91% in 2007 to 15.98% in 2008 (see Exhibit 1). However, core inflation on average was lower in 2008 compared to 2007.

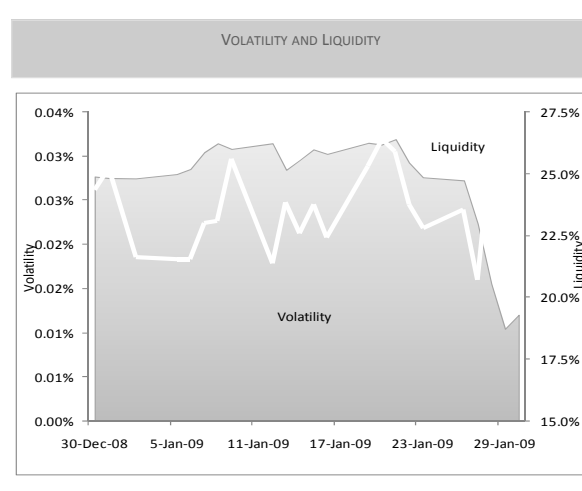
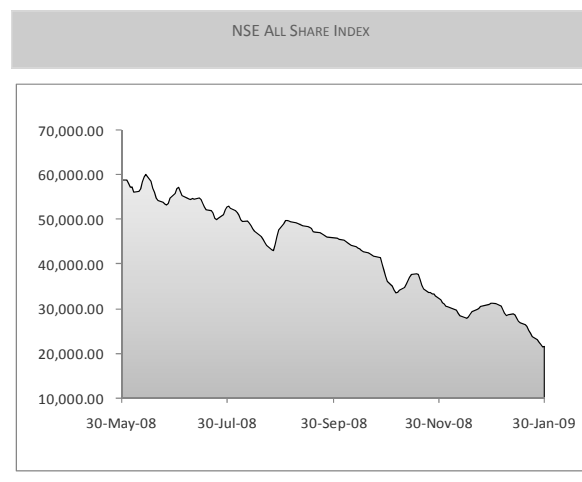
## NIGERIAN MARKET MONITOR

### Market Review

Nigerian stocks retreated in January 2009 as investor’s risk aversion to equities failed to ease. The NSE all share index recorded its worst monthly performance since 1998, dropping by 30.64% this month. The index was in the red in 17 of the 20 trading days losing an average of 2.11% daily to close at 21,813.76, a drop of 9,637.02 points from December’s close. The performance this month compares to last months drop of -4.77%. The last time trading on the exchange was this volatile was in October 2008 when the index fell by 21.4%. Stocks that topped the losers chart this month lost between 50% and 74%. On a regional basis, Nigeria lagged behind all markets under our coverage (see exhibits on page 3).

Analysts attribute the strong level of volatility seen this month to institutional investors winding down on their equity exposure. Also, uncertainty in the global space weighed on investor’s willingness to carry out investment transactions. As a result, the number of stocks closing on offer was on the increase while the level of buying dropped significantly.

The above factors culminated in the decline of activity on the exchange this month. A comparative analysis of volume traded in January 2009 and the corresponding period in 2008 shows that both volume and value traded fell by 78% and 89% respectively.



NSE: TOP 5 MONTHLY % GAIN SINCE 1998

Date	INDEX	MONTHLY PERFORMANCE
Jun-99	5,977.89	21.60%
Aug-06	33,096.37	18.71%
Oct-03	18,743.49	13.59%
Dec-00	8,111.01	13.58%
Jan-04	22,712.88	12.84%

NSE: TOP 5 MONTHLY % LOSS SINCE 1998

Date	INDEX	MONTHLY PERFORMANCE
Jan-09	21,813.76	-30.64%
Oct-08	36,325.86	-21.40%
Jul-99	4,964.35	-16.95%
Aug-04	23,774.27	-12.15%
Aug-08	47,789.20	-10.02%

**GLOBAL MARKET MONITOR**

This month, markets across the world, still suffered from the uncertainty that pervaded major equity markets during the last quarter of 2008. Investors adorned a cautious approach to equities, ensuring that their appetite for risk is still very minimal.

Worries about the deepening recession, as well as the rise of unemployment data across the developed world weighed on the equity market. Japan's bench mark index fell 9.8% in the month, this fall represents the biggest fall since the month of October 2008, when it dropped 24%. In London, the FTSE 100 index struggled for direction, the index closed down by 6.42%. In the US, the S&P 500 shed 77.5 points to close 8.6% down, while the Dow Jones Industrial Average lost 8% in the month.

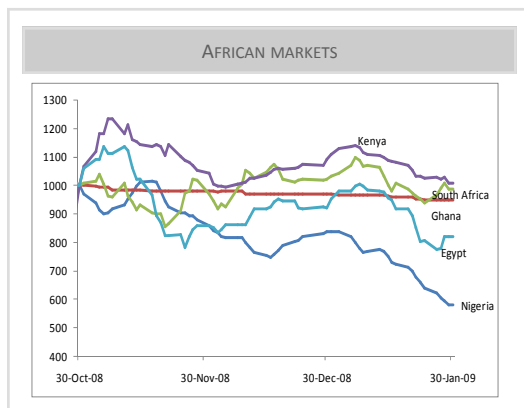
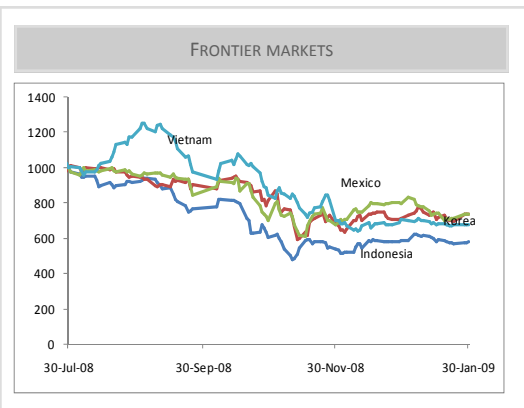
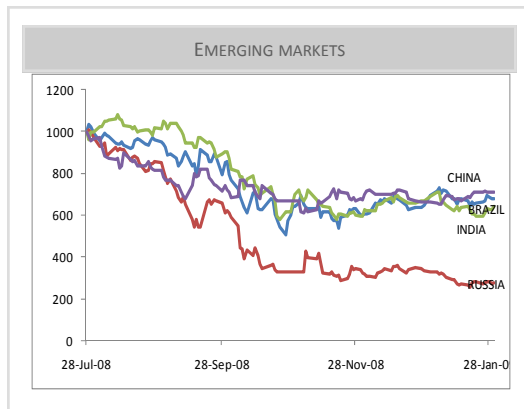
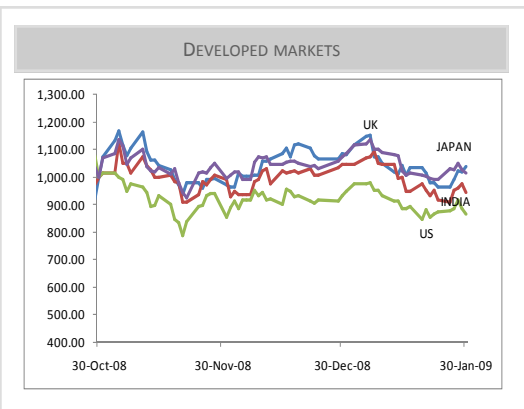
Regardless of the gloom surrounding the financial market, there are still efforts to revive ailing industries. The Obama administration has proposed another economic stimulus package to congress in this regard. Investors reacted positively to this news during the last week of the month.

AFRICAN MARKETS		
	MTD %	YTD %
Nigeria	-30.64	-30.64
Ghana	-2.42	-2.42
Egypt	-19.34	-19.34
Kenya	-9.15	-9.15
South Africa	-4.37	-4.37

DEVELOPED MARKETS		
	MTD	YTD
Japan	-9.77	-9.77
UK	-6.42	-6.42
US	-8.58	-8.58

EMERGING MARKETS		
	MTD	YTD
Brazil	4.66	4.66
Russia	-14.45	-14.45
India	-3.96	-3.96
China	9.33	9.33

FRONTIER MARKETS		
	MTD	YTD
Bangladesh	-4.2	-4.2
Indonesia	-1.68	-1.68
Korea	3.35	3.35
Mexico	-7.59	-7.59
Pakistan	-8.31	-8.31
Philippines	-2.55	-2.55
Turkey	-3.46	-3.46
Vietnam	-3.93	-3.93



## PORTFOLIO ALLOCATION

### Portfolio Positioning

Equities	Underweight
Nigeria	Neutral
Africa (x Nigeria)	Neutral
Developed World	Neutral
Emerging World	Neutral
Fixed Income	Overweight
Fixed Deposits	Overweight
FGN Bonds	Underweight
Real Estate	Underweight
Alternatives	Neutral
Private Equity	Neutral
Commodities	Neutral

### Sector Positioning

Sector	Positioning
Banking	Overweight
Building Materials	Overweight
Consumer Goods	Overweight
Healthcare	Overweight
Insurance	Overweight
Industrials	Neutral
Petroleum Marketing	Underweight
Packaging	Neutral
Others	Neutral

The current turbulence in the global macroeconomic environment poses short-term challenges which necessitated the review of our portfolio allocation strategy. However, we view this uncertainty as a great opportunity to begin to accumulate underpriced assets with a view to hold for the long-term.

**Equities:** We continue to recommend that clients keep diversification as a watchword, particularly in these times of uncertainty. Hence we recommend that clients desist from keeping all their equity and currency exposure in one country.

Last year's correction has made select equity markets, including Nigeria, very attractive over the medium to long term. Therefore, we recommend that investors begin to leg into the market with caution; accumulate select high quality names on dips with the view to be fully invested over 12 months.

We now remove our underweight to global equities and now recommend a neutral allocation, as these markets have likely priced in most of the bad news of the global crisis. In addition, historically, these markets tend to recover long before the data reflects good news.

**Fixed income:** Fixed income assets will increasingly appear as a good investment alternative to the stock market as rates stay high and markets remain volatile. We expect rates to remain in the high double digits, making simple fixed deposits very attractive. Also, institutional investors will have ample opportunity to buy credit at depressed prices due to the global de-risking that is still ongoing.

**Other Asset Classes:** We have downgraded our previous weighting of real estate from a neutral to an underweight position. We expect the high-end of the real estate market to correct anytime soon as valuations appear stretched primarily due to speculative activity.

## SECTOR POSITIONING

Given the ongoing market correction, we continue to see true value across a range of sectors and industries. We are particularly biased towards the banking and insurance sectors as stocks have continued to show solid earnings growth even as stock prices dropped. We however recommend a cautious and defensive position within these sectors—overweight the quality names as we expect the market to place a premium on these stocks.

We continue to recommend that clients diversify their holdings across several sectors as this minimizes portfolio risk. Non-financial sectors, such as consumer goods, healthcare, and building materials, also look very attractive. We are however underweight the petroleum marketing sector as valuations indicate that these stocks may still be overpriced relative to the rest of the market. We are neutral Industrials, Packaging and others as there are no clear catalysts to unlock their value in the medium term.

Globally, we recommend an overweight to defensive sectors such as Food & Beverages and Healthcare whose earnings are likely to be more resilient to the global slowdown.

**PORTFOLIO REVIEW****Performance:**

Stocks that formed our recommendation list struggled to perform above expectations considering the prevailing investment climate, where fundamentals are thrown aside in favour of fear. PZ cussons out performed in the month recording a gain of 2.8%, Crusader remained flat while other stocks that formed the portfolio lost.

**Downgrade/Upgrade:**

This month, there were no changes from any of our positions. We believe current market conditions presents opportunities for investors with an investment horizon of between one year and five years. The contraction in fundamental valuation indicators like price-to-earnings multiples and trailing measures of book value make future expected returns higher than recent history. Investors who maintain their long-term discipline could be presented with potentially attractive entry points. Also, for investors who have exposure to these stocks this is a time to lower cost.

**Additions/Deletions:**

There were no additions or deletions from our recommendation list. However, our target prices were update to factor in additional risk that could result from the global crisis.

**PORTFOLIO PERFORMANCE**

Company	Sector	Target Price	Previous Price	Last Price	MTD
ASHAKA CEMENT	MATERIALS	27.80	17.01	9.30	<b>-45.3%</b>
LAFARGE WAPCO	MATERIALS	40.65	25.50	12.88	<b>-49.5%</b>
NIGERIAN BOTTLING COMPANY	CONSUMER GOODS	46.10	35.18	22.48	<b>-36.1%</b>
SEVEN –UP BOTTLING PLC	CONSUMER GOODS	46.32	38.61	36.01	<b>-6.7%</b>
DANGOTE SUGAR	CONSUMER GOODS	29.25	15.50	10.08	<b>-35.0%</b>
FLOUR MILLS	CONSUMER GOODS	113.04	31.99	15.12	<b>-52.7%</b>
NIGERIAN BREWERIES PLC	CONSUMER GOODS	54.21	40.85	29.99	<b>-26.6%</b>
GUINNESS NIGERIA PLC.	CONSUMER GOODS	103.76	99.50	70.20	<b>-29.4%</b>
UAC NIGERIA PLC	CONSUMER GOODS	59.30	34.60	24.88	<b>-28.1%</b>
NESTLE NIGERIA PLC	CONSUMER GOODS	136.78	191.44	133.73	<b>-30.1%</b>
PZ CUSSONS	CONSUMER GOODS	31.13	11.24	11.55	<b>2.8%</b>
BAGCO	CONSUMER GOODS	5.10	3.49	2.41	<b>-30.9%</b>
AIICO INSURANCE	INSURANCE	3.15	1.79	0.91	<b>-49.2%</b>
SOVEREIGN TRUST INSURANCE	INSURANCE	2.29	1.17	0.85	<b>-27.4%</b>
CRUSADER INSURANCE	INSURANCE	5.61	7.35	7.35	<b>0.0%</b>
MUTUAL BENEFIT ASSURANCE	INSURANCE	2.88	1.48	0.74	<b>-50.0%</b>
CONTINENTAL REINSURANCE PLC	INSURANCE	1.94	1.80	0.94	<b>-47.8%</b>

**RECOMMENDATION LIST\***

SUITABLE FOR AGGRESSIVE INVESTORS WITH HIGH RISK APPETITE AND A 12 MONTH HORIZON

	Sector	Last Price	Old Target Price	New Target Price	Recommendation	Rationale
ASHAKA CEMENT	MATERIALS	9.30	37.07	27.80	BUY	Supply gap in the cement market, rising cement prices and capacity addition would boost long term earnings despite energy constrains
LAFARGE WAPCO	MATERIALS	12.88	52.25	40.65	BUY	Rising cement prices, increased demand for cement and capacity additions would boost margins
NIGERIAN BOTTLING COMPANY	CONSUMER GOODS	22.48	56.21	46.10	BUY	Capacity expansions and upgrade of plants will help boost sales and efficiency ratios
SEVEN-UP BOTTLING PLC	CONSUMER GOODS	36.01	54.29	46.32	BUY	Capacity expansions and upgrade of plants will help boost sales and efficiency ratios but, rising raw material cost will drag down margins
DANGOTE SUGAR	CONSUMER GOODS	10.08	39.29	29.25	BUY	Capacity additions and increased demand for bio-fuels will widen demand-supply gap
FLOUR MILLS	CONSUMER GOODS	15.12	107.34	113.04	BUY	Capacity additions and growth in flour consumption driving price
NIGERIAN BREWERIES PLC	CONSUMER GOODS	29.99	60.27	54.21	BUY	Substantial scope for growth in the beer market, increased demand from growing middle class and generous dividend payout
GUINNESS NIGERIA PLC.	CONSUMER GOODS	70.20	131.06	103.76	BUY	Substantial scope for growth in the beer market, increased demand from growing middle class and generous dividend payout
UAC NIGERIA PLC	CONSUMER GOODS	24.88	63.99	59.30	BUY	Continuing disposal of non-performing assets will free up cash and capital across the business
NESTLE NIGERIA PLC	CONSUMER GOODS	133.73	164.63	136.78	SELL	Increasing economic conditions will spur demand but, increase in price of raw materials a major downside risk
PZ CUSONS	CONSUMER GOODS	11.55	30.74	31.13	BUY	Strong competition from Procter & Gamble, Unilever and imports will keep margins low
BAGCO	CONSUMER GOODS	2.41	5.73	5.10	BUY	Biggest supplier of woven sack in Nigeria. Capacity to grow earnings is enhanced by the growing demand for cement in Nigeria.
AIICO INSURANCE	INSURANCE	0.91	4.59	3.15	BUY	Economic growth, reforms in the insurance sector and improved capitalisation key to achieving target price
SOVEREIGN TRUST INSURANCE	INSURANCE	0.85	2.86	2.29	BUY	Economic growth, reforms in the insurance sector a catalyst but ,margins compared to peers a bear point
CRUSADER INSURANCE	INSURANCE	7.35	7.10	5.61	HOLD	Economic growth, reforms in the insurance sector a catalyst but ,margins compared to peers a bear point
MUTUAL BENEFIT ASSURANCE	INSURANCE	0.74	3.67	2.88	BUY	Economic growth, reforms in the insurance sector and improved capitalisation key to achieving target price
CONTINENTAL REINSURANCE PLC	INSURANCE	0.94	2.79	1.94	BUY	Economic growth, reforms in the insurance sector a catalyst but ,margins compared to peers a bear point

\*We recommend an overweight of banking stocks generally but, as a result of recent measures taken by the Banker's Committee to combat de-marketing of banks by fellow peers. Our recommendation in the interim will not include individual banks. Please call your broker for a list of banking stocks to buy.

## STOCK SELECTION METHODOLOGY

Stocks on our recommendation list are selected from the universe of equities quoted on the Nigerian Stock exchange. This portfolio of stocks is ideal for investors with a medium to long term investment horizon and high risk tolerance.

In selecting stocks that form this portfolio we screened companies listed on the exchange for features listed below:

### **Stock return relative to Industry average return:**

First, considering the ongoing market correction we screened for stocks which have performed poorly compared to their industry average. These stocks could have a greater upside potential compared to their peers.

### **Stocks with Return on Equity (ROE) greater than industry average:**

Stocks that passed the first screen were screened further to identify those that are creating value. ROE is one of the quickest ways to gauge whether a company is creating value from capital invested by shareholders or destroying it. Companies with ROE higher than their industry average are more desirable.

### **Stocks with Price to Earnings (P/E) ratio trading at a discount to their industry average:**

As a final screen, we screened for companies with P/E ratios lower than their industry average. The price-earnings ratio is a good basic measure of how a share is valued. Companies with a P/E lower than the industry average are more valuable than those that trade higher.

Stocks that passed the above three screens we valued using several discounted cash flow valuation techniques.

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