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1 THE GLOBAL ECONOMY

The economic meltdown, which was prompted by the financial crisis in the United States, was the main backdrop to activities in the past 12 months. The pace at which this crisis unfolded and its far-reaching effects make it difficult to describe the review period in terms of one central defining theme. Nonetheless, in varying degrees, the dramatic re-pricing of credit risk emerged in the third quarter of 2008, and this was made worse by lack of liquidity in many markets. The most significant causes of the crisis are the failure of financial supervision, an unsustainable model of development characterised by prolonged low savings and unbridled consumption, inappropriate macroeconomic policies, including lax lending protocols, low interest rates and the blind pursuit of profit.

By the fourth quarter of 2008, the central policy challenge across major economies, especially in the developed economies of North America and Western Europe, was clear. Generally, regulators were saddled with numerous concerns. There was a need for urgent solutions to the failure of major financial institutions in Europe and America, rapidly rising yields on mortgage-backed securities and other higher-risk securities, the crash of quoted equity prices in most stock exchanges, uncertainty over the dispersal of losses and concentration of counterparty risks (key downside of the originate-to-distribute model); increased volatility of currency and commodities prices; and liquidity crisis.

In the end, strategies in Western Europe and Northern America were focused on maintaining market liquidity through massive injection of funds with the financial services sector as prime beneficiary because of its central role in the credit creation process. The consequent recapitalisation of major banks, particularly in the US and UK, though considered inevitable, led to worries about the implications for the liberal world view of nationalising key sectors of these economies. From the US Federal Reserve, through to the European Central Bank,

additional responses by monetary authorities aimed at maintaining market liquidity included the purchase of delinquent assets; and significant interest rate cuts.

Economies in Asia, especially those heavily dependent on the export of manufactured goods, who were already buffeted by falling global demand, tried to correct for growth by stimulating domestic demand. As in a couple of Latin American economies, a number of Asian countries had recourse to policy cushions (built up in the buoyant phase of the now ended economic cycle) to ease pressures on their economies. Measures adopted included the relaxation of monetary conditions in support of the credit creation process, and permission of exchange rate depreciations. Nonetheless, spurred by the current economic trajectory, especially with domestic demand holding up much stronger than previously envisaged, China and India should weather this storm slightly better than most other economies.

Emerging economies declined somewhat faster in response to the crisis, in part because their export sectors contribute a larger portion of their domestic output. Emerging European economies faced the added challenge from the fact that a number of local credit instruments are denominated in foreign currencies, with clear exchange rate threats to households. In Africa, the gains from recent reforms, helped by positive external financing conditions, may unravel in the absence of policy to compensate for the large income loss from falling commodity prices.

Prospects for global economic recovery would depend to a great degree, unlike in previous downturns, on improving conditions in the advanced economies, especially the United States of America. It is increasingly clear that hopes pinned on growth in intra-Asian trade as a counterweight to recession in the developed economies may have been misplaced, as activity in this sector has failed to help end the downturn. For developing and emerging economies, the fiscal and monetary policy relaxation on which they

Our Brand Pillars

ENTERPRISE

In today's complex operating environment, our spirit of enterprise is helping us to meet the challenges. Through tenacity, resourcefulness and flexibility, we are maintaining FirstBank on a firm footing and repositioning as a truly modern Bank.



Cadogan Place, a residential apartment block in Oniru, Victoria Island, Lagos owned by Atrib Group, financed by FirstBank

Cadogan Place is a residential apartment block located at Oniru, Victoria Island, Lagos, owned by Atrib Group and solely financed by FirstBank. The facility will provide high-quality residential accommodation.

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had depended in their battle to contain the spills from the global economic crisis, have to be addressed within a sustainable medium-term economic framework if they are not to prove counter-productive in the longer term. This is because the size of the fiscal imbalances arising from such a relaxed policy regime will be crucial in determining the pace at which these economies will recover.

Across economies, current estimates are for continued restructuring, first in the financial services sector, which, if successful, is expected to impact on the real sector of the economies positively. This process is expected to continue all through 2010, culminating in a recovery by 2011.

1.1 The United States of America

In the year ended December 31, 2008, US policy intervention was dominated by high-profile rescues of a number of companies, the possible collapse of which posed severe risk to the system. However, with the Lehman Brothers' (one of the largest investment banks in the US) default in September 2008, intervention by the public sector only heightened existing financial sector concerns over counterparties' ability to meet their respective obligations.

With government recourse to fiscal easing, monetary policy was loosened as the Federal Reserve System subordinated its previous focus on maintaining a leash on domestic prices to its desire to keep the lending taps open. Still, the markets for short-term financing conditions continued to deteriorate as the credit squeeze was further tightened for some businesses and households. Initial policy concerns with providing liquidity to the financial services sector led to a reduction in borrowing costs, with US policy rates at 0.5%, near the zero interest floor.

Although non-financial companies entered this phase of the business cycle in better shape than in the last downturn in 1991, industrial production and merchandise trade succumbed to falling global demand and dwindling consumer spending. Corrections in household balance sheets, and rising

unemployment figures will, therefore, continue to threaten the prospects of a recovery in business confidence in the US.

With growing downside risk to the medium-term outlook, and the risk of deflation now a major worry, the US economy is now forecast by the IMF to contract by 2.8% in 2009 and to stagnate in 2010.

Over the next 12 months, the US economy is expected to come up against limits imposed on the financial services sector by a decline in consumer spending, financial sector deleveraging, and corrections to the housing sector. Although a number of initiatives have been put forward by the new administration to address this chapter of negatives, a paucity of information has meant that the markets remain tentative, and the remedies continue to underperform.

As indicated by the problem with General Motors and a number of iconic US companies, the adjustment necessary to return the American economy back to the path of growth might be still more traumatic. It is becoming increasingly obvious that the need to understand how the excesses resulted in the current downturn is no more important than the need to resolve them.

Strong policy actions in the United States will still be required if existing projections of a gradual return to the growth path in 2010 are to be realised.

1.2 Europe

With the fall in global demand taking a huge toll on countries with large export sectors, the external sector in a couple of Western European countries has come under severe pressure. As a whole, however, the region has also been affected by corrections in household balance sheets, and in the books of financial services companies.

Economies of the Commonwealth of Independent States (CIS) and emerging markets in Europe, have, on the other hand, confronted extremely challenging external financing conditions, following the reversal of capital inflows, and declining commodity prices.



Radisson Hotel, Victoria Island, Lagos

Strategically located at 1 Ozumba Mbadiwe Street, Victoria Island, the Radisson is a 170-room, five-star hotel being promoted by Anchorage Leisure Limited, to be managed by the Radisson SAS Group of Denmark. The project is being financed through a syndication of banks including FirstBank, with a syndicated medium-term debt facility contributed by the banks and a 25% equity contribution by the stakeholders. The project is expected to complete in October 2009 and the hotel should be commissioned before the end of December 2009.

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Falling global commodity prices along with the constraining effect of rising output gaps across the region have held down prices, causing policy rates to fall to record lows in the Eurozone and 0.5% or lower in the United Kingdom. As in the United States, authorities in Europe sought to relax the grip of non-performing loans on the financial services sector through the provision of guarantees and new capital. In the United Kingdom, for instance, the increasing magnitude of the official stimulus package pushed up the fiscal deficit, aggravated government debt levels, and put pressure on government bond yields.

In Germany (Europe's biggest economy) and France (its second biggest), real GDP was expected to fall from 1.3% and 0.7% in 2008, to -5.6% and -3% in 2009 respectively. Consumer prices were expected to decline over the same period, from 2.8% to 0.1% in the case of Germany, and from 3.2% to 0.5% in the case of France. Despite receding exports, Germany's current account position was expected to remain in surplus in 2009, although dropping by 110 basis points against the 2008 figure. France, on the other hand, reflecting lower domestic savings levels, was expected to see a worsening of its current account deficit over the same period. Overall, the Eurozone was expected to shrink by 4.2% in 2009 compared with marginal growth of 0.9% in 2008.

Although Europe has succumbed to the same aspects of the global economic crisis as most other advanced economies, especially the implosion of the housing sector and strained external financing conditions, problems with stimulating domestic demand, especially in the Eurozone, have worsened the impact of the crisis. In emerging Europe and the Commonwealth of Independent States (CIS), reversal of capital inflows has been the major source of their vulnerability.

The recovery outlook for the Eurozone, in particular, will depend on the extent to which the ongoing reforms of its labour and product markets help boost domestic demand. Further reforms to the financial

services industry are imperative in the economies outside the Eurozone. This would be necessary to help protect such economies against current vulnerabilities, and to boost domestic savings as a share of GDP.

1.3 Asia

The major problem confronted by Asian countries in the review period was how to compensate for the drop-off in the export-led growth of recent years, by putting in place growth-centric structural reforms that could stimulate domestic demand. That said, the more developed countries in the region manifested similar vulnerabilities to North America and Western Europe in succumbing to the economic meltdown.

Countries where exports account for a relatively lower proportion of GDP (especially in China and India) saw aggregate output growth fall far lesser than experienced by others. Across the region, the newly industrialised economies (Korea, Hong Kong SAR, Taiwan, Singapore); emerging economies in Southeast Asia; and Japan all witnessed decline in aggregate domestic output ranging from 10% to 25% in 2008.

Consumer prices in China (5.9%), India (8.3%), Pakistan (12%), Indonesia (9.8%), and Korea (4.7%) firmed in 2008, compared with their respective values in 2007. However, owing to their respective vulnerabilities to the external sector, and the strength of their domestic economies, only China (10%), Malaysia (17.4%), Hong Kong (14.2%), and Singapore (14.8%) maintained strong positive current account balances in the twelve months to December 31, 2008.

In spite of the current account balances of these countries, emerging Asia grew by 6.6% in 2008 as against 9.8% in 2007.

Intra-Asian trade, which was supposed to have allowed Asia ride the crest of the global financial storm, has not achieved the desired impact yet. Consequently, policy response across the region has sought to rebalance growth from external to domestic sources.

1.4 Africa

Africa has enjoyed robust economic performance in recent years, driven by healthier domestic policies and benign external conditions. However, while effectively divorced from direct subprime lending and related investment markets, the continent is being affected by a contraction in trade, investment inflows, diaspora remittances and, quite possibly, aid and donor inflows.

Consequently, the continent's aggregate output grew to 5.2% in 2008 from 6.2% in the previous year. With exports being the most affected by the downturn in global demand, international commodity traders have endured the most of the recent reversals in global economic fortunes. Across the continent, the negative feedback loop between the financial and real sectors of the economy has seen a readjustment of prices across sectors.

Although the relationship between falling commodity prices on the world market and prices in the respective economies on the continent is not as linear as in the advanced economies, inflationary pressures have softened, on the average, continent-wide. In countries where adjustment to the exchange rate has borne the brunt of domestic response to the external shocks, inflationary pressures have, indeed, pushed up slightly.

And the policy response function in the more advanced countries on the continent, especially the monetary and fiscal easing that were required to maintain system liquidity, could worsen the continent's overall fiscal position, even as current account balances are expected to deteriorate substantially. It is estimated that the external balance of the continent will weaken from a surplus of 1% in 2008 to a deficit of 6.5% of GDP in 2009.

Ethiopia (11.6%) and Angola (14.8%) turned in the region's fastest aggregate output growth rates in 2008. Although Angola, with its huge oil-base should witness negative growth this year, Ethiopia, given its more diversified economic base, should still grow by 6.5% in 2009. Tanzania (7.5% in

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2008 and 5% in 2009), Ghana (7.2% in 2008, and 4.5% in 2009), and Morocco (5.4% in 2008 and 4.4% in 2009) are all expected to ride the storm better than most economies. Overall, oil importers are expected to do better than oil exporters.

The global financial crisis impacted the continent in different ways. Commodity importers on the continent have borne the brunt a lot less than exporters. However, recourse to structural reforms by a number of economies on the continent ahead of the crisis meant that the continent has responded to this particular shock in earnest, unlike in the past. Enhanced private sector contribution to the domestic value creation process, and improved public expenditure management frameworks have been vital to this process.

The region's short- to medium-term outlook is a function of how it recovers from the current crisis, and its ability to play larger roles in the global economy. Ultimately, both these dimensions call for further reforms in its respective economies, especially those reforms that could help boost intra-region trade. The rising popularity and return of democratic governance and accountability across the continent have been material to the success of the reform drive. Going forward, this process must be broadened to ensure that decision-making across the continent resides at the lowest feasible level of government.

2 NIGERIA

2.1 The Domestic Political Environment

Nigeria's most recent democratic experiment, the Fourth Republic, came of age in the review period, as neither rulings by election tribunals, nor the eventual outcome of by-elections for seats where elections had been declared inconclusive, threatened the nation's social and political fabric. The Independent National Electoral Commission (INEC) conducted 41 by-elections during the review period, comprising five governorship, two senatorial, six for federal constituencies, 27 for state constituencies, and one

councillorship election. In recognition of the need to strengthen voice and accountability in our democracy, the federal government received a White Paper on the report of the Electoral Reform Committee headed by Justice Muhammad Lawal Uwais (retired).

There were, however, major negatives to the political outlook, including the restiveness in the Niger Delta, and ethno-religious clashes in some parts of the country. The Niger Delta militancy disrupted the country's oil production and the supply of gas to the nation's thermal plants, which affected electricity generation and supply negatively. In search of an enduring resolution of the crisis in the Niger Delta, the federal government continued with its reforms through the creation of an additional ministry for the area. It is hoped that this initiative will lend extra focus to official attempts to resolve the sense of exclusion felt by some stakeholders in the area.

Official concerns over spillover effects of the global economic crisis on the domestic economy prompted President Umaru Musa Yar'Adua, GCFR, to set up a steering committee to evolve and drive the response to the challenges posed by the development. Also, in continuation of its reform of public sector institutions for efficiency in service delivery, the federal government began the process of decentralising the Bureau of Public Procurement, also known as the Due Process Office. When completed, this phase of the reform effort is expected to head-off delays in the commencement and implementation of projects.

Clearly, the next phase of the reform agenda should concentrate on removing all impediments to trade and business in the economy. Government remains key to the process of launching this economy on the path of sustainable development, both as the main source of most of the costs that businesses bear when they set up, and in operation – as well as a provider of collective infrastructure for the proper running of the economy.

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2.2 The Domestic Economic Environment

On the back of strong non-oil sector performance, aggregate output growth was estimated at 5.3% last year compared with 6.4% in 2007. Although industrial output fell by around 2% in the review period, this drop was compensated by strong performance in the building and construction sector (13.1%), wholesale and retail trade (12%), services (10.3%) and agriculture (6.3%).

Aggregate banking credit (net) to the domestic economy continued its upward swing during the review period, with lending to the private sector growing by 59.5% over the end-December 2007 level. This was, however, much lower than the 90.8% growth in the period ended December 2006. Aggregate bank lending to the economy rose by 100.6% in the review period as against 276% over the 12 months to end-December 2007. Bank lending largely drove the increase in monetary aggregates in the review period. Broad money supply (M2) and narrow money supply (M1) rose by 58% and 56.5% respectively, compared with 25% and 36.6% in the preceding year. Consequently, consumer prices remained under pressure during the year, rising by 11.2%, despite having grown by 5.5% in the previous year.

Although gross external reserves at US\$52.8 billion by year-end 2008 indicated a marginal increase over the US\$51.3 billion recorded in the same period in 2007, the sharp swings in the monthly totals during the year reflected a progressive decline in the nation's oil production levels. After averaging 2.5 million barrels a day (mbd) between 2003 and 2006, the nation's oil production dropped off to less than 2.2mbd by the end of 2008.

Declining oil production and oil prices on the international markets were key inputs into the ₦3.1 trillion 2009 Appropriation Bill approved by the President; 6.9% higher than the 2008 budget. At the Wholesale Dutch Auction System (WDAS),

the weighted average exchange rate of the naira in relation to the US dollar appreciated by 0.3% to US\$1/₦120.7 over the end-December 2007 figure, but depreciated from US\$1/₦123.8 to US\$1/₦125.3 in the bureaux de change segment of the market.

Government-led reform of the economy during the year included the adoption of the Financial Sector Strategy 2020 (FSS 2020) as the blueprint for its bid to ensure that the Nigerian financial system becomes one of the safest and most developed in Africa and among the top 20 in the world by the year 2020. In addition, as part of steps towards restructuring and stabilising the capital market which had experienced monumental contraction during the year, companies quoted on The Nigerian Stock Exchange were given the option to buy back up to 20% of their shares.

Given the origin of the current crisis, there are considerable limits to the use of domestic levers to prop up output. As the global economy recovers, external demand should begin to pick up. In view of Nigeria's dependence on oil export earnings, this should feed into growth. To date, domestic efforts in maintaining system liquidity require further restructuring, to lock in the gains from an orderly response to the crisis. Basic requirements for this include the need for a conservative accounting for bank loan books, and for consistent treatment of this across the sector. Public purchase of the delinquent portions of the industry's loan books, within the context of an asset management framework, may yet be necessary.

Nevertheless, the key reform requirement is at the macro-economic level, including the need to reposition the economy from its current dependence on oil export revenue. While this should reduce the economy's vulnerability to external shocks, because it requires the build-up of sustainable domestic capacity, it should also help improve the economy's growth rate.