

Group Managing Director/ Chief Executive Officer's Review



WELCOME

Distinguished Shareholders, Ladies and Gentlemen, on behalf of the Board of Directors of First Bank of Nigeria Plc, it is my pleasure to welcome you to the 41st Annual General Meeting of our Bank, and to present to you the financial statements for the nine months ended 31 December 2009.

We are meeting at a critical time in the annals of the nation's financial services sector. This reality is obvious from the fact that this general meeting has been convened at the end of a nine-month financial year. Over the last 12 months, the regulatory climate has changed radically, with the Central Bank of Nigeria (CBN) shifting its emphasis to the transparency and reliability of industry financials. Accordingly, during the period under review, the CBN directed all banks and discount houses operating in the country to harmonise their financial year-ends, and indicated end-December 2009 as its preferred date for the commencement of this policy. On the other hand, the after-effects of the global financial and economic crisis would include the redesign of the architecture of the financial services sector worldwide.

Along with the threats that come with these developments at the global level, we see innumerable opportunities in the local regulator's attempts at strengthening the domestic industry. The most immediate of these opportunities include the chance to grow our domestic and international footprints through a variety of relationships with other banks in such a way that the latter benefit from our strong franchise, while we in turn secure access to new markets. We are, to put it simply, in a unique position today, to chart new frontiers in the financial services sector, both nationally and internationally.



HEADWINDS FROM THE GLOBAL FINANCIAL AND ECONOMIC CRISIS REMAINED STRONG

In the review period, we operated in an environment dominated by risks from the global financial and economic crisis. At the global level, output continued to contract in the review period, albeit at a noticeably slower rate than has been the case previously. In the United States of America, Europe, and some parts of Asia, the first signs of recovery became noticeable towards end-December last year. However, because of the uneven nature of much of the emerging data on unemployment (US), quarter-on-quarter increases in GDP figures (US, Europe and China), and stronger than expected response in domestic demand (China), worries remained over the sustainability of this recovery. By year end, it was clear that the main task for policy authorities all over the world in the coming months will be to decide the point at which they may properly exit the financial and monetary easing, which helped, at the height of the crisis, to put a floor on the global economy's downward slide. Second-level challenges will include determining when and whether the subsequent inflationary pressures justify a firming of monetary policy. Either way, it will be crucial that fiscal and monetary authorities across the world continue to coordinate policy responses throughout the crisis.

THE DOMESTIC ECONOMY CAME UNDER PRESSURE FROM THE SECOND ROUND EFFECTS OF THE GLOBAL CRISIS

Domestically, a pickup in global crude oil prices led to an improvement in government's fiscal position and the economy's output growth. A major downside risk to the economy's outlook was removed with the conclusion of an amnesty programme, which drove a reduction in the militancy in the Niger Delta region. Because restiveness in the country's oil-producing heartland had adversely affected the nation's domestic oil-producing capacity, the pacification of the Niger Delta region ought to lead to further improvement in the economy's fiscal outlook. However, capacity limits encountered in the implementation of the budget for fiscal 2009 have raised the spectre of further setbacks in government's performance, especially the ability of the three tiers of government to meet the millennium development goals.

The adverse external and internal economic environments took their toll on the domestic banking industry. The imploding stock market and the subsequent tightening that resulted from the regulatory authorities' attempt to strengthen the market, saw a drop off in aggregate monetary growth, and a rapid build up of bank deposits. In the review period, the CBN took the unprecedented step of conducting a special audit of banks in the country. Eight banks performed relatively poorly on these tests, prompting the central bank to continue its policy of quantitative easing, including the injection of ₦620bn into the eight banks that failed the stress tests.

Not surprisingly, FirstBank was one of the banks to come away from the CBN's audit unscathed. We have always placed considerable premium on our strong ethical practices, the result of more than a century's commitment to doing business on a sustainable basis within the Nigerian economic space. Add to this our commitment to sound corporate governance practices, and robust risk management framework, and it was inevitable that we passed muster.

Significantly, the markets suffered a build up of pessimism in reaction to the apex bank's intervention in the industry. Nonetheless, deposits continued to rise as money market returns outperformed returns from other asset classes in the economy. But as soon as the market for credit came under adverse pressure because of the apex bank's activities, the industry's most pressing challenge became what to do with the increasing liquidity in the system.

Citing limited institutional policy response to the global economic downturn and the consequent sharp fall in the price of oil, the nation's leading export Standard & Poor's, a leading international rating agency, recently downgraded its rating outlook for the country from 'stable' to 'negative'.

FIRSTBANK'S PERFORMANCE

In this environment, our challenge has been how to reconcile the drop in domestic demand for credit with the build up in industry liquidity as a result of the apex bank's intervention to protect a couple of industry operators. The funds glut did result in a dwindling of margins. Consequently, across asset classes in the money market, real yields turned negative, as inflation remained sticky in lower second decile figures.

On the back of all these, in the nine months ended 31 December 2009, gross earnings rose by 28.8% to ₦196.4 billion as against the ₦152.5 billion recorded in the nine month period to December 2008. However, compared to the full year ended 31 March 2009, which had 12 months, there was a slight drop in earnings by 9.9% from ₦217.6 billion to ₦196.4 billion.

With total operating costs (excluding provision for loan losses) declining by 11.4% from ₦87.7 billion for the full year ended 31 March 2009 to ₦78.3 billion for the nine months ended 31 December 2009, the Group recorded profit before tax and provision for losses of ₦52.2 billion. However, there was an unprecedented leap in loan loss expense charged during the period on the back of aggressive provisioning for the Bank's exposure in the capital market and oil and gas segments. Post CBN-audit, the Bank made a total provision of ₦41.5 billion for loan losses as against ₦14 billion charged during the prior year ended 31 March 2009. This impacted profitability resulting in a profit before tax of ₦11.6 billion for the Group for the year ended 31 December 2009. This represents an annualised decline of 71.3% in profit before tax compared to ₦53.8 billion made for the prior year ended 31st March 2009.

While the Bank will continue to consolidate the gains of its various cost control and optimisation initiatives, during the period in review, we made a couple of improvements to our risk management process based on the lessons learnt in the year. A number of these improvement initiatives have been introduced to the Bank's credit process in order to minimise credit losses, going forward. Risk assets growth will be to sectors strategic to the economy, subject to acceptability of the risks. The process of credit portfolio planning, risk identification, measurement, control, monitoring and reporting will be more rigorous and suited to effectively manage prevailing challenges. Competency and skills in analysing and managing specialised assets will be enhanced, while remedial management of assets showing early signs of weakness will be intensified. There will be a collaborative effort between the market-facing and risk management units at ensuring that weak accounts are promptly turned around.

With the acquisition of the SAS Risk Management and Business Analytics Module, the Bank will be in a position to measure the risks in its credit portfolio, develop models to test, stress and validate different business scenarios, and more importantly determine and maintain the appropriate economic capital for the risks in the portfolio.

CHARTING A NEW ROADMAP

Given the balance of risks in the operating environment, the central task before management over the medium-term is to lead the transformation of FirstBank and its related subsidiaries into the leading financial services group in sub-Saharan Africa (ex-South Africa). In pursuit of this goal, we will be building on our strength in the domestic economy, and we will do this largely in response to the relative size

of the Nigerian economy within sub-Saharan Africa. Within this context, two things will drive the design of our domestic footprint. First, will be the fact of a relatively young population and the comparatively shallow penetration of financial services within this population; less than 30% of the domestic population have access to formal banking services. Secondly, and this is just as important, recent reforms to the domestic economy have meant its growing integration with global financial markets. Accordingly, along with a rise in demand for more sophisticated banking services from our traditional client base, as we open new markets, we expect to see rapid growth in the demand for non-bank financial services.

Seven years ago, we launched the first wholly-owned Nigerian commercial bank subsidiary in the United Kingdom in response to the needs of our clients for cross-border financial services that followed the trade flows between Nigeria and the UK. Since then, as equally strong trade flows have developed, we have gone ahead of our customers to build supporting service platforms through the setting up of representative offices in South Africa and China. I believe that this decade will see most sub-Saharan African economies consolidate on the strong policy environment, which most of them implemented over the last decade. While the plethora of free trade arrangements across the region would be useful vehicles to push this new level of reforms, it is doubtful that full regional integration can happen without extensive collaboration across the financial services space.

We intend therefore over the plan period, to which my management of FirstBank is committed, to broaden our service imprint on the continent. In the coming months, we shall be creating, through a variety of growth/entry options, a number of local banks in key economies on the continent, which shall, nonetheless, be able to leverage their membership of the FirstBank Group to provide seamless bank and non-bank financial services across political and economic frontiers.

I am aware that the success of what we have termed the 'multilocal' bank model will depend on our services and products consistently adding value to the supply chain of both existing and potential customers. Consequently, the main success factor for this model requires that going forward, we must be number one in each business line that we set up. It will be important in this respect that we are able to deploy resources as appropriate across the Group in support of our diverse business lines.

As part of the process of attaining this goal, we commenced a transformation drive in the last two years that has seen us invest extensively in the institutional capacity required to meet our ambitious growth targets. Our growth goals are very clear. And it is equally clear that we will need impeccable service levels to fulfil these aspirations. We have also invested in innovative performance management systems that will ensure that the processes through which our people realise their dreams feed through directly into the processes designed to meet our diverse stakeholder universe at its different points of need.

BANK/INDUSTRY OUTLOOK

FirstBank remains a very strong brand, strategically placed to be a dominant player in the industry. Having survived what is arguably one of the most difficult periods in the history of the nation's banking industry, there is the need for a re-positioning going forward. We have defined the outlines of the Bank's outlook to include the need to:

- build a much more efficient financial services supermarket;
- scale up our processes to take advantage of new opportunities as they emerge; and
- become the institution of choice for top talent in the industry.

In the next 12 months, we shall embark on policies that will lead to sustained growth through:

- leveraging our extensive domestic franchise to create improved risk assets;
- sourcing for low-cost deposit that can improve our net interest margins;
- income augmentation measures including write-backs on the back of aggressive recovery efforts;
- aggressive re-pricing of assets and liabilities to improve net interest margins; and
- a centralised processing infrastructure that will effectively improve operational efficiency;



Over the next plan cycle, as we pursue these objectives, we will face a considerable degree of uncertainty from planned changes in the regulatory framework. The main threats from this include proposed changes to the Basel accord's capital adequacy ratio. Although details are still being worked out, the Basel committee's reform package currently includes provisions for banks to hold countercyclical capital buffers. Ideally, these should encourage the build-up of appropriate buffers at individual banks and in the industry, which can

be deployed in periods of stress. As proposed, the planned reforms will employ countercyclical capital buffers whose value and composition will depend on one or more credit variables to ring fence the financial services sector from periods of excess credit growth. We believe that in the near-term, this will act as an additional restraint on the financial services industry's ability to create new credits.

Similarly, over the next 12 months, we expect lending conditions to tighten, as we review our respective risk acceptance criteria to reflect the lessons learnt from the current crisis. Although we expect credit demand to remain subdued over the review horizon, it is important that the Central Bank continues to promote bank restructuring to increase the industry's resilience to future shocks. That said, we expect a rapid transition to transactions in short tenured assets, as our response to the fall in interest revenue. The interbank market will remain a further downside risk. As indicated elsewhere in this report, rates in our immediate market have moderated remarkably, further limiting revenue possibilities. Elevated deposit rates could mean that over the next year, we see a restructuring of deposits away from purchased funds towards retail deposits. But until this restructuring is complete, the bigger concern would be the negative effect of all these on net interest margins.

On the upside, we see strong opportunities, in the current combination of events in the industry, for us to restructure our treasury activities. Borrowed term deposits represent a major downside risk to our outlook, as their acquisition costs constitute one of the biggest sources of pressure on current levels of profitability. If our commitment to deliver sustainable value to shareholders over the long term is to have any meaning in the current circumstance, then these unprofitable positions would have to be wound down. In other words, we have taken a conscious decision to strengthen our profit position at the expense of a drastic reduction in our balance sheet size. However, higher competition levels mean that the chance to raise contributions from the other income line would be increasingly difficult. Ultimately, a lot will depend on the extent and full effects of recoveries.

Thank you

Yours sincerely

Stephen Olabisi Onasanya
Group Managing Director/
Chief Executive Officer