Zenith Economic Quarterly

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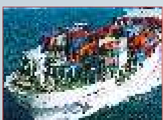

Export Processing Zone Scheme:
Nigeria's Roadmap to Economic Diversification

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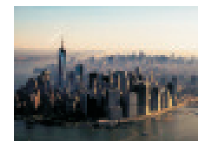

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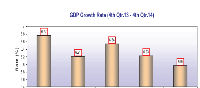
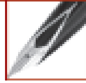


From the Editorial Suite



The Way Forward

The Federal Government of Nigeria has recently been compelled to initiate some 'austerity measures' essentially aimed at mitigating the unfolding harsh effects of the crash of the price of crude oil in the international market. The sudden crash of the price of oil, starting about seven months ago, exposed Nigeria to the vagaries and vicissitudes of a mono-product economy—which dependence on oil has made of the country for close to half a century.

In course of these decades Nigeria has become a victim of the '**Dutch disease'.** Oil boom and its attendant economic development have led to the decline or virtual abandonment of other sectors of the economy, especially the 'real sector' as represented by manufacturing and agriculture. While the huge petro-dollar inflow lasted, the nation's currency gained all the strength against other currencies resulting in the nation's other exports becoming more expensive for other countries to buy, and imports becoming cheaper, making the manufacturing/agric sector less competitive.

For every effort to free the country from the 'Dutch Disease' must be such that will lead to foreign exchange inflow other than from oil.

But with the sudden decline in the price of oil and accompanying sharp drop in revenue inflow, certain initiatives and policies have become imperative. Although the concept of 'economic diversification' has always been part of Nigeria's development plan documents, it has hardly been put into practice. It has remained just a Mantra or sing-song for successive governments, as the massive petro-dollar inflow continued. Today, the tide has changed; real economic diversification is the game changer if the economy must be salvaged. Our cover topic: 'Post-2015 Elections: Some Drivers of Nigeria's Economic Growth' points the way forward.

In the drive for the diversification, export of locally produced items must be the focus. For every effort to free the country from the 'Dutch Disease' must be such that will lead to foreign exchange inflow other than from oil. Thus, our support cover topic: 'Export Processing Zone Scheme: Nigeria's Roadmap to Economic Diversification' is an appraisal of the scheme with a view to making it more effective now than ever before. In a related treatise in 'Foreign Insights', our man in London analyses how major global developments and regional instability affected market dynamics in 2014 and points out to investors fresh directions and opportunities.

In our 'Global Watch' segment, the author examines the challenges of small-scale businesses and youth-led entrepreneurship in Ghana and offers suggestions on how to promote inclusive growth. The series on risk management in the banking industry (Number Six) continues; it harps on the imperatives for compliance with global trends and best practices.

Other segments of the journal contain no less current and informative pieces. Thus, the 'Periscope', 'Policy' and 'Facts & Figures' retain their usually rich content.

Enjoy your reading, please!

Marcel Okeke

I write to acknowledge with thanks the receipt of the July 2014 edition of the above named journal and to appreciate you for always sending us copies. The journal is insightful and educative and also a solution provider for Nigeria and global economic policy challenges.

The journal has been added to the list of our materials in the library for the benefit of staff and the public. Kindly accept the assurances of our highest regards.

Yours faithfully,
Dame Elizabeth O. Agu *(HCIB)*
Branch Controller
Central Bank of Nigeria
Maryam Babangida Way, Opposite State Secretariat PMB 1010, Asaba, Delta State.

We write to acknowledge the receipt of your letters dated January 6, April 1, July 7 and October 8, 2014, forwarding four different editions of the Zenith Economic Quarterly (ZEQ) which were received on November 27th, 2014. We commend your contribution to national development publications and we look forward to deepening relationship with you in this area. Kindly accept our best wishes

Yours faithfully,
Caroline Amachaghi (Mrs.)
For: Director General
Enugu Chamber Of Commerce,
Industry, Mines and Agriculture.

I am directed to acknowledge with thanks, receipt of the July, 2014 edition of the 'Zenith Economic Quarterly' under the cover of your letter dated 8 October, 2014.

The content of the journal was so enriching and has provided a deeper insight into Nigeria and the Global economy. We look forward to receiving your future editions. Please accept the assurances of the Ambassador's highest consideration.

Mrs. Eucharia N. Eze
For: Ambassador
Embassy of the Federal Republic of Nigeria Spain

May I please refer to your letter dated October 8, 2014, accompaniedwith the Zenith Economic Quarterly (ZEQ) which were received in this Chambers today 30th January, 2015. I am directed by his lordship to write and acknowledge the receipt of your recent publications of July, 2014 Edition of the Zenith Economic Quarterly (ZEQ) "Global Oil Outlook: Is Nigeria in a Shrinking Market?" which analyses Core Values of Banks in Nigeria and the Customers' Perception etc. and the contents therein were well understood. His lordship most sincerely appreciates the gesture and also thank you for having him on the list of those you consider should have copy of the publications. Our best wishes to you, your family end all entire members of the Zenith Bank Plc.

Yours sincerely,
Joe Osa's Igbinadolor
Secretary to Hon. Justice Mahmud Mohammed, GCON
Chief Justice of Nigeria

I am directed to acknowledge the receipt of a copy of your October 2014 edition of the Zenith Economic Quarterly (ZEQ), which focuses on "Global Oil Outlook: Non-Oil Export as Nigeria's Trump Card." There is also an analysis on Pension Assets: Catalyst for economic Development? There is no doubt that the journal is interesting and informative especially as it provides the critical information on the Nigerian and global economy for strategic policy decisions. The Director-General/CEO wishes your Bank the best in your subsequent publications.

> *"The content of the journal was so enriching and has provided a deeper insight into Nigeria and the Global economy."*

Thank you and God bless.
Uwaham Diana
For: DG/CEO
National Centre for Technology Management (NACETEM)
Federal Ministry of Science and Technology

I am directed to acknowledge with thanks the receipt of your letter dated 5th January, 2015 and the enclosed copy of your 2014 Edition of the Zenith Economic Quarterly Magazine. The report has given the Commission an insight into both the Nigerian and global economy for policy decision. Please accept the assurances of the Honourable Chairman's highest regards.

Lucky Nwosu
For: Chairman
Independent Corrupt Practices and Other Related Offences Commission (ICPC)

I hereby acknowledge the receipt of a copy of the April 2013 edition of your journal. Indeed, the theme on sustainable development is very interesting, educative and quite relevant for the academia as well as for strategic policy decisions. I appreciate your thoughtfulness and gesture. The journal is not only beautifully-printed but also well-researched. It would be a pleasure to have other editions to keep in the College library. Thank you very much.

Yours faithfully,
Professor Olukoya J. Ogen
Provost, Adeyemi College of Education
Ondo, Nigeria.

On behalf of the President of Onitsha Chamber of Commerce, Industry, Mines and Agriculture (ONICCIMA), I am pleased to acknowledge, with deep gratitude, receipt of the October 2014 edition of the Zenith Economic Quarterly Magazine. With its in-depth analyses of all the topical issues in this edition, the ZEQ has once again demonstrated its great capacity for incisive research and timely presentation of critical topics of invaluable degree to the socio-economic development of the country.

No doubt about it, our Chamber has found this edition (like all the previous ones, for that matter) very informative, indeed; and we shall remain ever grateful to you. Again, we thank you for returning our Chamber to your mailing list, after two years we have ceased receiving this publication. Please, do not leave us out again from your subsequent editions. Thank you Sir, and may you keep on doing the good job for our society. Accept the assurances our sincerest regards.

Yours faithfully,
Dominic Ajibo
Director-General
Onitsha Chamber Of Commerce,
Industry, Mines and Agriculture

I acknowledge the receipt of one copy of your informative quarterly. The quarterly is well edited and has content validity. I congratulate your team for a well-researched quarterly publication. The Department of Management will appreciate it, if previous volumes will be sent to us for our Departmental Library, even if this is done at a cost to the department. This copy is the first one we have received. Thank you for a job well done.

Yours sincerely
Prof. Donald I. Hamilton
Department of Management
Faculty of Management Sciences
Rivers State University of Science and Technology (RSUST)

PERISCOPE

Nigeria: Economy sustains Resilience

By Marcel Okeke

There is no doubt that the sudden crash of the price of crude oil in the international market by the third quarter 2014 unleashed unpalatable consequences on Nigeria and its economy. Indeed, the Organization of Petroleum Exporting Countries (OPEC) Average Monthly Basket Price of crude oil lost 43.21 percent in the whole 2014, having opened the year at US$104.71 per barrel and closing at US$59.46 per barrel. But specifically, the OPEC Average Monthly Basket Price of crude oil which peaked at US$107.89 per barrel in June came down very sharply to US$59 per barrel at end-December 2014. Despite the import and impact of this trend on Nigeria, the global rating agency, Standard & Poor's (S &P) in its latest report on the country, retained Nigeria's sovereign credit rating at BB-, with a 'negative watch.' S & P also affirmed the country's short-term foreign and local currency sovereign credit ratings at 'B'.

The agency attributed the slight adjustment in its rating for the country to the "effects of falling oil prices on the economy as well as political risk." Incidentally, some oil producing countries like Nigeria, including Kazakhstan, Bahrain, and Oman got downgraded by S & P while others, including Saudi Arabia have been put on "negative watch." In a related pronouncement on the Nigerian economy, the CNN-Money in a business analysis programme in January 2015 listed Nigeria as one of the fastest growing economies for this year. According to the report, in 2014, Nigeria's economy grew by 7.1 percent. It said that in 2015 the economy was expected to grow by another 7 percent. "By our estimate, the fastest growing economies in 2015 will be China, Qatar and Nigeria. "Nigerian economy, growing by 7.0 per cent came after China 7.3 per cent and Qatar 7.1 per cent," it said.

Also, a survey by the New York-based financial services provider, Bloomberg, shows that Nigeria is among the 20 fastest growing economies in the world, and will remain so in 2015. The survey which analyzed the economies of 57 countries placed China topmost, followed by Philippines; Kenya and Nigeria are Africa's only competitors in the top 20 economies. Nigeria, Africa's largest economy, according to Bloomberg, is expected to grow at 4.9 per cent in 2015 as against the global growth rate of 3.2 per cent.

In line with these cheering perceptions of Bloomberg, S & P and the CNN-Money, the performance of the Nigerian economy in the last quarter 2014 was 'mixed'—with some of the economic indicators either meeting or exceeding projections. For instance, the inflation rate which opened year 2014 at 8.0 per cent, closed the year

at end-December 2014 at the same level. Although the rate hit its highest level during the year in August (8.5 per cent), it decelerated all through the last quarter. It also retained the single digit, and indeed, the 6.0—9.0 per cent benchmark set by the Central Bank of Nigeria. By this trend, the inflation rate has remained in the single digit range for two consecutive years.

On the hand, the country's external reserve position was under pressure in 2014 from the increased demand for foreign exchange by foreign investors that wanted to exit the market. In the first half 2014, the external reserves declined by 14.06 per cent from US$43.61billion at end-December 2013 to US$37.48billion as at end-June 2014, and further declined by 8.04 per cent from the end-June figure to US$34.47billion as at end-December 2014. Year-on-year, the external reserves declined by 20.96 per cent.

The increased demand for foreign exchange was attributable to the eventual end of the asset purchase programme of the United States Federal Reserve (The Fed) otherwise known as 'quantitative easing'. There is also foreign investors' perceived negative impact on Nigeria's internal and external balance of the continuous decline in the price of crude oil in the international market. The insistence of the CBN to defend the value of the Naira also led to the sharp drawdown from the external reserves, as the apex bank strived to meet all perceived genuine demand for foreign exchange in the market. However, the unabated demand pressure led to the introduction of administrative measures by the CBN aimed at stemming the persistent high demand for foreign exchange and curbing the incessant drawdown from the external reserves. This has led to a devaluation of the Naira towards the end of the year.

http://www.cometonigeria.com/five-of-the-best-travel-tips/abuja-travel-tips/

Thus, the monthly average exchange rate of the Naira against the US Dollar remained relatively stable for the greater part of the year 2014, hovering around N155.23/$. The exchange rate at the rDAS window during the year opened at N157.29/$ and closed at N169.68/$, representing a depreciation of N12.39 following the adjustment of the mid-point of the official window of the foreign exchange market from N155/$ to N168/$ (that is, devaluation). At the interbank segment of the market, the Naira depreciated by N23.37 to N180.33/$, from N156.96/$ at which it opened the year. In the same vein, in the Bureaux De change (BDC) segment, the exchange rate depreciated by N29.33, from N159.12/$ in January 2014 to close at N188.45/$.

As stated earlier, the CBN in the effort to defend the value of the Naira, made sharp drawdown from the external reserves, even as the price of oil kept plummeting in the international market. On the other hand, the nation's stock of public debt inched up during the last quarter 2014: standing at N11.24 trillion as at end-December 2014, up 3.70 per cent from N10.84 trillion as at end-September 2014. The Debt Management Office (DMO) records show that

the country's domestic debt stock (Federal Government and States) stood at N9.61 trillion—representing 85.49 per cent of total debt, while external debt (Federal and States) was N1.63 trillion (US$9.71 billion)—representing 14.51 per cent of total debt.

Details of the external debt stock show that multilateral institutions accounted for 70.01 per cent. The International Development Association (IDA), a member of the World Bank Group, accounted for US$5, 857.95 million, while another member of the Group, International Fund for Agricultural Development (IFAD), is owed US$90.64 million. African Development Bank (AfDB) is US$150 million while African Development Fund (ADF) US$586.53 million. Nigeria also owes European Development Fund (EDF) US$85.98 million while US$23.78 million is owed the Islamic Development Bank (IDB). The Arab Bank for Economic Development in Africa (ABEDA) is owed US$4.48 million.

The combined external debt profile of the 36 states and the Federal Capital Territory (FCT) as at end-December 2014 stood at US$3.27 billion. Lagos State ranked tops as the most indebted state (external debt) with US$1.17 billion representing 35.82 per cent of the 36 states' and FCT total external debt. Kaduna and Cross River states came second and third with US$234.42 million (or 3.63 per cent) and US$131.47 million (or 1.35 per cent) respectively. Edo and Ogun completed the top five most indebted states (external debt) with US$123.13 and US$109.15 million respectively. Taraba is the least indebted state (external debt) in the country with US$22.78 million, representing 0.69 per cent of the country's stock of external debt.

The 'mixed' performance of the Nigerian economy in the last quarter 2014 is also reflected in the 5.9 per cent growth year-on-year it recorded in real Gross Domestic Product (GDP) terms during the period. The National Bureau of Statistics (NBS) data show that this growth level compared unfavorably with 6.2 per cent and 6.8 per cent growth recorded during the third quarters 2014 and 2013 respectively. The non-oil sector, as has been the case in recent times, was the major growth driver during the quarter under review: expanding by 6.4 per cent, though representing a decrease from 8.8 per cent and 7.5 per cent in the corresponding periods of 2013 and third quarter of 2013 respectively.

However, the oil sector surprisingly grew by 1.2 per cent during the quarter, relative to the 9.4 per cent contraction it recorded in the corresponding period in 2013. This development was attributable to the significant growth in the volume of oil production to 2.18 million barrels per day (mbpd) in the fourth quarter 2014, from 2.15 mbpd in the same period in 2013. Even with this, available data show that the sharp fall oil prices in the last seven months (to January 2015) has resulted in about 29.0 per cent drop in Nigeria's revenue. The country's gross receipts fell to a total of N3.676 trillion between July 2014 and January 2015. This represents a reduction by N1.433 trillion compared to N5.109 trillion gross Federally collected revenue recorded by the Central Bank of Nigeria in its economic report for the first half of 2014.

Federation Account figures show that while Nigeria's gross receipt in July 2014 was N630.3 billion, it was

N601.6 billion in August 2014, and dropped further to N502 billion in September 2014. It stood at N536.6 billion in October, N500 billion in November and N490 billion in December 2014; in January 2015, it declined further to N416 billion. The Federation Accounts Allocation Committee (FAAC) shared a total sum of N7.75 trillion among the three tiers of government in 2014, a decline of about N150 billion, or 1.89 per cent over the N7.9 trillion which was shared in the 2013 fiscal year.

The Capital Market

Bearish sentiments prevailed for most of the year in the capital market as foreign investors steadily withdrew from the Nigerian market, due to currency risk and the recovery of developed economies, and the effects of the US Federal Reserve tapering of its quantitative easing (QE) policy. Several macroeconomic developments also contributed to the decline in market performance. These were: (i) fall in crude oil prices and related pressure on the Naira; (ii) the impact of CBN's monetary policy changes introduced at various points throughout the year; (iii) Nigeria's declining foreign reserves; (iv) uncertainty around the upcoming 2015 elections; and (v) weak corporate earnings. The air of uncertainty that hovered over the Nigerian capital market throughout 2014 caused investors to increasingly adopt a 'flight to quality' strategy.

The All-share Index (ASI) decreased by 6, 672.04 points from 41, 329.19 points on December 31, 2013 to 34, 657.15 points on December 31, 2014. Market Capitalization decreased by N1.75 trillion from N13.27 trillion on December 31, 2013 to N11.48 trillion on December 31, 2014. Investors in the equities segment of the NSE carried out transactions worth N2.657 trillion in 2014; a breakdown of this shows that foreign portfolio investors accounted for 57.52 per cent or N1.53 trillion while domestic investors accounted for the balance of N1.136 trillion. Although 2014 was not a particularly good year for the NSE in terms of returns as the ASI closed the year with 16.14 per cent negative return, total equity transactions increased by 30.4 per cent or N624 billion during the period. In 2013, total equity transactions stood at N2.051 trillion, with foreign portfolio investors accounting for N1.042 trillion (50.80 per cent) and domestic investors accounting for the remaining N1.009 trillion.

The NSE data show that foreign investors sold off Nigerian stocks valued at N846.5 billion (US$4.5 billion) in 2014; 65 per cent more than in 2013 as a result of decline in oil prices and the naira currency depressed sentiment. Foreign investors increased the pace of stock market outflows from September 2014, selling out relatively liquid banking, consumer and oil sectors as the price of Brent crude, the benchmark against which Nigeria's oil is priced, slumped.

NASD Plc, which is the platform for trading of unlisted securities in the over-the-counter (OTC) segment of the NSE traded shares worth N2.32 billion in 2014. 120 million shares were traded in 417 deals during the 12 months of the year. This was a significant improvement on the 239, 165 shares worth N75 million traded in 34 deals from July to December 2013 when the company started operations.

In November 2014, the NSE admitted the Lotus Halal Equity ETF designed to track the performance of the NSE Lotus Islamic Index. In December 2014, the Stanbic IBTC ETF 30 was admitted to trading, and also tracks and delivers returns based on the NSE 30 Index. In November 2014, the NSE signed a capital markets agreement with the London Stock Exchange Group (LSEG) to strengthen cooperation and promote mutual development between the two exchanges.

The agreement also supports African companies seeking dual listings on the Lagos and London bourses. To increase access to Nigerian and other West African capital markets, the NSE launched direct market access (DMA) in October 2014 as a first step to the implementation of sponsored access under the West African Capital Markets Integration (WACMI) program, thereby giving global inves-

tors more control over final execution of their orders, as well as the ability to exploit price and liquidity opportunities.

The NSE was admitted to full membership in the World Federation of Exchanges (WFE) in October 2014, following a multi-year process that included a two-day onsite inspection in September 2014. Full membership in the Federation bestows a higher level of credibility and visibility upon the NSE, enabling it to promote higher standards. It also provides an avenue for increased international cooperation, as well as increased investment flows.

Oil and Gas

Available data show that average daily crude oil and gas output declined steadily throughout 2014. In the first quarter, crude oil production stood at 2.26 mbpd, valued at N2,612,066.21 million in nominal terms. In the second quarter, this decreased to 2.21 mbpd, valued at N2,633,328.61, due to a 7.6 per cent increase in the average dollar price of oil from $104.31 to $112.25. The third quarter saw a further decline in production to 2.15 mbpd, with a value of N2,328,257.79 million in nominal terms. However, production climbed 110,000 barrels a day to 2.08 million by the close of fourth quarter 2014, due essentially to the successful repair of many oil pipelines in the Niger Delta region.

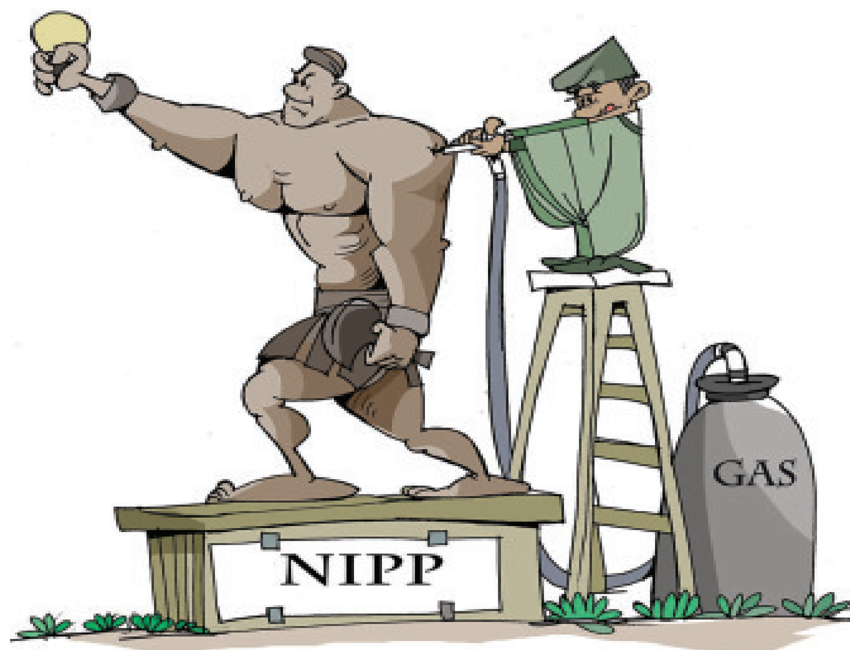
A feature of the oil and gas industry during the quarter continued to the non-passage of the Petroleum Industry Bill (PIB) by the National Assembly. The Bill has been mired in controversy, with no consensus on its key provisions. The PIB essentially proposes changes to the tax regime, royalty structure and onshore operations. While international oil companies with deep water assets are more concerned about the regulatory and fiscal provisions, others with more significant onshore assets believe the law will have adverse effect on current and future earnings as a result of reduced incentives, higher taxes and community development levies.

There are some non-fiscal issues that have been identified by the operators that require more attention from the lawmakers to ensure the viability of the industry.

These include the terms of the licenses and leases, provisions relating to the incorporated joint venture arrangements, discretionary powers of the minister of petroleum resources, dispute resolution framework, measurement point, domestic gas supply obligations and the roles of the National Oil Company.

During the period under review, security issues, sabotage and crude oil theft and pipeline vandalism continued to present significant challenges in the industry, adversely impacting onshore oil and gas production as well as the challenge to deliver same to market. The slight improvement in this situation led to some increase in oil production in the last few months of 2014.

The International Oil Companies (IOCs) operating in Nigeria continued with the sale of their equity in onshore and shallow water producing assets in the Niger Delta region. These divestments represent an opportunity for indigenous companies to participate in the upstream oil and gas industry.



Telecommunications

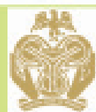
The fourth quarter 2014 data of the Nigerian Communication Commission (NCC) show that MTN and Visafone are respectively the nation's leading active operators in the GSM and CDMA telecoms markets. The South African telecom giant, MTN, still has the highest number of active subscribers in the GSM segment while Globacom is second. Further analysis shows that the MTN controls about 44 per cent of the GSM segment of the market while in the CDMA, Visafone controls about 99 per cent and Multilinks in the second place has less than one per cent of the market.

Over 60 per cent of the 18 operators in the fixed wired and fixed wireless segment have become inactive networks. However, the company, IPNX, which was inactive earlier in 2014, has become an active operator, increasing the number of service providers to six from the initial five. Overall, the GSM mobile operators accounted for 98.2 per cent, or 124.8 million, of the country's total telephony user base as at end-December 2014, followed by CDMA mobile networks with 1.57 per cent, or 2.18 million.

According to the NCC statistics, Nigeria attained 99.32 points teledensity in 2014; that is, a measure of the number of telephone connections for every 100 persons living within an area. During 2014, Nigeria grew its subscriber base by connecting additional 19.3 million, even though only11.4 million lines were active. Nigeria ended 2013 with 169.7 million connected lines with 127.9 million being active, and 88.4 points teledensity.

NCC records show that MTN had a total of 59, 797, 224 subscribers in the GSM segment as at the close of fourth quarter 2014, compared to 56, 766, 085 recorded in the corresponding period in 2013. NCC data also show that of the four CDMA operators, only two remained active at the end of 2014. Visafone led Multilinks with 2, 170, 521 subscribers in this segment. In the active fixed wired and fixed wireless segment, 21st Century Technologies had a total of 99, 446 subscribers as at end-December 2014, compared to 93, 692 recorded in the corresponding period in 2013. Visafone occupied the second place with about 99, 446 subscribers compared to 46, 046 customers in 2013. This shows that Visafone made a remarkable gain of 17.4 per cent in the fixed wired and fixed wireless segment, to close the gap with 21st Century Technologies.

(Marcel Okeke is the Editor, Zenith Economic Quarterly)



Micro, Small and Medium Enterprises Development Fund (MSMEDF) Guidelines (Revised – August, 2014)

Development Finance Department
Central Bank of Nigeria

Conclusion

CHAPTER FOUR

4.0 ROLES AND RESPONSIBILITIES OF STAKEHOLDERS

In order to achieve the desired objectives, the responsibilities of the stakeholders shall include:

4.1 Central Bank of Nigeria

The CBN shall:

a) Provide the initial Seed Fund
b) Ensure that other stakeholders co-finance the Fund
c) Act as Fund Managers
d) Chair the Steering Committee
e) Determine the limits of the Fund.
f) Specify the rate at which PFIs on-lend under the Fund
g) Absorb the subsidy which may arise in the pricing of the loans to borrowers
h) Provide regulatory and supervisory oversight
i) Determine sanctions under the Fund
j) Review the Fund Guidelines as may be necessary
k) Appraise Applications from PFIs
l) Release funds to qualified PFIs
m) Carry out verification/monitoring of projects under the Fund
n) Receive and process periodic returns from PFIs
o) Ensure the implementation of the Fund and publish periodic report on its performance
p) Retrieve funds from PFIs at the expiration of the loan tenor or infractions on the Guidelines
q) Build capacity of stakeholders.

4.2 Non-DMB /DFI Participating Financial Institutions (PFIs)

All Non-DMB/DFI PFIs shall be eligible to:

a) Grant credit facilities to MSMEs
b) Approve loan requests under the Fund based on normal business consideration
c) Open dedicated account with their correspondent banks for this window and forward details of the account to the CBN
d) Issue a letter authorizing the CBN to debit its account with the correspondent bank for recovery of outstanding principal and interest on the loan from the Fund
e) Disburse released funds to eligible borrowers within 5 working days
f) Ensure that 60 per cent of the accessed fund is disbursed to women entrepreneurs.
g) Put in place appropriate institutional arrangements for loan disbursement, monitoring and recovery.
h) Monitor the projects during the loan period.
i) Obtain credit information on borrowers from the Credit Bureaux
j) Report all disbursed loans to at least 2 Credit Bureaux
k) Render periodic returns on the performance of the loans under the Fund to the Central Bank of Nigeria as may be specified
l) Comply with the Guidelines of the Fund
m) Any other responsibility that may be required by the CBN

4.3 Deposit Money Banks (DMBs)/Development Finance Institutions (DFIs)

The DMBs/DFIs shall:

a) Not be used by State Governments to channel/ disburse funds to end users under the MSMEDF.
b) Act as correspondent banks to other PFIs (DMBs ONLY)
c) Participate under the SME window ONLY (DMBs & BOI)
d) On-lend to projects from any of the target SMEs eligible activities (DMBs & BOI)
e) Bear all the credit risk of the loans they shall be granting
f) Ensure due diligence is followed in the administration of credit facilities
g) Monitor and ensure proper utilization of the funds
h) Lend under the Fund at the specified rate
i) Submit to the CBN, Letter of offer by the bank and full details of the projects to be financed, disbursement schedule, Repayment schedule, the Credit Risk Management System (CRMS) report of the borrower;
j) Render monthly returns under the Scheme to the CBN on the reporting format.

4.4 Federal Government (FG)

The FG shall:

a) Contribute to the Fund
b) Support the Fund's activities
c) Serve on the Steering Committee

4.5 Development Partners

The Development Partners shall:

a) Contribute to the Fund
b) Provide technical assistance for the Fund's activi ties
c) Promote and support the development of MSME subsector

4.6 Apex Associations

The Apex Associations shall:

a) Confirm membership of would-be PFIs
b) Monitor performance and ensure prompt repay ment of loans by members.

4.7 Borrower

The borrower shall:

a) Utilize the funds for the purpose for which it was granted.
b) Adhere strictly to the terms and conditions of the Fund.
c) Make the project and records available for inspection by the CBN and PFIs.

CHAPTER FIVE

STATE GOVERNMENTS' AND FEDERAL CAPITAL TERRITORY (FCT) PARTICIPATION UNDER THE FUND

5.0 Background

In recognition of State Governments/FCT strategic role in grassroots economic development, the Fund anticipates their indirect participation through the PFIs in their respective jurisdictions.

5.1 General Requirements

To participate in the Fund, a State Government/FCT shall satisfy the following conditions:

a) Provide evidence of Resolution of State House of Assembly authorizing the State to participate and access the Fund.
b) Establish a Micro Credit/MSME SPV which shall coordinate the applications by PFIs for the Fund. However, the PFIs shall be solely responsible for the appraisal, disbursement and recovery of loans under the Fund.
c) Provide a Bank Guarantee/Irrevocable Standing Payment Order (ISPO) equivalent to the amount requested including interest charges. The ISPO shall be invoked to accommodate the outstand ing amount in default at the end of the loan tenor.
d) Sign a Memorandum of Understanding (MoU) with the CBN on modalities for the implementation of this window.
e) Operate a Sinking Fund Account with the CBN, into which any outstanding balance of disbursed amount shall be paid at the expiration of the loan.
f) Present a convincing annual framework on empowerment programme for prospective target groups, thereby creating sustainable demand for financial services and providing the basis for measuring performance of the Fund.

5.2 **Capacity Building**

Capacity building shall be conducted for PFIs and borrowers as specified below:

a) PFIs: PFIs shall mandatorily undergo pre-disburse ment capacity building programme to be imple mented by the CBN. The Programme shall cover loan appraisal, disbursement, monitoring and re covery among others.

b) Borrowers: The State Government/FCT shall provide capacity building opportunities to borrowers through State-owned skills acquisition/ vocational centres, CBN Entrepreneurship Development Centres (EDCs) or anysuch relevant agencies.

5.3 **Utilization of Fund**

a) **Maximum Limit per State/FCT**
A State Government or the FCT shall access a maximum of N2.0 billion.

b) **Tenor**
The facility shall have a maximum tenor of one (1) year for micro enterprises and up to five (5) years for SMEs with option of moratorium. PFIs shall access the fund as many times as possible upon full repayment.

c) **Interest Rate**
The interest rate shall be at 3% per annum to the State PFIs for on-lending to borrowers at a maxi mum of 9% per annum, inclusive of all charges.

5.4 **Participating Financial Institutions (PFIs)**

The State Government/FCT shall participate in the Fund through any of these PFIs (government or privately owned) in their Local Government Areas:

a) Microfinance Banks (MFBs) 21
b) Non-Governmental Organization – Microfinance Institutions (NGO-MFIs)
c) Financial Cooperatives
d) Finance Companies

5.5 **Mode of Application**

The required modalities are as follows:

a) The borrowers shall apply to the PFIs for a facility.
b) The PFIs shall appraise the applications for economic and financial viability of the request.
c) The PFIs shall forward their applications through the State SPV to the CBN specifying the amount, categories of clients, purpose, etc.
d) CBN shall appraise all applications submitted by the SPVs in favour of the PFIs, in line with the criteria in Section 5.5.
e) CBN approves and disburses funds through the PFIs' correspondent banks.

5.6 **Roles and Responsibilities of Stakeholders**

To achieve the desired objectives, the responsibilities of the various stakeholders shall include:

5.6.1 **Central Bank of Nigeria**

The CBN shall:

a) Articulate clear guidelines for the implementation of the Fund.
b) Provide funds for the programme.
c) Open a Repayment/Sinking Fund Accounts for the ISPO proceeds and the interest charges from the State Governments/FCT
d) Provide capacity building programme from the Grant Component to PFIs in the areas of loan appraisal, disbursement, monitoring and recovery among others
e) Release approved fund to the PFIs through their correspondent banks and advise the PFIs accordingly.
f) Notify the State Government/FCT through the State-SPV of all disbursements made to the PFIs
g) Monitor the implementation of the Fund and prepare periodic reports on its performance
h) Receive periodic returns from PFIs as may be specified
i) Ensure compliance of other parties with the Guide lines.

5.6.2 **State Government/FCT**

The State Government/FCT shall:

a) Provide evidence of Resolution of State House of Assembly authorizing the State to participate and access the Fund.

b) Establish a Micro Credit/MSME Special Purpose Vehicle (SPV) for the purpose of coordinating applications by PFIs for the Fund. The PFIs shall be solely responsible for the administration (disbursement and recovery) of the Fund.
c) Provide a bank guarantee or Irrevocable Standing Payment Order (ISPO) for the loan amount plus interest charges signed by the State Governor, Commissioner for Finance and State Ac countant General.
d) Comply with terms and conditions of the MoU.
e) Access the Fund on behalf of their participating financial institutions at 3% interest rate per annum.
f) Present a convincing annual framework/roadmap on their empowerment programme for prospective target groups, as a basis for measuring performance of the loan
g) Provide borrowers of the Fund with capacity building opportunities through State-owned skills acquisition/vocational centres, CBN Entrepreneur ship Development Centres (EDCs) or any such relevant agencies.

5.6.3 **State Special Purpose Vehicle (S-SPV)**

The S-SPV shall:
a) Collate and forward applications by PFIs to CBN
b) Carry out quarterly monitoring of PFIs activities
c) Render quarterly report on performance of the loans to the State Government and CBN.
d) Build capacity of MSMEs under this window

5.6.4 **Participating Financial Institution (PFIs)**

The PFIs shall:
a) On-lend funds to MSMEs
b) Disburse funds within 5 working days of receipt to the borrowers
c) Monitor funds utilization by borrowers
d) Ensure repayment by borrowers
e) Open dedicated account with their correspondent banks for this window and forward details of the account to the CBN
f) The PFIs shall repay principal and the interest on the approved facility to the CBN as and when due
g) Render periodic returns to CBN and State SPV
h) Not be eligible to function as SPVs for States under the Fund

5.6.5 **Deposit Money Banks (DMBs)**
a) Open a dedicated account for PFIs for disburse ment and recovery under this window.
b) Ensure release of approved funds to PFIs within 48 hours.
c) Remit repayments by PFIs to CBN within 5 working days.

5.7 Monitoring & Evaluation Framework
a) The projects shall be subject to on-site verification and monitoring by the CBN in conjunction with the PFIs during the loan period.
b) There shall be off-site monitoring through quarterly reports submitted to CBN and the State SPVs.
c) Reports of the monitoring exercise shall be shared with the concerned PFIs and State Governments.
d) The State SPVs and CBN shall leverage Apex Associations' capacities and information in monitoring and evaluation.
e) CBN shall periodically evaluate the activities of the State SPVs and PFIs to ensure achievement of the objectives of the Fund.

5.8 **Infractions**

PFIs and State Governments/FCT may be suspended or black listed for infractions such as fund diversion, etc.

5.9 **Amendments**

The provisions of the Guidelines under this window shall be subject to review as shall be deemed necessary.

Enquiries and Returns should be addressed to:
The Director, Development Finance Department,
Central Bank of Nigeria,
Corporate Headquarters
Central Business District, Abuja.
Fax No. 09-46238655
www.cbn.gov.ng

APPENDIX

Definition of Terms

1. **Micro Enterprises**
   These are enterprises with less than 10 employees with a total asset of less than N5 million (excluding land and buildings) and operated by sole proprietor.

2. **Small and Medium Enterprises (SMEs)**
   SMEs are entities with asset base of N5 million and not more than N500 million (excluding land and buildings) with employees of between 11 and 200.

3. **Women-Owned Enterprises**
   These refer to Nigerian women (group or individuals) or enterprises that are at least 75% owned by female Nigerians.

4. **Participating Financial Institutions (PFIs)**
   PFIs shall be Microfinance Banks, Microfinance Institutions (NGOs and Financial Cooperatives), Finance Companies and Deposit Money Banks (DMBs) that satisfy the eligibility criteria defined in this Guideline.

5. **Microfinance Banks (MFBs)**
   MFBs are companies licensed by the CBN to carry on the business of providing microfinance services, such as savings, loans, domestic funds transfer and other financial services that are needed by the economically active poor, as defined by the Revised Regulatory and Supervisory Guidelines for Microfinance Banks in Nigeria.

6. **Microfinance Institutions (MFIs)**
   MFIs are establishments registered to carry on the business of microfinance services, such as savings, loans and other financial services that are needed by its members.

7. **Finance Companies (FCs)**
   FCs are companies licensed to carry on the business of providing financial services to individuals, entrepreneurs, industries as well as commercial or agricultural enterprises as defined by the CBN Guidelines for Finance Companies in Nigeria.

8. **Deposit Money Banks (DMBs)**
   Deposit Money Banks (DMBs) are banks licensed by the CBN under the BOFIA and shall serve as PFI and as correspondent bank to other PFIs under the Fund.

9. **Development Finance Institutions (DFIs)**
   Development Finance Institutions are specialized financial institutions often backed by Government to provide crucial financial intermediation with the aim of closing up the supply gap in the financial system. DFIs usually provide long term, low risk debt and equity finance to projects for promoting sustainable economic growth.

10. **State-Special Purpose Vehicle (S-SPV)**
    A privately managed entity established by a State Government for the sole purpose of coordinating the activities of the PFIs that shall access funds under the MSMEDF. A PFI is therefore not eligible to function as an S-SPV under the Fund.

It is believed globally that the private sector is the engine of economic growth.

Promoting Inclusive Growth: The Entrepreneurial Environment for Scaling up Business in Ghana

By Obed Ankrah

It is believed globally that the private sector is the engine of economic growth. Studies have shown that the private sector, especially the small and medium sized enterprises (SMEs) typically account for more than 95 percent of all firms outside the primary agriculture sector, constitute a major source of employment and generate significant domestic and export earnings in the Organization for Economic Co-operation and Development (OECD), transition and developing countries. This indicates the significance of the private sector, particularly SMEs, in economic development. Additionally, young people form the largest segment of the population in many countries, especially in the developing nations. As a result of their numbers, coupled with the energy and exuberance with which they are naturally endowed, youth are usually involved in many activities. It is therefore not surprising that many countries, particularly developing countries, are advocating and actually working determinedly towards empowering their youth. It is thus essential to encourage many of them into the private sector and also promote youth led businesses.

Approaches and strategies to socio-economic growth that promote inclusiveness, especially of young entrepreneurs from different backgrounds, are critical to socio-economic development. Inclusive growth is viewed as a process of change, which creates economic opportunities along with ensuring equal access to them. Apart from addressing the issue of inequality, the inclusive growth may also make the poverty reduction efforts more effective by explicitly creating productive economic opportunities for the poor and vulnerable sections of the society. The inclusive growth by encompassing the hitherto excluded population can bring in several other benefits as well to the economy. The concept "Inclusion" should be seen as a process of including the excluded as agents whose participation is essential in the very design of the development process, and not simply as welfare tar-

http://accrareport.com/news/ghana-stops-receiving-disaster-alerts-from-the-us-geological-services-because-of-36000-debt/

gets of development programmes (Planning Commission, 2007).

This implies that inclusive growth should advance comprehensive policy approaches that create viable economic opportunities, level the playing field between varied entrepreneurs, and allow for entry of new enterprises, without excluding or disadvantaging any group or section of the business society.

The private sector and entrepreneurship are inseparable. However, it is imperative to recognize that entrepreneurs form the bedrock of the private sector, and the sector usually employs more of the working population than the public sector. For instance, according to the most recent Ghana's Population and Housing Census published earlier in 2012, the public sector, which is the second largest employer, accounts for only 6.3 percent of the economically active population (Arhin). This implies that the remaining 93.7 percent employment is employed by the private sector. Although many entrepreneurs in Ghana are in the informal economy, the entrepreneurial sector is extremely promising because when properly harnessed it has a large potential to provide employment opportunities for many more, especially the youth.

One major obstacle confronting youth-led businesses and entrepreneurs in Ghana is financing. The stark truth is that formal jobs created by the public sector over the years have not been sufficient to absorb the unemployed, especially the youth in Ghana. The alternate way to reduce this relatively high unemployment level is the private sector, specifically through entrepreneurship. Unfortunately, those who are willing to venture into the entrepreneurial environ-

ment are faced with the difficulty of securing start-up capital. However, some of the young entrepreneurs who eventually manage to start a business, finance their endeavors from their meager savings, which makes expansion extremely difficult, if not impossible. This is because the small amount of capital available to run their enterprises comes from the same pool of money to pay for their daily bread.

To a larger extent the financial sector in Ghana, including banks and micro-financing institutions, has contributed to the challenge of funding for youth led businesses. They simply lack confidence in young entrepreneurs and turn down these young people who genuinely need and apply for loans and other credit facilities to start or expand their businesses. In Ghana, the financial sector gives support to only entrepreneurs who provide collateral security. This lack or inadequate level of support from the financial sector to small enterprises limits the growth of the entrepreneurs and, by extension, the private sector in Ghana. In order to break the barrier of funding, youth who are interested in entrepreneurship often enter into partnership arrangements amongst themselves to pool resources and expertise to help start small businesses together. Also, coming together to form an identifiable business has another benefit of combining assets to provide the needed collateral to attract loans and credit facilities from financial institutions.

Another fundamental challenge to expanding youth-led enterprises is psychological in nature. In Ghana, the majority of the young entrepreneurs are risk-averse. For instance,

http://www.siemens.com/press/en/presspicture/?press=/en/presspicture/2011/corporate_communication/2011-11-african/soaxx201137-01.htm

most of my colleagues at the university preferred to work in the public sector, because to them, the public sector offers a guaranteed job. Thus, many of the youths who could have succeeded as entrepreneurs end up becoming employees rather than becoming entrepreneurs and, in turn, employing other people. Additionally, most young entrepreneurs and youth-led businesses that actually have the resources are afraid to pump substantial capital into their small enterprises because they fear losing their entire investment. They would rather play it safe by running their enterprises on a relatively small capital, so that they do not lose much investment in the event of possible economic downturns. This negative phenomenon, which I call 'anti-success mentality,' limits the expansion of many youth-led businesses in Ghana. It is therefore important that our young entrepreneurs muster enough courage to set up private businesses and further take calculated risks in expanding their enterprises. They should take advantage of their youthful exuberance.

Another critical observation about entrepreneurship in Ghana is that the sector (self employment) is misconceived by many Ghanaians, particularly among young graduates,

who believe that self-employment is the realm of the less educated or vocationally/technically trained persons, whereas college graduates deserve white collar jobs. Thus, many graduates are reluctant to go into entrepreneurship. It is not surprising that most Ghanaian graduates who take on entrepreneurship are mostly those who fail to secure formal jobs and have become frustrated. They therefore resort to setting up their own small businesses just to do something and sometimes lack passion and management skills to run their enterprises. As some entrepreneurs lack the know-how and skills to nurture their businesses, the enterprises end up collapsing or not growing. Moreover, some entrepreneurs also use such enterprises as temporary or subsidiary employment and do not devote much time and resources, leading to poor growth of their businesses.

To deal with this phenomenon of apathy, awareness about the promising and exciting aspects of entrepreneurship as a sector should be promoted to youth, especially university graduates. Additionally, entrepreneurs should be encouraged to improve their entrepreneurial and management skills periodically, in order to help them run their businesses effectively. For instance, continuing education or professional development could be provided occasionally for entrepreneurs, taking into account the ever-changing potentials and challenges of the sector so that they will be equipped with the necessary knowledge, skills, and leverage to operate and succeed in the entrepreneurial sector.

Creativity and innovation are also missing links in the Ghanaian entrepreneurial environment which prevent businesses from scaling up. Most entrepreneurs are always comfortable with the status quo. They fail to 'think outside the box,' and instead conservatively confine their businesses to methods and strategies that are out of touch with the contemporary global market. That is, they are unadventurous and fear to take up new challenges and opportunities that come their way. This myopic attitude and lack of creativity and innovation on the part of many youth led enterprises make it extremely difficult for business expansions. To counter this challenge, it is necessary for youth-led businesses and private enterprises to consider networking in order to share information and business ideas. This will foster advantages such as the sharing of information and ideas on new technology, new strategies, and new products and services in the market that are crucial to the growth and development of the entrepreneurial environment.

Furthermore, the high start-up cost for small firms, including licensing and registration requirements, impose excessive and unnecessary

https://pboats.wordpress.com/

burdens on SMEs (Aryeetey and Ahene). These conditions increase the cost of doing business and also affect the expansion and growth of the private sector and the overall entrepreneurial environment. It is important for the government to revise such policies in order to help promote and facilitate youth-led businesses to develop and expand so as to see this important part of society engaged in the economy.

Notwithstanding the numerous challenges confronting the entrepreneurial environment in Ghana, there exist some opportunities for entrepreneurs to succeed. One major opportunity is the existence of state bodies and institutions that have the oversight responsibility of ensuring the growth and success of the country's entrepreneurial sector. The Ghana Investments Promotion Centre, the National Board for Small Scale Industries (NBSSI), and Business Advisory Centers (BAC) at the district level exist to develop an enhanced environment for the functioning of private enterprises, most of which are SMEs (NDPC). Young people should take advantage of the enabling entrepreneurial environment created by these institutions, by establishing and growing their own businesses.

Moreover, the availability of successful Ghanaian entrepreneurs who are welcoming and ready to share their experiences and success stories with young and emerging entrepreneurs presents a great opportunity. There are a lot of entrepreneurs in Ghana who started at a very small and seemingly insignificant scale, but have grown their businesses into large and formidable forces over time. Notable among these businesses include Despite Group of Companies, KAMA Pharmaceutical Company Limited, and Antrak Airlines. Indeed, one is encouraged and motivated to get into entrepreneurship when these accomplished entrepreneurs share their stories. For instance, the CEO of Despite Group of Companies, Kwame Despite, started his life as a dealer in cassettes. He later traveled to Nigeria to seek greener pastures but was unsuccessful, and so he returned to Ghana to continue with his cassette business. Little by little, he managed his cassette business until he was able to raise enough capital to diversify his business. He then went into radio and other multi-billion investments, including in salt mining. He currently owns a number of radio stations, manufacturing businesses, and several foundations in Ghana. Young people should therefore take inspiration and lessons from the humble beginnings and experiences of these accomplished entrepreneurs, in order to start and grow their own businesses.

The tertiary educational system in Ghana offers the opportunity for all young graduating students, regardless of their studies, to take some

http://www.letstravelsomewhere.com/travel/africa/ghana/

form of entrepreneurial training in their final year before graduating. Fortunately, I enjoyed this opportunity during my university education at Kwame Nkrumah University of Science and Technology (KNUST). Students were taken through training sessions, including business plan preparation, how to raise capital for entrepreneurship, career development, and enterprise branding. As part of the training, students interacted with eminent entrepreneurs who shared their life experiences in the entrepreneurial sector. The training taught us young graduates that even with the little financial backing, we can go into entrepreneurship without relying on the public sector for employment. Thus, training and encouraging more young graduates to go into entrepreneurship will help encourage the expansion of the private sector.

Essentially, there is a need to grow small enterprises into larger and more prosperous businesses, so that more employment and wealth is created for entrepreneurs and trickle into the country at large. This will motivate many young people into the entrepreneurial environment without necessarily relying on the government for jobs. To grow small enterprises into larger businesses in Ghana, there is the need to make financing readily available for young entrepreneurs. Financial institutions should support the establishment and expansion of well-organized yet small businesses with or without collateral. Then they can play the role of monitoring the activities and progress of small enterprises and, where necessary, offer cautions and investment advice. These actions will be significant in financially supporting and expanding promising small businesses.

The government should protect and give preference to local and small businesses in terms of taxation and regulatory systems over the foreign businesses. The larger businesses,

especially the foreign ones, benefit from the economies of scale, technology and production systems, and global market at their disposal. This invariably gives the larger enterprises competitive advantages over the smaller ones in Ghana. These conditions make the smaller businesses unable to compete with the bigger enterprises, thereby limiting their growth and expansion. The government should therefore provide tax incentives to reduce the cost of doing business for small businesses and enable them to grow, while giving them some advantage over foreign-owned businesses.

It is also important to draw the distinction between management and leadership. While management seeks to create and maintain systems, leadership develops and provides direction for change. From this explanation, it is clear that management keeps the status quo by following structures and systems to get things done according to policy and norms, whereas leadership challenges the status quo by doing what is best at that time for the enterprise. Though managerial skills are critical, leadership is extremely important in the running of organizations, and therefore in order to create the needed change and direction for business expansion, there should be effective business leadership. Most of the young entrepreneurs in Ghana possess management skills but unfortunately lack leadership skills. This accounts for the lack of creativity, innovation, and courage on the part of young entrepreneurs to scale up their businesses. In light of this, leadership training centers should be set up to imbue young entrepreneurs with leadership qualities that will help them not just manage, but successfully lead their businesses into the inevitable changes necessary to succeed.

Also, youth-led businesses and young entrepreneurs should be mentored by accomplished and distinguished entrepreneurs and leaders who have succeeded in the entrepreneurial environment. This will provide the young and inexperienced entrepreneurs the requisite direction and sense of purpose to grow and expand their businesses.

The government can also help the necessary market for young entrepreneurs and youth-led businesses to thrive. For example in Ghana, young entrepreneurs, especially those in the arts and craft industry, lack demand from their local market. The major market for these artistic entrepreneurs is international. Unfortunately, the government does not support these entrepreneurs to market their services and products abroad. This phenomenon leaves their products at the mercy of the local market conditions, and sometimes they are left to rot in shops due to poor patronage. This culminates in the death of such enterprises. Therefore, it is advisable for the government to further understand its economy and help export products in which young entrepreneurs are well-versed. This will help grow our small arts and craft enterprises into larger and more prosperous businesses.

In conclusion, youth-led businesses in Ghana face several challenges with respect to expanding their businesses. Conversely, there exist some opportunities for such youth-led businesses and entrepreneurs to take advantage of in order to grow their small enterprises into prosperous businesses. Additionally, the government and the private sector should work together in building effective institutions and providing the right tools to grow small enterprises into larger and more prosperous businesses.

We are grateful to CIPE for permission to publish this article. *This article was the first place winner in the Inclusive Growth category of CIPE's 2012 Youth Essay Contest.*

(Obed Ankrah is a planner by profession, and also a researcher, writer, and entrepreneur).

Risk Management in the Nigerian Banking System: Challenges & Prospects (6)

By Chuks Nwaze

In the last edition of this serial, we completed a comprehensive discursion of the methodology to be employed, which has been duly employed, in the collection of field data for analysis. You will recall that the objective is to test the local efficacy of the global risk management practice which was articulated in the literature review earlier conducted. This will form the foundation of the proposed blueprint for risk management practice for our own environment which is the objective of this work. Having collected the desired data, therefore, this edition will be devoted to data presentation, analysis and discussion with a view to ascertaining the relationship between the various variables in line with the objectives of the study.

BASIS OF EMPIRICAL ANALYSIS AND TESTING

It is necessary to explain the framework for the impending empirical analysis. To enable us carry out empirical analysis and examine the effect of borrowers character, collateral, economic conditions and management on the indicators of loan performance and test the relevant research hypothesis of the study, the qualitative and subjective questionnaire responses were converted to quantitative data. To achieve this, a code scale was used to represent the degrees of agreement or disagreement of the respective respondents to the identified loan appraisal criteria and the impact of same on loan performance.

The questionnaire code ranges from strongly agree (5) to strongly disagree (1). The code manual itself relates to responses to the research statements that have to do with the two dependent variables designed to measure loan performance viz: quality of loans (QOL) and recovery of loans (ROL) as well as the responses to the research questions and statements associated with the independent variables which are borrowers character (BC), collateral (C), economic conditions(EC) and remedial management (RM). Since each of the variables has a set of research statements or questions associated with

http://sunnewsonline.com/new/?p=72468

it, the average of each respondent's opinion was computed based on the applicable degree of agreement or disagreement and quantified accordingly in terms of the relevant code representing the respondent's subjective responses. These averages were then classified into dependent and independent variables and entered into the regression model. The model was then estimated after which the numerical values of model coefficients and other relevant statistic were obtained and used for analysis.

According to the prior conceptualization that the stated loan appraisal criteria actually exert effect on the performance of such loans, functional relationships were theorized between the two sets of variables. In other words, the independent variables considered in this study are the parameters of loan appraisal. Hence, each measure of loan performance is functionally related to the same set of appraisal parameters. Thereafter, the outcome was then subjected to enhanced discussion between the estimated model and the priori expectations and further evaluated against the background of previously defined decision criteria. This evaluation will give rise to the eventual testing of the research hypotheses, leading to the acceptance or rejection of the hypotheses for the respective models at 5% level of significance (i.e. 95% confidence level).

Please see Appendix1for functional relationships and model specification as well as the regression analysis results for models 1and 2 which will form the basis of our analysis and discussion shortly.

MODEL EVALUATION AND HYPOTHESIS TESTING

Consistency with Theoretical Expectations

As can be observed, the parameter results of Models 1&2 above are consistent with a priori expectation of a positive relationship between the underlining determinants of loan performance and the ultimate fate of facilities granted with the exception of economic conditions (EC) which exhibited negative relationship with loan performance in Model I only which has to do with quality of loans (QOL). Based on the analysis of the respondents' views, this indicates, perhaps, that the impact of economic conditions such as interest rates, inflation, unemployment, government policy, etc, do not manifest at the specific time the loans were booked. But for Model 2 that deals with loan recovery, all the theorized parameters which are borrowers' character (BC), collateral(C), economic conditions (EC) and remedial management (RM) exhibit positive relationships with loan performance in line with a priori expectations.

SIGNIFICANCE AND EXPLANATORY POWER: EVALUATION OF MODEL COEFFICIENTS

Model coefficients are evaluated for statistical significance in terms of the effects of borrowers' character, collateral, economic conditions and corporate governance on the loan performance measures which are quality of loans and recovery of loans granted. This will facilitate decision on the relevant research hypothesis to adopt within the context of the model. This involves the following two steps viz.: (i) evaluation of significance of the partial or individual effects of the independent variables on the performance measures and (ii) evaluation of the joint or overall effect of all the independent variables on the performance measures. These evaluations

will facilitate the operationalization of acceptance or rejection of the research hypothesis. The applicable statistics are the t-statistic and F-statistic respectively.

Additionally, the model is further evaluated to ascertain the power of the same independent loan appraisal variables considered in the study in explaining changes in, or responses of, the performance measures which constitute the dependent variable. The purpose of this is to determine the extent to which the loan appraisal variables contained in the model are relevant in explaining variations in the loan performance measures. The relevant statistic here is the coefficient of determination (R-Squared or R^2).

Table 4.5.4: Summary of Total Effect (F-Statistic and Associated Probabilities)

	Model I	Model II
F-Statistic	52.782	324.4248
Probability	0.000000	0.000000

Significance of Total Effect: F-Statistic

Decision Rule:

Fo r the aggregate effect of loan appraisal parameters or variables on performance measures, if the probability associated with the computed value of the F-statistic is less than the level of significance selected for the operationalization of the hypothesis, the aggregate effect is deemed to be statistically significant; otherwise, it is not considered statistically significant.

In other words, if:

Prob (F-statistics) < 0.05, reject H_0 and acceptH_1.

Prob (F-statistic) > 0.05, reject H_1 and accept H_0.

Decision

According to the relevant items in the regression results of Tables 4.3.1 and 4.3.2 which have been summarized as Table 4.5.4 above, it can be observed that the computed values of the F-statistic in models 1 and 2 are 52.782 and 324.4248 respectively with associated probability of 0.000000 in each case which is less than 0.05 which implies that the aggregate effect of the loan appraisal variables on loan performance measures included in the model is statistically significant. Hence, the null hypothesis (H_0) is rejected and the alternative hypothesis is accepted. In other words, we can confidently conclude that the identified loan appraisal parameters, which are borrowers character (BC), collateral (C), economic conditions (EC) and remedial management (RM), have significant effect on the performance of loans granted.

Explanatory Power of the Independent Variables in Models 1&2

Again, the relevant items in the regression results of Tables 4.3.1& 4.3.2 have been isolated and reproduced as Table 4.5.5 above. Here, the coefficient of determination (R^2) for model I is 0.498382. This implies that the loan appraisal variables exhibit a relatively weak power in explaining variations in loan quality. For model 2, however, with R^2 of 0.782516, this indicates that the loan appraisal variables exhibit high power in explaining variations in loan recovery.

In summary, the scenario in Models 1&2 above implies that the loan appraisal variables considered in this study, which are borrowers character (BC), collateral (C), economic conditions (EC) and remedial management governance (RM) are, perhaps, more relevant in explaining the dynamics of loan recovery than loan quality in the Nigerian banking sector.

4.5.5 Summary of Explanatory Power: Coefficient of Determination: R^2

	Model 1	Model 2
R^2	0.498382	0.782516

DISCUSSION OF REGRESSION RESULTS OF MODEL COEFFICIENTS

The regression coefficients of the two models presented below will be used to discuss the variables in line with the study. Recall that these coefficients have been extracted from Tables 4.3.1 and 4.3.2. earlier presented.

QOL = 3.298113 + 0.853621BC + 0.373226C – 0.483802EC + 0.727433RM————Model 1

ROL = 3.446821 + 0.822662BC + 0.723366C + 0.5224466EC + 0.433772RM————Model 2

Summary of Individual Effects (t-Statistic and Associated Probabilities)

With respect to the research hypothesis mentioned above, the following table is relevant:

BORROWERS CHARACTER (BC)

a) Objective: To investigate the impact of borrowers' character on the performance of loans in the Nigerian banking sector

b) Research Question: To what extent does borrowers' character affect the performance of loans granted in the Nigerian banking sector

c) Hypothesis: Borrower's character does not significantly affect the quality of loans in the Nigerian banking system.

From a partial analysis of the estimated models above, it can be observed that a unit improvement in borrowers' character (BC) on the performance measures will give rise to 0.853621 increase in quality of loans (QOL) and a 0.822662 increase in recovery of loans (ROL) granted. Hence, quality of loans and recovery of loans (ROL) as measures of loans performance correlated positively with borrowers' character which is the independent variable in the two models. This is in line with the a priori expectation. It is also clear from the two models that this particular independent variable exerts the greatest influence on each of the two measures of loan performance. Please refer to Appendix3 for a descriptive analysis of responses to research questions on the impact of borrowers' character on loan performance.

Model 1			Model 2		
Coefft.	t_{Cal}	Prob.	Coefft	t_{Cal}	Prob.
α_1	5.822120	0.0000	β_1	8.38892	0.0000
α_2	2.204881	0.0000	β_2	6.43638	0.0000
α_3	-5.57212	0.0217	β_3	11.94787	0.0000
α_4	3.148801	0.0006	β_4	4.46640	0.0000

Source: E-Views7 Regression Output

Decision Criteria:
In respect of the respective coefficients, if the:

1. Probability associated with the computed value of t-statistic is less than the chosen level of significance, the coefficient is statistically significant. Hence, we reject H_0 and accept H_1.

2. Probability associated with the computed value of t-statistic is greater than the chosen level of significant, the coefficient is not statistically significant. Thus, we accept H_0 and reject H_1.

Values of t-statistic from the regression outputs in Tables 4.3.1, 4.3.2 and 4.3.3 and their respective probabilities are summarized in the above table. It should be noted that 0.05 level of significance has been chosen for the test of research hypothesis.

Decision: Hypothesis
As can be observed above, with respect to borrowers character, the probability associated with its coefficient (á-$_1$) is 0.0000 which is less than the 0.05 level of significance. We hereby reject H_0 and accept H_1 which implies that borrowers' character exerts a statistically significant positive effect on loan quality as a measure of loan performance as represented in Model 1 above. This scenario is replicated in Model 2 with respect to loan recovery as a measure of loan performance where the probability associated with $\hat{a}_1$ coefficient is also 0.0000 which is less than 0.05

Discussion of Findings:
Borrowers' character was observed to exert fundamental influence not only on the quality of loans booked but also on subsequent recovery prospects. In fact, our regression results tend to suggest that of all the independent variables considered, borrowers' character constitutes the single most important driver of loan performance in the two models, with coefficients of 0.853621 and 0.822662 for Models I & II respectively. The importance of character was emphasized by Moini (2001) who is of the view that credit is a relationship of trust and confidence between two or more persons. He reiterated the fact that credit means that a certain confidence is given and a certain trust reposed; is that trust justified and is that confidence wise? This is also in line with the position of Nwankwo (1991) who described character in this context as attributes of honesty, integrity, industry and morality. It also refers to the individual or corporate integrity of borrowers and their commitment to abide by the contract they willingly entered into.

COLLATERAL (C)

a) Objective: To evaluate the importance of collateral on loan performance in Nigeria

b) Research Question: In what way does the absence or otherwise of collateral impact on loan performance?

c) Hypothesis: There is no significant relationship between collateral and the quality of credits granted

With respect to collateral (C) on the two models above, it can be observed that a unit increase will generate a 0.373226 effect on the side of quality of loans (QOL) and a positive change of 0.723366 on the side of recovery of loans (ROL), both of which are measures of loan performance. This is also consistent with the theorized positive correlation between collateral and measures of loan performance; the above research question has been answered.

Decision: Hypothesis
The research hypothesis can also be tested by referring to Table 4.5 above. For collateral, the probability associated with its coefficient (á$_2$) is also 0.0000 which is less than the 0.05 level of significance. We hereby reject H_0 and accept H_1 which implies that collateral exerts a statistically significant positive effect on loan quality as a measure of loan performance as represented in Model 1 above. The outlook is similar in Model 2 with respect to loan recovery as a measure of loan performance where the probability associated with $\hat{a}_2$ coefficient is also 0.0000 which is less than 0.05.

Discussion of Findings
The importance of collateral is also evident from the outcome of this study. With coefficients of 0.373226 and 0.723366 for loan quality and loan recovery in models I&II respectively, this result shows that the concept of collat-

eral becomes much more critical at the point of loan recovery. This is a logical implication from the meaning of collateral which is simply defined as a real or personal property pledged by a borrower to secure a loan, such that if the borrower fails to repay the facility, the creditor may assume ownership of the pledged property. Generally speaking, therefore, while an unsecured loan is considered a low-quality loan, but more importantly, an unsecured facility does not stand a good chance of being recovered.

The outcome of this study with respect to collateralized lending is supported by Greenbaum and Thakor (1995) as quoted in Blazy and Weill (2005). According to them, there are three fundamental reasons why banks ask for collaterals and the arguments can be summarized as follows. First, collateral allows for a reduction of the loan loss in the event of a default by providing for the bank a prior title on specific assets. Second collateral helps to solve the problem of adverse selection borne by the bank when lending as it constitutes a signaling instrument providing some valuable information to the bank.

These authors insist that collateral helps the bank to obtain private information owned by the borrower, as high quality borrowers are more induced to accept to provide collateral in compensation of a low loan rate than low quality borrowers. Thirdly, collateral helps to solve the problem of moral hazard after the loan is granted: namely, the borrower is not inclined to provide the optimal effort or the optimal level of investment.

ECONOMIC CONDITIONS (EC)

a) **Objective:** To assess how economic conditions such as inflation, interest rates, unemployment, etc, affect the performance of loans in the Nigerian banking system.

b) **Research Question:** How do prevailing economic conditions such as inflation, interest rates, unemployment, government policy, etc, affect the performance of loans granted in the Nigerian banking system?

c) **Hypothesis:** Economic conditions do not significantly affect the quality or performance of loans in the Nigerian banking environment.

Again, with reference to the model parameters presented above, it is evident that economic conditions (EC) displayed a negative correlation with quality of loans (QOL) booked as shown in Model 1 with a coefficient of -0.483802. This implies that economic conditions (EC) do not move in the same direction with quality of loans granted. However, this particular independent variable (EC) correlates positively with repayment of loan (ROL) which is the dependent variable in Model 2 with a positive coefficient of 0.5224466. Although this is not in conformity with the a priori expectation, the above research question has been fully addressed. Appendix3 contains the responses to relevant research questions in this respect.

Decision: Hypothesis

Again, with reference to Table 4.5 above, we can test the research hypothesis for economic conditions. Here, the probability associated with its coefficient ($á_3$) is 0.0217 which is also less than the 0.05 level of significance. We equally reject H_0 and accept H_1 which implies that economic conditions exerts a statistically significant positive impact on loan quality as a measure of loan performance as represented in Model 1 above. For Model 2 with respect to loan recovery as a measure of loan performance where the probability associated with $â_3$ coefficient is 0.0000 which is less than 0.05, the conclusion is the same.

Discussion of Findings:

With a coefficient of -0.483802 with respect to loan quality, economic conditions marks a fundamental departure from other variables because of its negative correlation in model 1. This implies that factors such as interest rates, inflation, GDP, government policy, unemployment etc, ordinarily do not swing in the same direction with loan quality as a measure of loan performance. In other words, these factors do not determine whether a facility is a low or high quality one. However, its positive coefficient of 0.5224466 in model 1 with respect to loan recovery as a measure of loan performance is instructive. It suggests that these factors can adversely affect the chances of recovery of a facility. This is because both the borrower and the purpose for which the loan is being sought are affected by the prevailing economic and environmental factors at any point in time.

The above analysis has also been corroborated by Farhan, Sattar, Chaudhry and Khalil (2012) who focused on the economic determinants of non-performing loans (NPLs) in the Pakistani banking sector since 2006. All the

hypothesis were accepted and correlation and regression analysis described interest rate, energy crisis, unemployment, inflation and exchange rate as having a significant and positive relationship with the nonperforming loans while GDP growth has significant negative relationship with the non-performing loans of Pakistani banking sector. They added that unemployment is the other factor which has caused a huge volume of NPLs especially in the consumer finance. Saba (2012) also did a similar research on the subject which confirmed the positive association not only between interest rate and NPLs but also between real GDP per capita and NPLs.

This position was also supported by Khemraj and Pasha (2005) even though the emphasis here is on the positive link between real interest rate and NPLs. In other words, when a commercial bank increases its real interest rates, this may translate immediately into higher NPLs. It should be observed that this positive correlation has to do with model II in our study which focuses on loan recovery.

REMEDIAL MANAGEMENT MEASURES (RM)

a) Objective: To investigate the impact of remedial management measures on loan performance.

b) Research Question: What is the impact of remedial management measures on the overall quality and performance of loans?

c) Hypothesis: Remedial management measures have no significant impact on loan performance.

A look at the model parameters above will also reveal the fact that a unit improvement in remedial management (RM) practices will give rise to a positive change of 0.727433 for quality of loan (QOL) as well as a 0.433772 increase in recovery of loan (ROL) in the first and second models respectively. In other words, in line with the a priori expectation, there is a positive correlation between remedial management initiatives and loan performance in the Nigerian banking sector.

Decision: Hypothesis

To enable us test the hypothesis in respect of remedial management measures, we again refer to Table 4.5 above. Here, the probability associated with its coefficient ($á_4$) is 0.0006 which is less than the 0.05 level of significance. We equally reject H_0 and accept H_1 which implies that remedial management measures exert a statistically significant positive impact on loan quality as a measure of loan performance as represented in Model 1. For Model 2 with respect to loan recovery as a measure of loan performance where the probability associated with $â_4$ coefficient is 0.0000 which is less than 0.05 the same conclusion is also reached.

Discussion of Findings

Remedial Management: It should be noted that the remedial management under consideration here has to do with the lending institution (the bank itself). Although there is also a component of management that refers to the evaluation of management success on the venture for which money has been borrowed as well as the estimate of management determination to honour its obligations to the lender, these have been captured as part of borrowers' character. Our discussion on remedial management is focusing on the lending institution because it is the lender that bears the ultimate brunt of non-performing facilities. It is also the lending institution that must ensure that the borrower makes wise decisions not only in relation to the credit application, but also with respect to the implementation of the project for which the loan was obtained.

Perhaps, this is the reason for the superior ranking of remedial management as second only to borrowers' character with a positive coefficient of 0.727433 in Model 1 with respect to loan quality as a measure of loan performance in this study. The importance of remedial management, however, appears to diminish significantly in Model 2 at the point of loan recovery with a lower coefficient of 0.433772. The rationale for this would seem to be the fact that a facility that has been properly appraised and granted is less likely to pose recovery problems for the lender. Nonetheless, the importance of management cannot be underplayed especially with respect to remedial management of non-performing facilities which often entails internal work-out processes as well as the use of Asset Management Companies (AMCs) to acquire toxic assets and put distressed banking institutions back to liquidity where the need arises.

In the extensive study conducted by Karim, Chan and Hassan (2010) on the relationship between bank management and non-performing loans, these authors supported the hypothesis proposed by Berger and DeYoung (1997) which suggests that poor management in the banking institutions results in bad quality loans which, by implication, escalates the level of non-performing loans. In recent times, compliance with generally accepted management principles has gained considerable momentum and the banking sector is no exception.

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APPENDIX1

FUNCTIONAL RELATIONSHIPS AND MODEL SPECIFICATION

Functional Relationships

This study wishes to re-iterate its objective which is to establish functional relationships between the two dependent variables for the measurement of loan performance which are quality of loans and recovery of loans and the four independent variables that were employed for credit appraisal which are borrowers' character, collateral, economic conditions and remedial management. The two functional relationships involved are as follows:

QOL = f (BC, C, EC, RM)..Function 1

ROL= f (BC, C, EC, RM)..Function 2

Where:

QOL = Quality of Loans

ROL = Recovery of Loans

BC = Borrower's Character

C = Collateral

EC = Economic Conditions

RM = Remedial Management

Model Specification

For purposes of measurement, each of the parameters designed to measure loan performance constitutes a model. The applicable models can, therefore, be specified as follows:

$QOL = á_0 + á_1 BC + -á_2 C + á_3 EC + á_4 RM + µ$..............................Model I

$ROL = â_0 + â_1 BC + â_2 C + â_3 EC + â_{4\ RM} + µ$............................ Model II

Where: $á_i$ and $â_i$ (i= 0, 1, 2, 3, 4) are model parameters while

$á_i$ and $â_i$ (i= 1, 2, 3, 4) are coefficients of the respective independent variables with $á_0$ and $â_0$ being constants. A coefficient is a measure of the effect of each independent variable such as borrowers' character, collateral, economic condition and corporate governance on non-performing loans while µ represents a random disturbance from other factors not included in the model under consideration.

REGRESSION ANALYSIS RESULTS

The following is a summary of the regression analysis results for the two models representing the parameters of measuring loan performance (loan appraisal and loan recovery).

Model 1
Dependent Variable: QOL (Quality of Loans)
Method Employed: Least Squares
No. of Observations: 232

Table: 4.3.1

Variable	Constant	Std. Error	t- Stat	Prob.
C	3.298113	0.419721	5.702241	0.0000
BC	0.853621	0.062732	5.822120	0.0000
C	0.373226	0.124271	2.204881	0.0000
EC	-0.483802	0.099752	-5.57212	0.0217
RM	0.727433	0.056642	3.148801	0.0006

R-Squared (R^2) = 0.498382 **F-Statistic= 5 2 . 7 8 2**
Adjusted R-Squared = 0.477233 **Prob. (F-Statistic)= 0.000000**

Source: Econometric Views7: Regression Output

Model 2
Dependent Variable: ROL (Recovery of Loans)
Method Employed: Least Squares
No. of Observations: 232

Table: 4.3.1

Variable	Constant	Std. Error	t- Stat	Prob.
C	3.446821	0.462242	9.83323	0.0000
BC	0.822662	0.064311	8.38892	0.0000
C	0.723366	0.076322	6.43638	0.0000
EC	0.5224466	0.0537836	11.94787	0.0000
RM	0.433772	0.033663	4.46640	0.0000

R-Squared (R^2) = 0.498382 F-Statistic= 52.782
Adjusted R-Squared = 0.477233 Prob.(F-Statistic)= 0.000000

Source: Econometrical Views 7: Regression Output

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Post 2015 Elections: Some Drivers of Nigeria's Economic Growth

By **Sunday Enebeli-Uzor**

To say that the Nigerian economy could be in dire strait in the face of dwindling crude oil prices is to restate the obvious. Nigeria is currently experiencing economic challenges which appear to occur almost every decade – a slump in crude oil prices. The steep and sudden crash of crude oil prices in the international commodities markets and the dictates of today's global economic conditions and realities have made it imperative for urgent reform measures to guarantee sustainable economic growth and development. As an oil exporting country, decline in crude oil prices is a downside to the economy in both the short and medium term. Nigeria's fiscal revenue is overwhelmingly dominated by the oil sector which accounts for approximately 80 percent of government revenue, and up to 95 percent of foreign exchange earnings. The declining revenue from crude oil receipts cannot even be compensated by revenue from natural gas, as gas exporting countries are also wincing following a glut in the gas market. Consequently, there appears to be palpable and germane concerns on the longer term sustainability and growth of the Nigerian economy. The emerging global oil dynamics tends to indicate that the days of low crude oil prices may just be in the early days.

The unfolding scenario has again exposed the Nigerian economy to downside risks of volatility in oil prices with attendant consequences and multiplier effects on the economy and businesses as well. Anxiety on the outlook is further aggravated by past experiences where boom-bust cycle of oil (in the 1980s and 2008) culminated in macroeconomic instability induced by capital inflow reversals and currency devaluation with dire economic consequences. The concerns about the Nigerian economy have been exacerbated by the lack of a robust mitigating buffer as a result of lack of strict fiscal discipline to build reserves during boom period. The first impact of the evolving development is decline in the gross federally collected revenue accruing to the federation account. Consequently, there has been a drop in the monthly Federation Accounts Allocation Commit-

http://www.proudlyarabian.com/Abu-Dhabi/Top-Oil-Gas-and-Alternative-Energy-Companies.aspx

tee (FAAC) shared among the three tiers of government. Aside declining revenue, the Nigerian economy is faced with other headwinds. For instance, the supply gap in the foreign exchange market is increasing as the demand for dollars outpaces supplies, exerting enormous pressure on the Naira. This has led to the depreciation of the currency by the Central Bank of Nigeria (CBN). The depreciation also means that imports are likely to be more expensive and are expected to slow going forward.

Government's Initial Response

Rising to the challenge and to avert imminent fiscal crisis, the federal government adopted some austere measures to cushion the effect of the persistent drop in revenue. Some of the measures include the downward revision of the benchmark price of crude oil for the 2015 budget. A new figure of $65 per barrel has now been proposed to the National Assembly. This new benchmark has however been overtaken by the continuous slump of crude oil prices which are currently hovering around $60 per barrel. There is also renewed emphasis on non-oil revenue streams, especially taxation. The federal government has given indication that the existing framework for Value Added Tax (VAT) revenue might be adjusted to enable the states and local governments get more revenue. Under the current framework for allocation of VAT revenue, the Federal Government, States, and Local Governments receive 15 percent, 50 percent and 35 percent respectively. Possible upward review of VAT from the current 5 percent is also probable considering that VAT rate in Nigeria is one of the lowest among its African peers (Ghana – 17.5 percent, South Africa – 14 percent, Egypt – 10 percent, Algeria – 17 percent, Angola – 10 percent, and Morocco – 20 percent). One of the outcomes of the GDP rebasing exercise is the huge gap in the ratio of tax revenues to the GDP (down from 22 percent to 12 percent).

Other measures taken by the Federal Ministry of Finance (FMF) include the review of tax waivers and exemptions to rake in additional tax revenues. The FMF has announced the introduction of new surcharges on the importation and consumption of some luxury goods and services to yield an estimated N10.56billion addi-

tional revenue in 2015. Details of the proposed measures which are expected to kick in from the beginning of the second quarter of 2015 include: a 10 percent import surcharge on new private jets (estimated to yield about N3.7billion in 2015); a 39 percent import surcharge on luxury yachts (estimated to rake in N1.6billion in 2015); 5 percent import surcharge on luxury cars (estimated to yield about N2.6billion additional revenue in 2015); 3 percent luxury surcharge on champagnes, wines and spirits (expected to generate about N2.3billion this year); 1 percent mansion tax on residential properties within the Federal Capital Territory, with value of N300 million and above (estimated to yield additional N360million); and a surcharge on business and first class tickets on air travellers.

Additional measures involve plugging of revenue leakages, strengthening of tax administration, and curbing incidences of non-remittance of requisite funds to the treasury by some agencies. Consequently, the federal government has deployed electronic platforms – Treasury Single Account (TSA), Government Integrated Financial Management Information System (GIFMIS) and the Integrated Payroll and Personnel Information System (IPPIS). A number of short-term expenditure cutting measures has also been unveiled to improve government spending and save an estimated N82.5billion. Specifically, procurement and upgrade of buildings have been curtailed, potentially saving about N44billion. International travels and training have been cut by 50 percent for all Ministries, Departments and Agencies (MDAs) of the government, and this is estimated to save about N14billion. Similarly, administrative expenditure for buildings equipment and supplies as well as MDAs' provisions for the procurement of administrative supplies and equipment will be cut, saving about N5billion. Also, other provisions for overhead expenditure have been dropped completely, saving about N4billion. Finally, government also announced the commencement of partial implementation of the Whitepaper on the rationalisation of government agencies, commissions and committees, potentially saving about N6.5billion in 2015. The implementation of these short-term measures to shore up revenue could be impeded by political exigencies which oftentimes overrides economic rationality.

Beyond Short-Term Austerity Measures

As the election season comes to an end and government settles down to its responsibilities, it has assumed the "urgency of now" to chart a clear and ambitious plan to steer the economy away from near absolute dependence on oil and set it on the path of sustainable growth and global competitiveness. To ignore this exigent national imperative is to continue on a perilous course that makes the economy susceptible to the

boom-bust cycle of oil. Therefore, rather than agonize over the current economic headwinds, falling crude oil prices should provide an impetus to undertake urgent and fundamental economic reforms and diversification. With the right approach, the current oil price volatility could turn out to be the critical turning point on Nigeria's path towards economic diversification.

Interestingly, one of the major highlights of the recent rebasing of Nigeria's Gross Domestic Product (GDP) is that the Nigerian economy is more diversified than previously reported in official statistics. This vital piece of information has however been subsumed in the euphoria of becoming Africa's largest economy and knocking South Africa off its decades-long perch as the continent's largest economy. The rebased GDP numbers showed that the non-oil sector represented about 87 percent of the total GDP in 2013 compared to about 67 percent reported pre-rebasing. The oil sector on the other hand accounted for about 13 percent of GDP in 2013 post-rebasing as against about 32 percent reported prior to rebasing. The importance of this is that the contribution of the non-oil sector has been previously grossly understated alongside its enormous economic potential.

Continuous Dependence on Oil Revenue not Sustainable

Crude oil prices are exogenously determined by factors beyond the control of nominal players in the global energy market as they are mere price takers, Nigeria inclusive. The factors that drive oil prices are not always conventional interplay of market fundamentals – demand and supply. Crude oil is a potent arsenal in geopolitical war of attrition and international diplomacy. The 1973 Arab oil embargo in response to U.S. involvement in the Yom Kippur War lends credence to this assertion. Oil played a very critical role in the Second World War and since the war ended, there has been several disputes that either disrupted or threatened to disrupt the world oil supply system, especially from the Middle-East region. Even during the Cold War era, oil was at its epicentre. All over the world, from the Persian Gulf to the Caspian region, and Gulf of Guinea, wherever oil is found, there is one form of agitation, crisis or unpleasant tales.

The overwhelming influence and political leaning of major crude oil producing countries also determine crude oil prices. Major oil producing countries utilise their oil resources to pursue strategic and political objectives. Some major oil exporting countries sometimes cut oil supply to countries perceived to be pursuing antithetical interests in what has been christened "energy blackmail". The safety of oil investments has been at the fore of global peace since the Cold War. Disagreements between powerful nations that are endowed with oil resources or exert influence over oil often cascade into a spike or slump in oil prices. For instance, the ongoing bearish run in the global oil market has been blamed in part on Russia's standoff with the West. Russia is presently under excruciating pressure from the West due to the crisis in Ukraine. Russia is the world's largest exporter of crude oil, any shock to crude oil price will be encouraged by the West to hurt the Russian economy. Consequently, all other oil producing countries are vicariously bearing the brunt of Russia's impasse with the West.

The influence of the Organisation of Petroleum Exporting Countries (OPEC) in the global oil market appears to be waning. OPEC's mission is to coordinate and unify the petroleum policies of its member countries and ensure the stabilisation of oil markets in order to secure an efficient, economic and regular supply of petroleum to consumers, a steady income to producers and a fair return on capital for those investing in the petroleum industry. The cartel's avowed mission has been called to

question recently due to the lackluster posture of some powerful members. The 12-member OPEC cartel was expected to weigh in on slumping oil prices by cutting production quota to shore up prices but failed to do so in its recent meeting. Some powerful members of the cartel shirked from cutting production quota to prop up prices and instead chose to defend their market share.

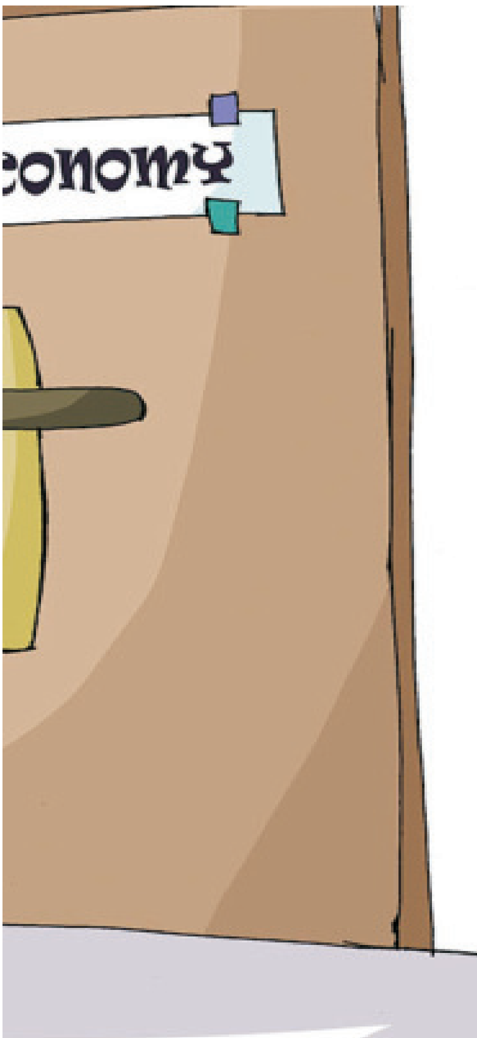
There is also a new twist in the energy market – shale oil, which has fundamentally altered the dynamics of the international oil market. Shale oil is emerging as the game changer and price determinant in the global oil market. In point of fact, the current downward spiral of crude oil prices started in June 2014 following growth in shale oil production in the United States. Shale oil is the product of technological breakthroughs – hydraulic fracturing and horizontal drilling, which have enabled U.S. domestic production to replace a significant proportion of imports. According to some estimates, the marginal cost of shale-oil production is between $55 and $70 per barrel. If a $5 profit margin is factored in, the price trajectory of oil is expected to be between $60 and $75 per barrel in the best case scenario. Consequently, except there is a significant supply shock such as major conflict in an oil-exporting region that could constrain supply and induce spike in prices, crude oil prices are expected to be moderate in the short to medium term.

Whither the Petroleum Industry Bill?

Diversifying the Nigerian economy is not a short term economic fix. It requires fundamental restructuring with policies and programmes that have long gestation periods and would take some time to yield the desired results. In the short to medium term, Nigeria will continue to rely on the oil sector and revenue from oil and gas receipts as efforts are made to derive more revenue from the non-oil sector. Curiously however, in addition to the uncertainties surrounding crude oil in the global market, the future of the oil industry in Nigeria appears grim. This is so because the much awaited Petroleum Industry Bill (PIB) is still before the

In the short to medium term, Nigeria will continue to rely on the oil sector and revenue from oil and gas receipts as efforts are made to derive more revenue from the non-oil sector.

outgoing Seventh National Assembly for consideration and enactment into law. The PIB was first presented to the Sixth National Assembly in 2009 but it was not passed into law before the expiration of the assembly. The bill has been adjudged to be one of the most profound legislations in the history of Nigeria and the oil sector. Although Nigeria's upstream oil sector ranks as one of the most developed in the continent, it is yet to attain its full potential. The PIB is expected to herald a new fiscal regime for the sustainable development of the oil sector and improved revenue for the country.



As expected, the PIB has elicited reactions from several stakeholders. Whilst it has received groundswell of support from some quarters, others contend that it is not an all-purpose elixir that will address all the challenges of the oil sector. For instance, the International Monetary Fund (IMF) has canvassed for the early passage of the PIB. The IMF reckons that the bill would boost investment, government revenue and fiscal transparency. International Oil Companies (IOCs) on the other hand have maintained that the proposed higher taxes in the PIB would make exploration of oil and gas uneconomical in the country. They contend that the bill will make Nigeria's *Production Sharing Contract* (*PSC*) regime among the harshest in the world. The IOCs consider the PIB as extremely punitive towards them in terms of new investments and this has somewhat stalled new investments. It is estimated that about $50billion planned investment especially in deepwater exploration is on hold and could be imperilled. Aside the uncertainty created by the hanging PIB, falling crude oil prices have also kept some investment decisions on hold. For instance, NNPC recently stated that there is a possibility that the declining crude oil prices may delay or probably cancel three deep-water projects in Nigeria.

The continued delay of the passage of the PIB is being further complicated by the recent discovery of commercially viable oil reserves in some African countries. Although these new discoveries do not come anywhere near the crude oil reserves in Nigeria, Angola, Egypt, Libya and Algeria, IOCs have been more willing to explore for reserves in other African countries due to cheaper and better exploration technology, convivial business environment, political and economic stability. Another major attraction of IOCs to the new African frontiers is the high success rate in drilling operations. Also, oil from these African frontiers especially West African oil is similar to Nigeria's crude which has low sulphur content and easy to refine. The "new kids on the block" from sub-Saharan Africa are not encumbered by OPEC quota and as such, IOCs are at liberty to sell whatever share of oil they are entitled to under their production sharing agreements with the host governments. These factors taken together incentivize IOCs to pursue business opportunities in these new African frontiers in the face of uncertainties in Nigeria over the Petroleum Industry Bill (PIB).

As the PIB debate rages, it is pertinent to note that the legislation is not all about higher taxes and royalties payable by IOCs, and instituting a Petroleum Host Communities Fund (PHC Fund). The bill also seeks to make some profound changes in the oil sector by restructuring and improving the management of Nigeria's oil resources. It provides for the dismantling of the state-owned oil behemoth – the Nigerian National Petroleum Corporation (NNPC) into nine commercially oriented and profit driven agencies that do not rely on government subsidies. The nine agencies will comprise two regulatory agencies, three funds, three commercial companies, and one technical and support bureau. The NNPC would be restructured in the mould of Saudi Arabia's Aramco, Malaysia's

http://pixgood.com/electrical-substation-hd.html

Petronas and Brazil's Petrobras with improved corporate governance. The PIB also provides for the delisting of NNPC from the Public Enterprises Privatisation and Commercialisation Act. It also requires the government to divest up to thirty percent and forty nine percent of the authorised shares of the National Oil Company and the National Gas Company respectively to the public in a transparent manner on the Nigerian Stock Exchange. The bill seeks to optimise domestic gas supplies, particularly for power generation and industrial development, and encourage domestic refining of crude oil.

Poor electricity supply has been variously identified as a major challenge inhibiting Nigeria's economic diversification as almost every business has to generate its own power at enormous costs...

Power Sector: The Great Hiatus

Poor electricity supply has been variously identified as a major challenge inhibiting Nigeria's economic diversification as almost every business has to generate its own power at enormous costs, further increasing the cost of doing business in Nigeria. The provision, availability and affordability of efficient power supply remains a sine qua non for economic growth, diversification, and prosperity. Reliable electricity is crucial for the industrialisation of modern economies. The poor performance of Nigeria's Small and Medium Enterprises has been blamed on epileptic power supply. According to the Manufacturers Association of Nigeria (MAN) and the National Association of Small Scale Industries (NASSI), an estimated N2billion is spent weekly on private power generation by their members. Private power generation account for about 30 percent of manufacturers' cost of production and this impact negatively on their profitability and competitiveness. Households also expend a significant proportion of their disposable income on private power generation as an estimated 80 percent of Nigerian households generate their

own electricity from alternative sources to augment irregular public power supply.

Taking cognizance of the power hiatus in the country, government has recently undertaken the most ambitious reform in the power sector to attract private sector investment in a bid to achieve increased access to electricity, improved efficiency, affordability, and reliability of power supply. The state-owed power behemoth – the Power Holding Company of Nigeria (PHCN) has been unbundled into eighteen (18) successor companies. The management, operations, and financing of the successor companies have subsequently been successfully transferred to the organised private sector. Government has also established an independent regulatory commission – the Nigerian Electricity Regulatory Commission (NERC), to provide balanced regulatory framework and protect investors and consumers. Also, the Nigerian Bulk Electricity Trading (NBET) was created to provide securitisation and be an effective and efficient catalyst for private sector investment in the power sector. Similarly, Manitoba Hydro International (MHI) of Canada was engaged as a management contractor to reorganise the Transmission Company of Nigeria (TCN) into technically, financially and commercially viable and market driven company. Government will therefore focus on policy formulation and long-term development of the power sector.

Cheeringly, the federal government and the Central Bank of Nigeria (CBN) are giving maximum support to the new owners of power infrastructure. For instance, the CBN in partnership with banks have pledged to provide facilities to assist in power project financing. Recently, through the gas intervention scheme, the CBN has settled outstanding debts totalling N36.9billion with promise to pay for all other rendered services onward. The Central Bank of Nigeria also recently availed N18.26billion as loan to five power firms (Ibadan Electricity Distribution Plc, Eko Electricity Distribution Plc, Jebba Hydroelectric Plc, Kainji Hydroelectric Plc and Shiroro Hydroelectric Plc). The loan, which attracts an interest rate of 10 per cent with a repayment period of 10 years, is part of the N213billion Nigerian Electricity Market Stabilisation Facility.

Barely two weeks after the first tranche of N18.26billion was availed to five power firms, the CBN disbursed N39.52billion to another set of 10 power distribution and generation companies to boost their operations. This brings the total intervention made under the Nigerian Electricity Market Stabilisation Facility to N57.78billion. The disbursements of the loan is sequel to the Memorandum of Understanding (MoU), between the CBN, participating Deposit Money Banks and the Nigerian Electricity Regulatory Commission to resolve liquidity challenges in the power sector. The MoU seeks to facilitate the channelling of funds to the power firms in order to de-risk the value chain in the electricity supply market. Foreign Direct Investments (FDI) are also expected to flow into the power sector and unlock the sector's value chain. It is believed that the success story of Nigeria's telecommunication sector liberalisation will be replicated in the power sector.

Agriculture for Food Self-Sufficiency & Employment Generation

Agriculture has been the mainstay of the Nigerian economy despite its decline especially since the oil boom of the 1970s that heralded the petrodollar era. Till date, a greater proportion of the population – about two-thirds of the total labour force of Nigeria, depend on the sector for their livelihood and the rural economy is propelled by agriculture. It is the main source of food for most of the population and is also the dominant economic activity in terms of employment and linkages with the other sectors of the economy, serving as a major source of raw material for the agro-allied industries and a potential source of foreign exchange earn-

ings. The sector has been a major contributor to the nation's GDP over the years – accounting for 24 percent of nominal GDP in 2013 (post GDP rebasing). With an area of about 924,000 square kilometres and topography ranging from the Sahel, Sudan and Guinea Savannah of the North to the Southern rain forests, Nigeria's agricultural potential are enormous. The country has a highly diversified agro-ecological condition with a total agricultural land of 79 million hectares, surface water of 267 billion cubic metres, underground water of 57.9 billion cubic metres, and a potential irrigable area of 3.14 million hectares. About 75 percent of Nigeria's land is arable, of which over 50 percent is not cultivated. Some 10 percent of the total land is covered with forest, including large stands of tropical trees including mahogany, walnut, and obeche – veritable sources of timber. Bountiful flora and fauna, constituting a rich source of biodiversity that could serve as a reservoir for the pharmaceutical industry and a sustainable source of genetic materials that can improve the nation's food production potential towards self-sufficiency. The country is also endowed with rich fishery resources and potential for large-scale fish farming.

These potential notwithstanding, Nigeria's food import bill is monstrous and mind boggling to say the least. Agriculture in Nigeria is still largely subsistent, characterised by smallholdings, traditional, and inefficient methods of cultivation. The country's food import bill as at end 2013 was N684.7billion ($4.35billion), down from a whooping N1.1trillion ($6.9 billion) in 2009, according to the Federal Ministry of Agriculture. As at 2009, annual food import accounted for 35 percent of the nation's total budget. The modest achievement of recent years nonetheless, food import bill remains a major drain on the nation's foreign exchange reserve. Although recent reforms in the agricultural sector has yielded some

modest results, there is still much to be done to transform agriculture from being subsistent to a mega business all through the agric value chain. Government's new approach in focusing on the youths to drive agriculture is encouraging and should be mainstreamed. The federal government recently launched the Youth Employment in Agriculture Programme (YEAP) and the Fund for Agricultural Finance in Nigeria (FAFIN). YEAP is targeted at 740,000 market-oriented young agricultural producers in rural areas while FAFIN is an agriculture-focused investment fund that provides tailored capital and technical assistance solutions to commercially-viable small and medium-sized enterprises (SMEs) and intermediaries across the agricultural sector. While the above are steps in the desired direction, programmes and policies for large farm holdings especially access to finance should complement these efforts.

Diversification as a National Exigency

Although the Nigerian economy has been growing moderately at an average of 6 percent in recent years, it has been argued that the growth has not been impactful and inclusive as expected especially in employment generation. The reason for this scenario is not farfetched. The Nigerian economy is dominated by the oil and

gas sector which accounts for less than 5 percent of total employment. The oil and gas sector is capital intensive, not labour intensive like the manufacturing sector which employs more people. The clarion call for the diversification of the Nigerian economy to broaden its export base for improved revenue, and conservation of depleting foreign reserves has somewhat become a cliché. In fact, virtually all economic reforms and strategic national plans from independence in 1960 till date have been conceived to achieve this singular objective. From the First National Development Plan through the Fourth National Development Plan, the Vision 2010, Vision 20:2020 and the *National Economic Empowerment and Development Strategy (*NEEDS), diversifying the economic base of Nigeria has been a major preoccupation of policy makers. The imperatives of a modernised and diversified Nigerian economy cannot therefore be overstated. Diversification has long been identified as the precondition for accelerated development of the economy as the non-oil sector has the potential to bolster the competitiveness of the Nigerian economy in the emerging global economic order.

http://www.channelstv.com/2014/12/16/nigeria-launches-youth-employment-in-agriculture-programme/

It has also been argued that diversification will maximally create and appropriate existing opportunities and potential inherent in the Nigerian economy as has become obvious from the rebased GDP statistics. The present mono-product export structure of the economy that is susceptible to the caprice of crude oil price volatility is not only precarious but also not sustainable. The slump in crude oil prices consequent on the discovery of shale oil, and the lull in demand should more than ever before serve as an impetus for urgent reforms to derive revenue from non-oil sources. It has therefore assumed a national economic exigency of sorts to rev up efforts to diversify the Nigerian economy and create a buffer in the event of a sudden crash in oil price to avert the dire consequences in the mould of the experiences of the early 1980s when there was glut in the international oil market. Some oil exporting countries have successfully leveraged on their other comparative advantages to diversify their economies from oil. For instance, the Emirate of Dubai (one of the United Arab Emirates) has evolved from being one the most oil-dependent economies to one of the least dependent. The Emirate of Dubai has reinvested its wealth to diversify its economy to become a thriving one in the Middle East and also a global business hub essentially through the free trade zone concept. There is no better time than now to chart a new course for Nigeria's long term sustainability outside the oil sector because the current reality suggests that the days of surging crude oil price and bumper revenue may well be over.

(* Sunday Enebeli-Uzor is a Research Economist, Zenith Economic Quarterly)

2015: If you thought 2014 was tough for investors... Think again...

- By Neil Hitchens

For the majority of investors who tried valiantly, or more likely, blindly, to keep their portfolios in line with their tracking index of choice, whether it was a strategy of following solely the MSCI World Index, or one where this investment benchmark was combined with either (or both) the MSCI Frontier and MSCI Emerging Market Indices, there was no overall happy ending for many.

Indeed, 2014 for investors turned out markedly worse than had been hoped or expected, especially when, even as late as the end of the Third Quarter, a quiet end to the investment year was predicted by many as the most likely and favourable prediction.

Yet, we find ourselves scratching our heads wondering if investment returns in the final 12 weeks of the year were merely a short-term correction or the start of something more sinister. Certainly, the investment outlook continues to confuse and contradict, yet given a few certainties for the coming year, overall returns have the opportunity to be solid rather than spectacular and money invested in equities should produce overall returns that will trump anything that may be possible from mainstream fixed income markets. However, as we have stated previously, it will not simply be a case of taking your particular index benchmark, shutting your eyes and investing indiscriminately. The investment world from the perspective of the first few days of 2015 looks like it is going to be more than usually volatile, but, oddly enough, the coming unpredictability is because of many already 'known knowns' – mainly geo-political – that are already in the diary and cannot be ignored or cancelled.

My formula for success is rise early, work late and strike oil - John Paul Getty (1892 - 1976)

However the coming year will also be one where equities will continue to be driven, in part, by the move in commodities – or rather, the move in one particular commodity – Oil. While I am very happy to report back to readers that 10 out of my 12 forecasts for 2014 eventually happened (the exception being the interest rate move in the UK which has merely been delayed, not cancelled, so we can chalk that one up as a score-draw), it was the sudden move in the price of crude oil in the Fourth Quarter of 2014 that came as a surprise in its severity, speed and shock. Simply, the market did not see it coming – not as a move per se, which we had felt by the latter part of 2014, could well see oil being softer going into 2015 on the back of increased US output via fracking - but it was the size of the move that has shocked everyone. To see crude halve in value in six months, while not totally unprecedented, is a new phenomenon when it happens from a starting price of US$ 110 a barrel.

The shock waves from this highly deflationary move continue to ripple their way through the global economy – in some cases for positive effect, for others in a not so beneficial manner. Certainly, for countries that rely on a higher oil price, this sharp fall in desperately desirable revenue is potentially destabilising and leads to increased local tensions, where they currently exist, or initiate new tensions that had only remained hidden because of the revenue cushion that had been in place.

Away from the oil conundrum, most of the geo-political problems from 2014 have continued into 2015. Such unending problems continue to vex and exasperate while also impacting to a greater or lesser extent on investors and investment psychology. At risk of repeating or continuing the bad news we highlighted in our previous item, it is readily apparent that the world remains a very dangerous place for investors and their money – one slip and you could find yourself nursing a very bad loss.

As we continue to reiterate and try and reinforce good investment practice for our friends, in uncertain times it is sometimes simpler to concentrate on the basics of investing – the "who, when, where and how" principles.

Firstly - who can you trust with your money – do you prefer the proportionately greater security and transparency of the US or the UK to invest as opposed to riskier areas such as Russia, Venezuela or Zimbabwe. Secondly - when should you consider investing – do you average in your investments if the investment is a larger one or do you

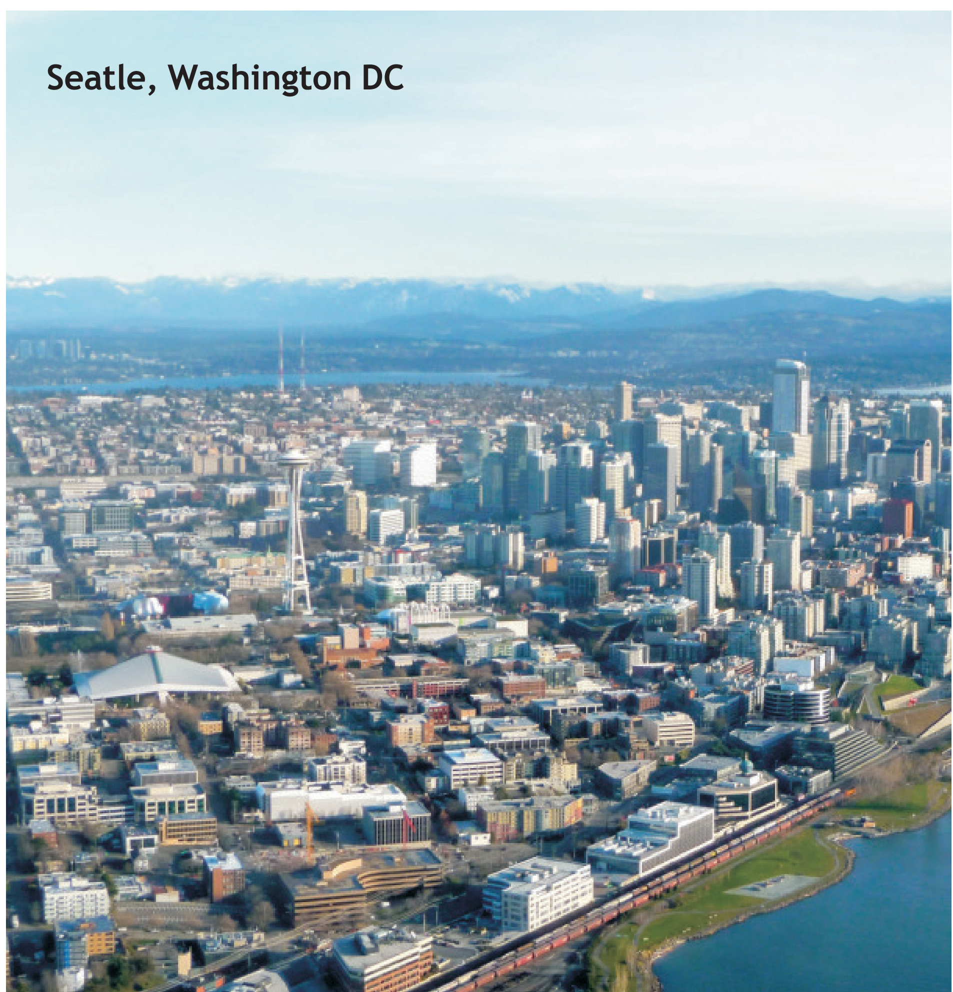
just make a single purchase and hope it all goes well. Thirdly – where to invest – do you buy equity exposure directly via the local markets or do you hope, when investing in significantly risker/volatile assets, that you can make your investment via a more regulated exchange in Europe, North America or Asia? Do you aim to have an index weighted investment which mirrors your chosen global index, or do you have an over or under weighted investments that match your own risk profile? Do you invest blindly, for instance, in Russia or the Ukraine because the weightings are part of your chosen tracker index, or do you use some intelligence and weigh up the risks of investment in a particular area and realise, for instance, that despite the MSCI World Index possibly having exposure to Russia, Ukraine or Zimbabwe, that these three areas might actually not be the markets with the greatest, or indeed, any potential returns in 2015 and that there are better value options elsewhere, such as, for example India, China or the US and Canada. Finally - how do you invest – do you invest directly though a local broker and make the decisions yourself or do you use a trusted and safer investment professional who has many years of global experience and can guide you with their expertise through the pitfalls that can easily trap the unwary.

Always have at the back of your mind how easily it will be to repatriate your money should you wish to sell your investments and move the money to an alternative investment area – it is unlikely that the US or the UK will ever impose currency controls again in our lifetime. Yet investing in Russia has recently proved to be a losing bet as external capital controls have ensured that not only is there a delay in the settlement processes and currency transmission conduits, but foreign exchange delays means getting your hands on your money is more difficult; the delays now being experienced by investors in getting money out of Russia has led to additional and unexpected currency losses due to factors beyond any individual's controls.

Allow me to be blunt – just because an investment 'is there' doesn't necessarily mean it *has* to be included as part of your portfolio – individuals have their own distinct risk parameters and a one size fits all investment policy does not work - ever!

To continue the slightly pessimistic note, we see from the overall global picture at the beginning of 2015 that the world is a mess and getting messier. Currently, any hope for global peace is in a shambles and we now see that both Russia and the USA are dusting off their blueprints for the possibility of fighting a global war – a war on terrorism that has all the hallmarks of turning far uglier than we could possibly have thought two years ago.

However, war is not just fought in hand to hand combat or via airstrikes against desert targets – we are also seeing an outbreak of economic warfare, the like of which has never been experienced in the recent modern era. We see governments waging wars with printed money to ward off the collapse of currencies, the collapse of nations, and the dismemberment of national unions to fight deflation, debts, and defaults to overcome unemployment, poverty, and popular rebellion. The recent, much



http://en.wikipedia.org/wiki/List_of_cities_in_Washington#mediaviewer/File:Seattle_Downtown_and_Elliott_Bay.jpg

anticipated and long overdue announcement by the European Central Bank (ECB) that it will now print $70 billion per month is just the latest example. Before the ECB move came the Bank of England, the Bank of Japan and the U.S. Federal Reserve – each being varyingly levels of success.

In 2014 we also saw the return of what can only be described as Cold War economics – we see battles being waged with economic sanctions, trade blockades, asset freezes, spying and cyber-attacks. Such warfare is not restricted to the old adversaries of the USA and Russia but it is now a global occurrence and has the possibility of destabilising governments and large corporations.

Terror wars also continue with an increasing level of aggression – we have in 2014 witnessed rampant

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bloodshed and unprecedented horrors on every Continent except Antarctica. At the same time, we've seen how the threat of terror enables governments to justify new kinds of foreign aggression and new levels of domestic repression.

Such short-term pessimism is justified, even if we can grasp the possibility that somehow there may eventually be concrete steps to resolving part of these issues in 2015. But for the moment for investors there remain very few certainties to juggle with and safe havens to invest in. It is a truth to be acknowledged that there is currently a three-way battle unfolding globally. In 2015, it will be more evident that the war is not simple East vs. West, Capitalism vs. Communism or Allies vs. Axis forces. What has thrown everything up in the air is the growing Jihadist threat. This is now not just restricted to 'only' the Middle East or 'only' sub-Saharan Africa. No, the threat is now one which encompasses additional areas as disparate as Western Europe, Russia and even China.

In Yemen, for example, the source of the recent Paris attacks, the entire country is coming unglued as Houthi rebels (Shia) have taken over the capital city Sana'a and the U.S.-backed government (Sunni) has just collapsed. The U.S. has lost one of its biggest allies in its war against the Al Qaeda Jihadists. So now it's open season for Al Qaeda on the Arabian Peninsula to launch bloody attacks against all of the above.

In Iraq and Syria, we continue to see the never-ending three-way war among Shia forces, which control both central governments, Sunni forces, mostly aligned with anti-government forces and ISIS, which is winning against them all. In fact, ISIS has not only conquered territories larger than the UK, but is also holding firmly to those gains despite four months of massive allied bombings.

Shifting to Europe, in Ukraine, the continuing conflict has now splintered into one where there are now pro-Western extremists, pro-Russian rebels and a series of government administrations, which have forever been unable to steer a stable middle ground between the two. Just as we go to press the problems have all significantly escalated as the Russian and pro-Russian forces sent Ukrainian troops fleeing in panic and took full control of the critical Donetsk airport and now appear to be heading for an even more acute battle for the strategically important port of Maruipol, which, were it to fall could well mean that the Sea of Azov (North East of the Crimean peninsula that was recently absorbed into the Russian Federation) then becomes a private Russian Navy enclave. In other words, twenty years after the collapse of the Soviet Union, the threats we highlighted in our previous com-

mentary are becoming more real – President Putin is most definitely trying to glue back his shattered empire.

This is not good news.

In France, Germany, and most European countries with sizable recent immigration, we see a three-way conflict among anti-immigration forces marching in cities all across the continent, anti-government rebellions putting still more pressure on central bankers to abandon austerity or print more money and national governments that are incapable of agreeing on cohesive policies to address either. The recent Greek victory by the Leftist Syriza party again does not augur well for the economic stability of South Eastern Europe even if the Grexit (Greek Exit) from the Euro is only a footnote at present.

How will it all end? Badly.....were things to continue unabated and unchecked.

But...fortunately the global economy is unlikely to unravel in 2015— nor could this happen in the near future.

Yes, we do have some deflation.

But the deflation is limited mostly to oil and related commodities. It's already saving companies and consumers a lot of money. It historically drives stocks higher, especially in the technology and consumer sectors and on top of all that, it's giving the Federal Reserve more excuses to delay its long-feared rate hikes.

But all this is creating a huge opportunity right now and raising serious questions about likelihood of dangers down the road.

So brace yourself. What you've seen so far is just the beginning.

In short the watch word for 2015 has to be one of safety first, for the moment.

Oil - Are we there yet, or is there more pain to come?

Rather than comment first on the prospects for global equity markets, the most pressing problem for many readers is the oil sector: what happened and what might happen in 2015.

The oil price has fallen by more than 50% since June 2014, when it was $115 a barrel. It is now consistently below $50 and has been as low as $47. The failure by OPEC (Organisation of Petroleum Exporting Countries), which controls nearly 40% of the world market, on production curbs, sent what was an already

http://www.canwestpropane.com/sectors-we-service/oil-gas

weak commodity, to new lows. So how did we reach this new recent low, what caused it and what is likely to happen?

This plunge is partly due to the sluggish world economy, which is consuming less oil than markets had anticipated, and partly to OPEC itself, which has produced more than markets expected. As we correctly noted previously the newest factor in the oil price equation has been from what was, certainly a few years ago, an unexpected source – the oilmen of North Dakota and Texas. Over the past four years the boom in extracting oil from shale formations previously considered unviable has been unprecedented. The sheer number of new wells drilled, some 20,000 since 2010, is more than ten times Saudi Arabia's. This has boosted America's oil production by a third, to nearly 9m barrels a day which is just 1 million barrels short of Saudi Arabia's output. The contest between the shale men and the sheikhs has meant that oil shortages are now oil surpluses.

Low demand can be pinned on the continuing inability of Europe to extricate itself from an almost self-induced recession, along with the lower than expected, but still worthy GDP growth rates of over 7% from China. However, problems within the OPEC cartel also do not seem to have had much effect at all on the price, which in the past would have been the case. The turmoil in Iraq and Libya—two big oil producers with nearly 4m barrels a day combined—has not really affected their output.

The market remains more sanguine about the risks in these countries, but oil output here has not ceased nor is likely to cease completely, nor is it likely to, especially if government forces in both countries manage (as is possible in the longer term) to regain majority control of production. While America has become one of the world's largest oil producers, it does not export crude oil, but conversely imports much less, creating a lot of spare supply. Finally, the Saudis and their Gulf allies have decided not to sacrifice their own market share to restore the price. They could curb production sharply, but the main benefits would go to countries they detest such as Iran and Russia. Saudi Arabia can tolerate lower oil prices quite easily. It has $900 billion in reserves. Its own oil costs very little (around $5-$6 per barrel) to get out of the ground.

There will, of course, be losers.

Oil-producing countries whose budgets depend on high prices are in particular trouble.

Russia is one of the world's largest oil producers, and its recent dramatic interest rate hike to 17% in support of its troubled Rouble underscores how heavily its economy depends on energy revenues, with oil and gas accounting for 70% of export income. It has been calculated that Russia loses about $2bn in revenue for every dollar fall in the oil price. The World Bank has recently warned that Russia's economy would shrink by at least 0.7% in 2015 if oil prices do not recover. Despite this, Russia has confirmed it will not cut production to shore up oil prices mainly because it, like Saudi Arabia, does not want to lose market share.

Falling oil prices, coupled with western sanctions over Russia's support for separatists in eastern Ukraine have hit the country hard and even the government has cut its growth forecast for 2015, predicting that the economy will sink into a mild recession. Given the pressures facing Moscow now, some economists expect further measures to shore up the currency and this is likely to be seen in a combination of spending cuts as well as possible introduction of fierce capital controls – which would hit individuals hard.

Were there to be further interest rate rises, additional problems could ensue as high rates can choke economic growth by making it harder for businesses to borrow and spend. Short-term, Russia is in crisis, but the longer term destabilising effect of this sharp reduction in oil revenues could lead to internal unrest, which might lead to a further overspill of problems in the Ukraine as Russia could be tempted to deflect public criticism with military action.

While Russia may have some large problems, a country like Venezuela has been dealt an almost lethal blow. Venezuela is one of the world's largest oil exporters, but thanks to economic mismanagement it was already finding it difficult to pay its way even before the oil price started falling. Inflation is running at about 60% and the economy is teetering on the brink of a deep and serious recession. The need for spending cuts is clear, but the government faces difficult choices.

The country already has some of the world's cheapest petrol prices and fuel subsidies cost the government about $12.5bn a year - but President Maduro has ruled out subsidy cuts and higher petrol prices. Such caution is understandable as a petrol price rise in 1989 saw widespread riots that left hundreds dead. Venezuela looks ever closer to defaulting on its debt.

While I do not comment on the state of affairs in Nigeria, it must be noted that because of the sharp drop in oil, Nigeria has been forced to raise interest rates and devalue the Naira.

The spectre of defaults and the speed and scale of the price plunge have unnerved financial markets.

But.... - and there is always a 'but' in such a gloomy short-term scenario - cheaper oil should act like a shot of adrenalin to global growth.

Every US$ 10 fall in the price of oil shifts some $325 billion from producers to consumers. So with a cumulative US$60 fall in the oil price we are looking at a near US$ 2 trillion stimulus to the global economy. The typical American motorist, who spent $3,000 in 2013 at the pumps, will now be at least $800 a year better off—equivalent to a 2% pay rise.

Big importing countries such as the Euro area, India, Japan and Turkey are enjoying especially big bonanzas. Since this money is likely to be spent by consumers rather than stashed in a sovereign-wealth fund, global GDP should rise. The falling oil price will reduce already-low inflation still further, and so may encourage central bankers towards looser monetary policy. The Federal Reserve will put off raising interest rates for longer; the European Central Bank will act more boldly to ward off deflation by buying sovereign bonds.

The falling oil price will reduce already-low inflation still further, and so may encourage central bankers towards looser monetary policy.

http://fineartamerica.com/featured/the-us-federal-reserve-board-building-susan-candelario.html

But the overall economic effect of cheaper oil is clearly positive.

Just how positive will depend on how long the price stays low and the signs are that, for the moment, oil will stay around the US$ 50 a barrel level for the next couple of quarters at the very least while the continuing wrangle lasts between OPEC and the (mainly US) shale-drillers. Several members of OPEC have expressed a desire to cut output, in the hope of pushing the price back up again. Saudi Arabia though has a longer memory about the experience of the 1970s, when a big leap in the oil price prompted huge investments in new fields, leading to a decade-long glut. Instead, the Saudis are happy, for the moment, to be trying a different tactic to let the price fall which in turn will put high-cost producers out of business leading to a cut in supply, causing prices to rise.

There are signs that such a move is already beginning to occur. The share prices of shale producing companies have been very weak over the past quarter. Many of them are up to their derricks in debt and even before the oil price started falling, most were investing more in new wells than they were making from their existing ones. As revenue collapses they will find themselves over-stretched and a slew of bankruptcies and/or capital reorganisations (some in the form of mergers) is likely. This is likely to take the shine off the attractiveness of the sector with investors. As such, this has to mean that we should flag the sector as an 'Avoid' for the moment.

The remaining companies may find traditional capital raising opportunities closed for some time leading to a reduction in expenditure down to match the levels of cash they generate from selling oil. Since the life span of many shale-oil wells are very short (output can fall by 60-70% in the first year), any slowdown in investment will quickly translate into falling production.

This shake-out will be painful but necessary. In the long run though, the future of the US shale industry seems positive. Fracking is a relatively young technology and in many respects still has to see the full potential that can be achieve with the inevitable and necessary improvements in efficiency. It has been calculated that the cost of a typical project has fallen from $70 per barrel produced to under $57 since 2013 as oilmen have learned how to drill wells faster and to extract more oil from each one. Adversity will make shale stronger as it stimulates innovation, cuts drilling costs through standardisation and introduces new fracking techniques that increase output.

The surviving companies will have considerably more shale to exploit than is available at present. Drilling is just beginning in the Niobrara formation in Colorado, for example, and the Mississippian Line along the border between Oklahoma and Kansas. Nor need shale oil be an exclusively American phenomenon: there is similar shale bearing geology all around the world, from China to the Czech Republic.

Most important of all, investments in shale oil come in conveniently small increments.

The big conventional oilfields that have not yet been tapped tend to be in inaccessible spots, deep below the ocean, high in the Arctic, or both. America's Exxon Mobil and Russia's Rosneft recently spent two months and $700m drilling a single well in the Kara Sea, north of Siberia. Although they found oil, developing it will take years and cost billions.

By contrast, a shale-oil well can be drilled in a week or less, at a cost of $1.5m. With access so easy the only question is how many wells to drill in a particular area. The second demand increases new wells can be online in a matter of days to meet this new need. It really is that quick and simple, so long as the political will is there to encourage such exploration.

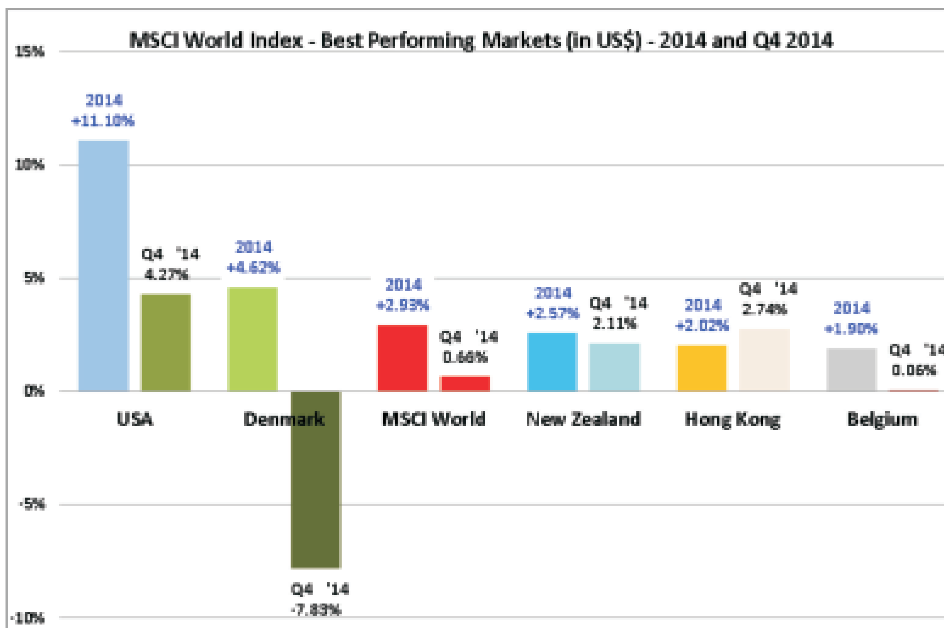
So...the economics of oil have changed.

The market will still be subject to political shocks. A prolonged or widespread war in the Middle East or the overdue implosion of Vladimir Putin's regime would send the price soaring, but probably only to under US$100 initially. Certainly for the first half of 2015 the price of oil price should be less vulnerable to exogenous shocks or manipulation.

Even if the extra oil that the United States now pumps out is a small proportion of the 90 million barrels a day the world consumes, America's shale is now a genuine rival to Saudi Arabia as the world's marginal producer. That should reduce the volatility not just of the oil price

but also of the world economy.

Oil and finance have proved themselves the only two industries able to seriously upset the global economy and have the potential to send it quickly into a recession. At least one of them should in future be a bit more stable and as such we expect the oil price to stabilise initially around US$ 50 a barrel and then trade, certainly for the near term between there and US$60, so long as there are no major economic or political shocks.



Source: MSCI Barra

Equities - US and UK still leading the way...Europe stalling.

2014 was for many investors a case of 'Where did it go so wrong?'

Returns for the three MSCI Indices were at best tepid and at worst disappointing: for the component parts the returns did fluctuate wildly, as they are prone to do.

However, there was, for those that had taken guidance from our previous contributions, the possibility was there not necessarily to have profited immensely, but certainly to have side-stepped some of the more obvious areas of contention and investment disappointment.

The raw data for both the full year as well as the final quarter of 2014 gives returns as follows:

Index Return	2014	4th Quarter 2014
MSCI World(Developed)	+2.93%	+0.66%
MSCI Emerging	-4.63%	-4.88%
MSCI Frontier	+2.90%	-12.66%

For Developed Markets the story continues to be one where the US leads the way and everyone else follows in its slipstream.

As we correctly identified, the best performing Developed Markets in 2014 were the Dow Jones and the S&P 500, which during the latter part of the year managed to clock up new record levels. The Dow Jones had a new intra-day high of 18,103.45 on December 26th and closed 2014 at 17,823.07. The S&P 500 also rallied into year end with a new intraday high on December 29th of 2,093.55 and closed the year at 2,058.90. Our forecasts for the indices to reach 2,000 and 18,000 in 2014 were just about spot on.

The year-end returns for the MSCI World Index of +2.93% were mainly due to the large component weighting of the US as the second and third best performing indices, Denmark and New Zealand with total returns of substantially less than half that of the USA, showed the disparate nature of investing in a booming economy as opposed to markets only just recovering from recession.

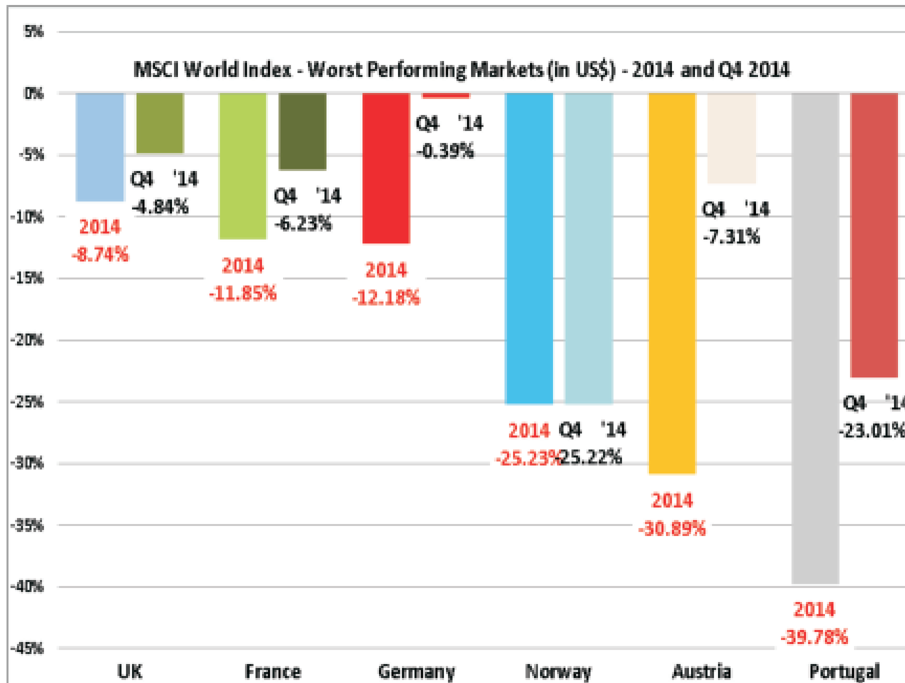
The US continues to show the rest of the world a clean pair of heels for equity investors as the Fed has managed to not only successfully remove the artificial stimulus of Quantitative Easing, but talk has already turned to that of the timing and extent of the necessary interest rate rises, especially given the continuing improvements in the labour markets in both absolute numbers of unemployed, but also the participation rate of labour as well as wage growth – all of which augurs well for 2015 and beyond.

In the US, as goes the stock market, so goes the US economy – usually. Stock market and equity enthusiasm will trickle through to the economy – an optimistic

driver if there ever was one. High stock prices do have a positive effect on consumer spending as the investment classes will spend their capital gains, even if they are on paper. However, we do feel that the near term strength of the US economy will be down to consumer spending and as such the retail sector is looking especially promising for the first half of 2015. Recent results from Apple reinforce this view.

However, were the stock market to falter and consumer confidence were to start sliding, it is highly possible that the Fed could intervene with some form of short term additional quantitative easing. But, for the moment at least there is a certain amount of post QE momentum driving the economy.

Away from the obvious and continuing success for the US, we find the rest of the major indices all managed to disappoint extremely. A lot of the extreme negative returns seen in the final quarter of 2015 came from the sharp fall in the oil price. Certainly the markets in Austria and Norway suffered from the relative preponderance of oil companies in the main indices, while the worst performing index, Portugal, is still wrestling with the fallout from the on-going fiscal squeeze being imposed by the European Central Bank (ECB).



Source: MSCI Barra

As we noted in our previous commentary, the likelihood of disappointment in forlorn or desperate hopes of a year-end rally in Europe were spot on. Such pessimism was in this case well founded and the underlying problems for Continental Europe remain and will play a major role in the fortunes for equity investors in 2015.

Certainly, the growing problems around the Euro are of major concern to most investors as despite the recent and much delayed announcement from the ECB about activating a Quantitative Easing programme, the picture remains one where the problems are now no longer merely cyclical but also structural.

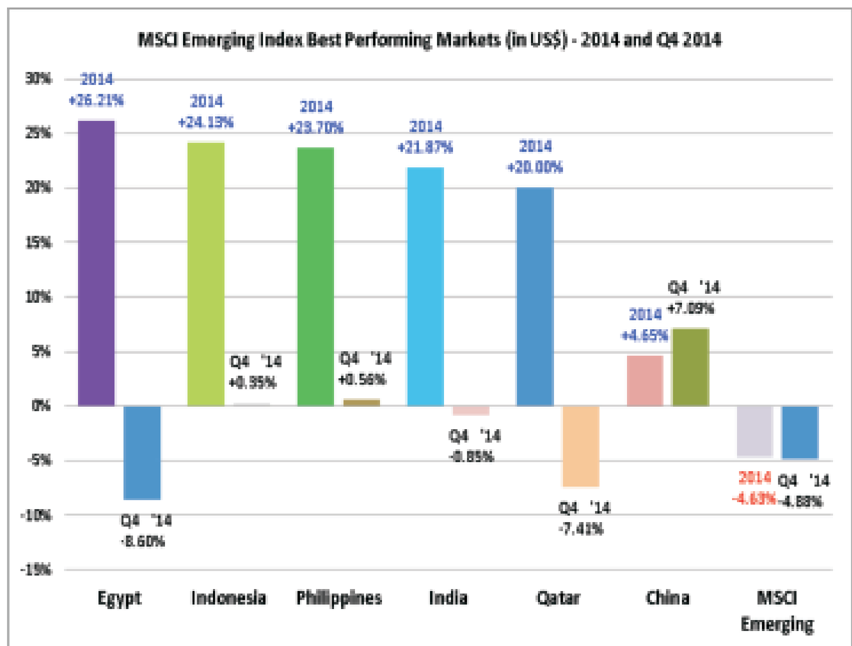
A growing sense that Euro Zone deflation is here to stay can only weigh on equity prospects for the entire Euro Zone community as consumers will start to delay big ticket purchases for an extended period of time because they know that by waiting a few months it might be possible to buy the fridge, car or whatever at a then lower price than todays. Such deflationary expectations will also weigh heavily on the fixed income markets where governments usually rely on a modicum of gentle inflation to gradually ease their overall debt burden.

Yet the fixed income market is also showing signs of some slightly warped thinking at the shorter end of the yield curve. When you see German 2 Year Bund rates of -0.16%, French, Dutch and Belgian 2 years at -0.09% (in other words YOU are paying the government to look after your money for 24 months); you know 'something is up'. A lot of this has to do with future inflation, or rather, deflationary prospects. But there is also the growing suspicion that the Euro in two years' time may be a slightly different entity to what we see at the beginning of 2015. There is an outside, but growing chance, that the Euro may well have to survive without the benign influence of Greece as a member and that such an expulsion or withdrawal could well lead to other members such as Italy,

Spain and Portugal reassessing their membership of the fixed currency.

For the moment, until the Greek question show some signs of a resolution, European equities remain fairly poor value and certainly a reassessment at the end of the first quarter is probably the most sensible thing to consider – certainly there is currently no overwhelming case for new investments in anything other than stock specific issues.

Away from the car crash economics of the Euro Zone the UK economy is, somehow, managing to lead the way in the global growth stakes – performing even better than the US. Despite an almost flat 2014 for equity markets the longer term prospects for the economy look reasonably positive for 2015, even if the economy grows slightly less than forecast at around 2.0% – 2.5% despite the benefits of sharply lower energy prices filtering through from the end of the First Quarter. Certainly, for the first few months markets are likely to remain round the 6,800 level on the FTSE and there may be a final push to break the old all-time high of 6,930.2 seen on 31st December 1999. To take over 15 years to reach new highs is not totally without precedent as the Japanese can testify when the likelihood of their all-time high of 29th December 1989, 38,957.44, being broken any time in the next five years looks so remote as the index closed 2014 at 17,450.77 – a level half of that of the high..



Source: MSCI Barra

But....2015 is an election year in the UK and at present the chances of any single party gaining an overall majority are simply not being factored in. Nor, we feel, should they, as the fragmentation of the general vote is gaining pace with the likelihood of some sort of rainbow coalition being the most likely result with the distinct possibility of a Labour/Scottish Nationalist cabinet. The Liberal Democrats who currently are in Coalition with the Conservatives are likely to be decimated from their current 56 seats to possibly as low as 25, possibly fewer.

The closer we get to the pre-ordained May 7th polling date the more jittery UK markets are likely to become, even if we have breached the 7,000 level in the interim. There are precedents for such a possible stalemate some 40 years ago when 1974 was the year of two elections. The first one in February, on the back on an oil crisis, resulted in an initial minority administration which was followed by the inevitable fallout, recriminations and then government collapse with a new election in October that year with a Labour majority.

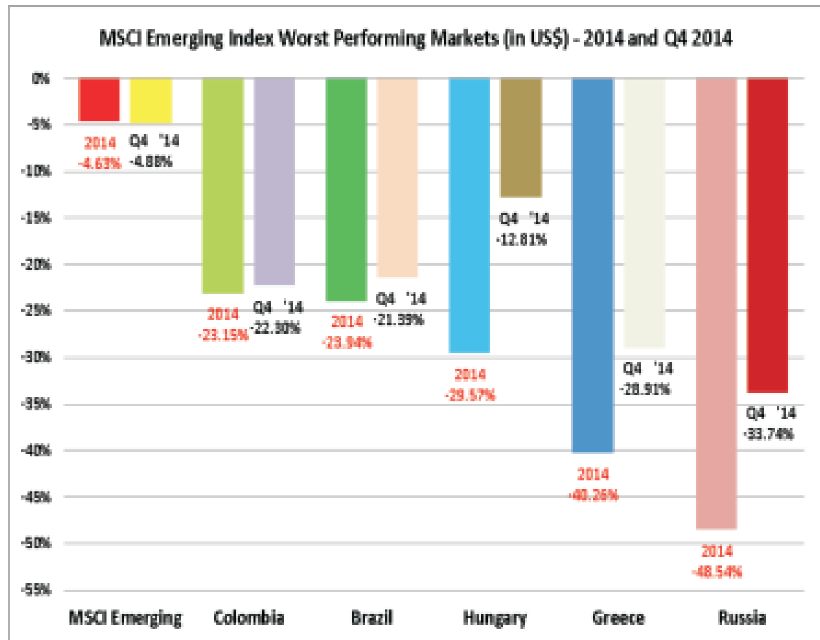
Markets hate such uncertainty and for the moment, despite the current positive underlying fundamentals, the risk of a market run grows.

While the possibility of a 6.8% move from the year end closing price of 6,566.09 to that 7,000 level cannot be ruled out it should be the possibility of a 10% -15% collapse from this level to below 6,000 that should frighten investors most. Even after the results, markets would remain jittery and as such we would suggest that certainly until any definite result that no new positions in the UK be initiated in either stocks or bonds.

So, for the moment, certainly until the end of the first quarter, we must maintain our earlier cautious stance on all developed equity markets except for the

US. It is not that there is any compelling reason to invest in any particular sector, but more that the shorter term volatility that will most probably erupt sporadically over the next three months means that only the luckiest investor will be likely to make any significant money at all.

However, a marginally more positive equity story can be shown in the slightly riskier equity markets within the Emerging Markets Index. Here, as can be expected, was a slightly more diverse series of returns for 2014, however, as we have seen globally, all returns were, almost without exception, negatively impacted in the final quarter of the year as the oil sector, upon which many of the second line indices depend, collapsed.



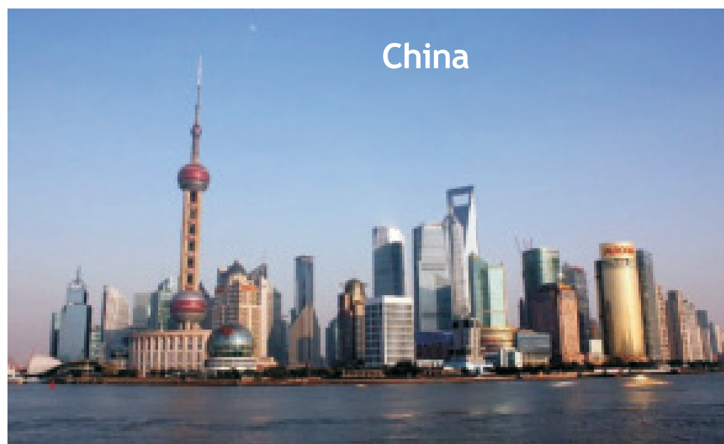
Source: MSCI Barra

Yet, as we noted in previous articles the equity markets in China and India continue to show the way forward. India continues to benefit from the positive glow that surrounds the new administration and the overall sensible yet slightly radical agenda. The long-term outlook for the Indian equities remains positive due to strong fundamentals, though markets may face some volatility in the short term. However, given the improved fundamentals of the country, India should deliver good reforms.

After a good run in 2014, when the Sensex index closed at 27,499.42 markets are likely initially to consolidate at the year-end closing levels for the first few weeks of the year, but the long-term outlook is positive. For there to be a 10% - 15% return for 2015 is not an outrageous possibility given the growing positive and less introspective looking fundamentals for the Indian economy as a whole.

We also note with interest that China still seems determined to keep to a growth rate of 7.0% - 7.5% for the next few years at least. Quite why the markets fret about whether this growth rate sometimes dips more towards 7.0% than around 7.5% is a mystery.

If you are growing at 7.0% a year the annual returns rebased to that first year by year Five means that the reported 7% growth rate then is the equivalent to +10.51% from the first year. Going forward by further increments of 7% a year we then see by the 10th year the implied '7%' = +12.87%: by year 15, = +18.05% and by year 20, = +25.32%. In other words the economies of scale kick in very fast. After 30 years that annual 7% equivalents to +49.8% - something that many people forget.

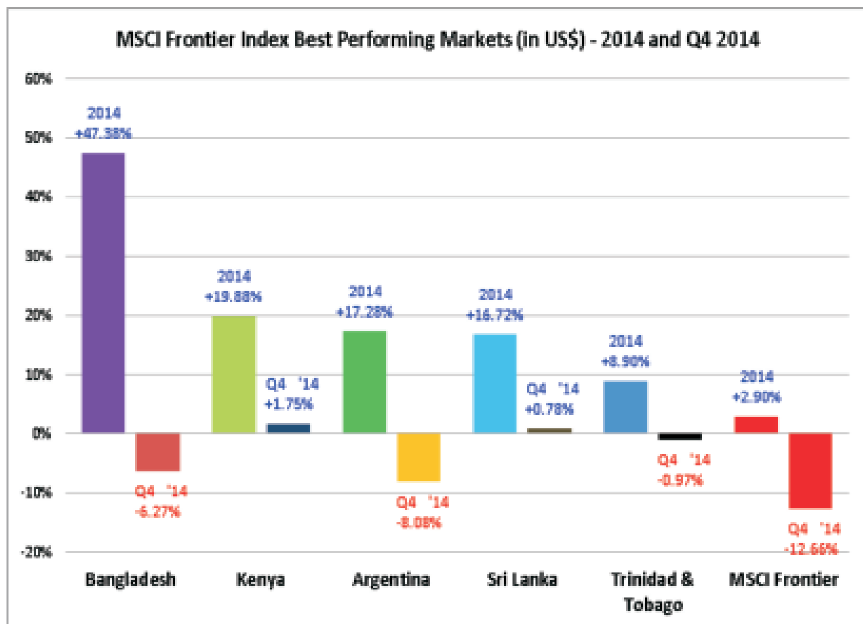


http://www.china-family-adventure.com/shanghai-skyline.html#.VNNt-53F-hM

Chinese economic growth will continue to moderate but supportive government policies should limit the downside risks. Real interest rates are high and with

little inflationary pressure and the recent fall in the oil price, there is room for further monetary easing and the stable macro environment enables the implementation of further reform measures, though actual results will materialize only over the longer term.

During the past five years Chinese equities have generally been an asset class that investors have loved to hate. Yet we consider that government policy will provide support to stabilize economic growth, which when combined with the very cheap valuations of many stocks will extend the current rally in markets.



Source: MSCI Barra

Have the economic fundamentals changed? The short answer is 'no'. China is consolidating during this period of qualified decelerating growth but is also managing to deleverage as well as the economy moves away from the old investment-led growth model. So long as the government can ensure continuing social stability, then the programme of reforms will continue to result benefits that will only materialize over the next 10-20 years. That said, the recent rally can certainly be justified by current lowly valuations.

There will be some profit pressure on companies during this deceleration, particularly the cyclical and macro-sensitive industries such as materials, traditional energy and banking. In contrast, however, we believe there are good reasons to be more optimistic about the potential for sustainable growth in sectors such as Retail, where lower inflation combined with growing wages results in more disposable income for the average worker, and Internet and E-Commerce, where, for instance we saw a record US$ 9.3 billion one day sales record from the now quoted Chinese e-commerce company Alibaba (Epic Code: BABA: US) which reaffirms the changing consumption pattern of Chinese consumers.

As such, we believe that a prudent, slightly index overweight positions in both these areas would be reasonable, however, excessive optimism certainly for the first quarter should be tempered in the light of oncoming geo-political events that may cause sudden swings in investor optimism.

The flip side of good on-going investor news in some of the larger Emerging Index stock markets is dire and continued bad news in others. As if to almost spite any brave inves-

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tors willing take a gamble, for at the moment this is all it can be, given the dearth of any positive fundamentals in either of these two markets, we find the two worst performing Emerging Markets for 2014 to be our 'old friends' Greece, -40.26% and Russia, -48.54%.

Russia has been skewered by the twin problems of a collapsing energy market from which it derives so much of its foreign revenue and the growing forcefulness of international sanctions over its continuing belligerency (whether actual or by proxy is a moot point) in the Ukrainian civil war. Added to these problems has been the consequential collapse in the Rouble on the world currency markets which moved from a mid-year high of 33.50 to the US$ to end the year at just under 60 (a fall of 79%), having at one stage hit 79.50 (a 137% devaluation). This was despite interest rates being raised sky high and currency controls per se being both introduced by the Russian authorities as well as reciprocal sanctions being imposed by most of the rest of the world to restrict the ability of capital to be withdrawn from Russia.

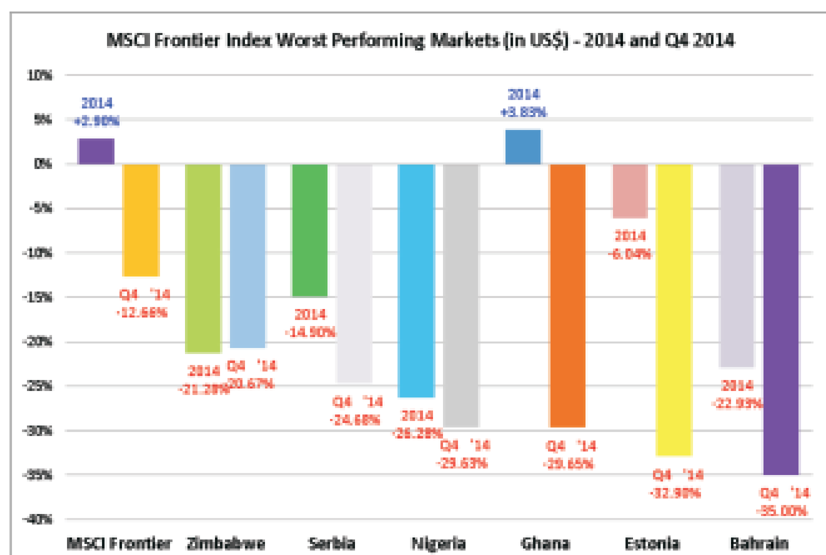
To add insult to injury, S&P also then cut the rating of Russian sovereign debt to BB+ which puts it at the same level as Bulgaria and Indonesia – not quite absolute junk status but enough to make raising money from investors harder.

In consequence, the Russian economy has been in free-fall and even the more optimistic forecasts for a recession of 'only 1% - 3% in 2015' already look somewhat desperate. Be in no doubt whatsoever, as we have warned in the past two quarters, investing in Russia at the moment is dangerous, chancy and downright irresponsible at the moment. The chances of civil unrest within the next 12 months are increasingly possible – it may be that even as soon as the Russian celebration of the 70th anniversary of the end of World War II, Victory Day, due on May 9th could act as a trigger for some 'unauthorised' protests in Red Square. Certainly, the whole of the Western part of Russia is at an elevated level of security due to the concurrent threat from Islamic militants as well as the on-going issues in Ukraine.

Any protests would be suppressed mercilessly, initially at least, by President Putin, but the harm could already have been done. A Kleptocracy (as the regime is described by some more militant observers) such as this could be shaken to the core by sustained and violent protests leading in turn to civil disobedience and culminating in a violent change of government, possibly from elements of the old Red Army.

Given the potential risks internally in Russia, to say that currently this is **NOT** a country to invest in is probably the understatement of the year. Even were you able to invest at a fair price, the probability of currency controls making any capital withdrawal impossible grow daily. Even then, with just a scintilla of the possible scenario outlined above unfolding the chances of the Rouble imploding from 60-odd to 120/240 or higher are significant factors to weigh. Yes, there will be an opportune moment to invest in this particular market but in all honesty it probably won't be this year. For the moment, this is not only an **AVOID** but a **DO NOT TOUCH.** If you are foolish enough to invest you could, possibly, get lucky, but the odds are that you will end up losing all your money.

Almost as if to spite us for a bad choice area to invest in, the second worst Emerging market in 2014 was Greece. "Quelle Surprise", as they may say....or inGreek **ôé Ýêðëçîç**



Source: MSCI Barra

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(pronounced ti ékpli1˜xi1˜).

It was increasingly obvious for the past couple of months that the Greek vote at the beginning of January would produce an anti-austerity winner in the far left Syriza party and already within a few days of winning, the new Prime Minister, Alexis Tsipras, has managed to completely spook the Greek markets. So...on top of a 40%+ loss last year there are already losses of over 12% in the Athens ASE equity market already for 2015 as we go to press along with bond yields jumping back to the "good old days" level of 2012 of 13½% for the domestic 5 year issues. If you were stupid (in this case this is precisely the correct phrase to use) to hold Greek bank shares you will already have seen nearly 50% wiped off your holdings in the past 3 weeks. We did warn you!

The agenda here is simple – Greece will ask for debt forgiveness from the ECB. Germany will initially protest and refuse any form of clemency. The Greeks will then threaten to leave the Euro and the Germans may, just may, eventually consider some form of debt extension or conversion of outstanding debts in part in the swapping of fixed coupon paper to something, say, like perpetual zero coupon bonds – essentially a promise to pay so far into the future as to be almost worthless. The problem here is that within the Euro Zone, were Syriza were to win its negotiations with the rest of the Eurozone, other anti-austerity parties in other countries would look more credible to voters. The victory of protectionist Marine le Pen in France's presidential election, not due until April 2017, would be an interesting test of markets' sangfroid.

However, were Syriza were to fail in talks with Brussels and Berlin, and the final exit of Greece, the much vaunted Grexit, from the Euro were to occur, investors might well pull their savings from any Eurozone country where nationalists are in the ascendant. Yet, and yet, investors throughout the Eurozone are not quite in a state of wholesale frenzied panic. Why? One slightly implausible explanation is that investors believe the Eurozone would actually be stronger without Greece, so long as no other big country followed it out the door. More likely, though, is that they believe reason will prevail, and Berlin will sanction a write-off of Greece's excessive debts.... eventually and without actually admitting defeat. After all, modern Germany would not be here without some form of debt forgiveness.

In 1953, an agreement was reached in London to cancel half of Germany's debt burden. That cancellation, and the way it was done, was vital in helping Europe recover from the war as Germany emerged from the Second World War still owing debt that originated with the First World War reparations imposed following the Versailles Treaty 1919. Many argued that these unpayable debts and the economic policies they entailed led to the rise of the Nazis and the Second World War.

By 1953, Germany also had new

debts raised to help with necessary reconstruction and, surprise, surprise, Germany's creditors included Greece and Spain, Pakistan and Egypt, as well as the US, UK and France. Even though the debt levels were below those now seen today in Greece, there was serious concern that debt payments would gobble up precious foreign currency reserves. Countries such as Greece willingly took part in a deal to help create a stable and prosperous Western Europe, despite the war crimes that German occupiers had inflicted just a few years before.

Debt was cancelled swiftly before a crisis could unfold and at a 50% forgiveness rate 'pari passu' to all debt holders. Following the London deal, West Germany experienced an "economic miracle" and has since become the economic giant of mainland Europe.

In Europe today, debt is having a debilitating effect on debtor countries and a solution needs to be found, not only for Greece but for all the very heavily indebted countries within the Eurozone. It is perhaps too much to suggest that Germany may well have to look the other way, but at current levels, this crisis will drag on for decades to come. After all, it was only 30 years ago that Latin American debt was similarly reduced or eliminated completely and we do also recently have other examples from Africa where the HIPC (Heavily Indebted Poor Countries) initiative has also given debt relief to many stricken countries.

Away from the Emerging markets, we also find some welcome relief in the Frontier Index member indices. Here investment is one where you have to deal with local illiquidity and the possibility of capital controls, yet the top countries, on the whole, have performed in a singularly positive manner, even though their indices are sometimes a little difficult to enter.

Certainly the double digit performances from Bangladesh and Sri Lanka can be seen as part of the positive effects of having a newly invigorated Indian economy, with the subsequent benefits in cross border trade with its closest neighbours and the ensuing follow-on economic optimism. Pakistan would have had a better performance than the eventual near flat lining for the year, but its domestic problems outweigh the positive benefits from a resurgent India, maybe 2015 might be kinder.

Argentina, though, is performing a little like Venezuela did in 2013. Despite the actual default of the bond market in mid-2014 and Argentina's economy contracting 0.8% annualised in the third quarter of last year following flat growth in Q2, the stock market ended in positive territory. The contraction was mainly due to a sharp fall in private consumption, which hit a record low in Q3. Exports continued to decline, although at a slower pace than in Q2, while investment posted negative growth for the third consecutive quarter. Recent data suggest that the economy remains weak.

However, with capital controls in place and little prospect of a solution to the on-going bond holder's legal challenges, capital only has one place to go and that is into the domestic market. Again, we should warn anyone considering a punt on the Buenos Aires exchange – you may well be able to get your money in, but if you can eventually get it out what could the exchange rate be and how long would it take to hit your bank account.

The worst performing markets in 2014 did throw up some surprises and yet a couple of regulars made yet

another appearance in the bottom six. Nigeria and Bahrain suffered immeasurably from the drop in oil prices and losses were exaggerated by the heavy index weighting of oil industry stocks. We will briefly note that Ghana, suffering from a weakening currency and the mixed upsets from problems close to its borders on both a geo-political and geo-biological nature did manage to squeeze out a +3.83% gain in the final quarter. Perhaps the tide has finally turned in Accra.

Estonia's problems are all too easy to educe as it is a near neighbour of Russia and is dependent on trade to prop up its economy – take away the trade to the East and everything starts to unfold, as we are also seeing in Eastern Finland where shops that did the vast majority of their trade cross border with Russia are closing at an unprecedented rate as this business has almost disappeared overnight.

So, do we feel confident about the investment prospects 2015 or do we not?

Probably this is a question to revisit at the end of the first quarter when we will have a better idea about the Greek question, for those concerned mainly with the Euro Zone and will also start having some hard evidence about the Russian backed incursive forces in Ukraine and whether they succeed in capturing more territory, especially the port facilities at Maruipol.

In the Middle East, while there are encouraging reports coming out of Northern Iraq and North Eastern Syria about the battles against the ISIS insurgency, more concrete and positive evidence will be required before we can definitively say that either the territorial advances are being reversed or that the ISIS 'problem' is retreating.

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It is highly likely that after the experiences in Paris that further terrorist atrocities may occur in a large city such as New York, Washington DC, London or even Berlin and this will keep confidence at a lower than expected level for some time.

This will all keep a lid on investment expectations in most areas, which after the mixed 2014 is to be expected. Certainly for the first quarter, new investments should be very carefully weighed up for their appropriateness and potential returns. However, were investors merely to bunker cash for the next 12 weeks and see markets similarly neutral, this would not be a great surprise nor much of an opportunity cost.

It is unlikely that many markets, except for the US and possibly China and India will actually do much between now and 31st March. Indeed, the opportunity is there for a lot of people to lose a lot of money in the Greece's of this world and have little capital to invest when the real opportunities present themselves later in the year.

For the second quarter in a row we advise investor caution in most markets – be careful out there!

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Export Processing Zone Scheme:
Nigeria's Roadmap to Economic Diversification

By Chinemerem Okoro

Like many developing nations, Nigeria has never disguised her desire for industrialization and export-led growth as strategy for economic diversification. After witnessing a shift from agriculture to crude oil and gas as the main driver of growth, the country has pursued various export-oriented strategies at various times to point the economy away from total dependence on hydrocarbon revenues. Mineral export constitute more than 90 per cent of the nation's export, with crude oil accounting largely for her foreign exchange earnings.

Indeed, the nation's over reliance on oil as a major foreign exchange earner has continued to be of major concern to economic watchers as well as managers especially during periods of economic bust. More critically, the recent collapse of oil prices in the international market and the resultant slump in Nigeria's foreign exchange earnings have once again brought to the front burner, the need for the country to diversify her economic structure and broaden her export proceeds.

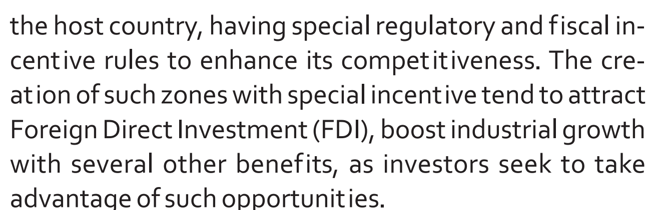
Beyond the drive for export-led growth, specifically non-oil export, Nigeria is known to be a heavily import dependent country. The country relies on importation for a majority of its goods, even food; thereby spendingachunkof her foreign reserve on payment for goods and services imported into the country. For example, Nigeria's value of total import stood at N5.34 trillion (more than US$35 billion)by Q3, 2014 according to National Bureau of Statistics (NBS).

This skewed economic structure has continued to put pressure on the country's stock of foreign exchange reserves as well as domestic currency; making industrialization very imperative. One policy instrument that the country can and has indeed attempted to leverage on, as a strategy for rapid industrialization and diversification is the Export Processing Zone (EPZ) Scheme.

Essentially, Export Processing Zone Scheme as an economic tool, involves a deliberate government policy to encourage exports of goods and services by offering a more conducive and competitive business environment; through the provision of special incentives including tariff exemptions to inputs and infrastructure provision in a geographically defined area called an Export Processing Zone or a Free Trade Zone.

Thus, an Export Processing Zone or Free Trade Zone is a specially designated enclave, clearly delineated and administratively considered to be outside the Customs Territory of

Like many developing nations, Nigeria has never disguised her desire for industrialization and export-led growth as strategy for economic diversification.



the host country, having special regulatory and fiscal incentive rules to enhance its competitiveness. The creation of such zones with special incentive tend to attract Foreign Direct Investment (FDI), boost industrial growth with several other benefits, as investors seek to take advantage of such opportunities.

The adoption of the scheme as a diversification strategy generated some substantial initial impacts in China and other countries like Ireland and Indonesia; leading to its acceptance by a large majority of developing countries including Nigeria. The adoption of Export Processing Zone (EPZ) Scheme as an economic policy by Nigeria was necessitated by the grim picture depicted by her economic structure. The aim is to integrate the economy into the global market through the establishment of a liberal market, promotion of exports in both traditional and non-traditional commodities and stimulation of the transfer, acquisition and adoption of appropriate and sustainable technologies to nurture competitive export-oriented industries.

More so, the Scheme as an economic tool seek to contribute to Nigeria's industrialization quest through forward and backward linkages. Forward linkages allow companies in Export Processing Zones (EPZs) to sell manufactured/finished goods to the domestic consumer basedepending on the model of Free Trade zones adopted while backward linkages allow companies within Export Processing Zones (EPZs) to buy inputs from the domestic marketof the host country and subcontract services to local enterprises. It is easy therefore to surmise from the foregoing, that if effectively and adequately harnessed, the country can leverage on the scheme to industrialize and diversify her economic base which will contribute immensely to meeting the present deficiency in the supply of foreign exchange in the country.

Nigeria's Export Processing Zone Scheme - An overview

In Nigeria, the Export Processing Zone (EPZ) Scheme as a policy tool was adopted in November 1991 to achieve sustainable economic growth, industrialization and diversification. Often referred to as Free Trade Zone (FTZ) Scheme, its overall objective for adoption is to "create an enabling environment aimed at enhancing economic growth and development of export oriented manufacturing in the non-oil sector of the economy, as well as the propagation of the Nigerian content policy in the oil & gas sector in order to diversify the country's economic base, attract Foreign Direct Investment (FDI), generate employment, increase foreign exchange earnings, enhance technology transfer, skill acquisition/upgrading as well as create backward linkages".

To achieve this laudable objective, two bodies were created to effectively manage these zones: the Nigerian Export Processing Zone Authority (NEPZA)established by the NEPZA No 63 of 1992 (now Cap. N107, LFN 2004) and the Oil & Gas Export Free Zone Authority (OGEFZA) established by OGFZA No 8 of 1996 (now Cap. O5, LFN 2004). The bodies are saddled with the responsibility of promoting and facilitating local and international investments into licenced free trade zones (general purpose zones and specialized purpose zones) in Nigeria. There are currently about 31 licenced free zone enterprises operating in the various zones across the country. Of the number, 14 are fully operational while 8 others are still under varying degrees of construction. Physical development is yet to commence in another 8 approved Free trade zones while 1 has its operational license suspended. Also, there are about 10 more Free Trade Zones awaiting approval at different stages.

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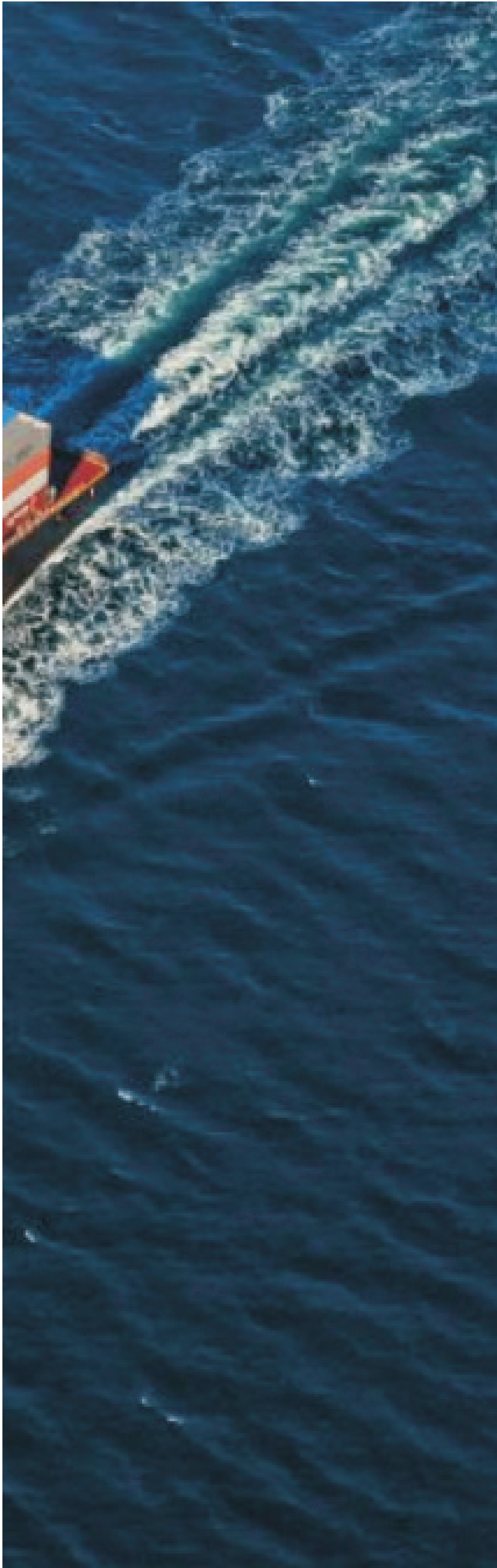

Incentives offered in Nigeria's Export Processing Zones (EPZs)

In order to attract investments in the Export Processing Zones (EPZs), government has strategically designed a wide range of incentives for potential investors to create a win-win situation for the country as well as for investors. Some of these incentives as administered by the governing legislations include: complete holiday from all federal, state and local taxes, rates, and levies;duty free importation of capital goods, machinery/component, spare parts; 100 per cent repatriation of foreign capital investment in EPZs at any time with capital appreciation on the investment; waiver of all import or export licenses; rent free land during the first six months of construction of factory space.

Others are unrestricted remittance of profits and dividend earned by investors in the zone; 100 percent foreign ownership of enterprises in the EPZ; and sale of up to 100 per cent of production (goods) in the domestic market (provided duty is paid on imported raw material).

In addition to these incentives, all free zones in Nigeria are provided with the following standard facilities in order to create an enabling environment for business transactions: large expanse of industrial land with good access to international airports and sea ports, fenced wall around the zones with good security network, trained Free Zone Customs/Immigration roles as obtained in the Free Zones Worldwide. Equally provided are: Police post to provide security for the zone, pre-built zone warehouses for ware-housing and storage of raw material and products, efficient telecommunication facilities, uninterrupted electricity and water supply, good internal/external road network and central transit warehousing facilities at major ports for efficient handling of Free Zone goods.

In a bid to create a readily available market to export goods produced within her shores, the Nigerian government entered into several trade agreements that guarantee preferential tariffs on her exports. Some of these trade agreements include: Global System of Trade Preference (GSTP), World Trade Organisation, African Growth and Opportunity Act (AGOA), Economic Community for West African (ECOWAS)Trade Liberalization Scheme (ETLS), Organisation of Oil Exporting Countries (OPEC), and Developing Eight (D-8) Preferential Tariff Agreement (PTA). All these fiscal, regulatory and infrastructural incentives are geared toward attracting investors into the country's Free Trade Zones.

Beyond Incentives, Nigeria's attractiveness as an Export Hub

Nigeria possess features that make investment in Export Processing Zones (EPZs) very attractive to investors. Besides her abundant natural endowment (both mineral and non-mineral), Nigeria's teeming population of over 170 million people provide a ready market for goods and services. With her policy of allowing sales of goods to the domestic market, investors have access to arguably the largest consumer market in Africa. In addition, the population provide a large pool of skilled and unskilled labour required for productive activities.

Nigeria enjoys an excellent location that creates easy access to markets in Africa, the Middle East, Europe and the Americas. Her access to seashores and even inshore waters make movement of goods from production point to export destinations very convenient. Furthermore, the country has a well-developed aviation industry with six international airports and same number of major port complexes. These features make her arguably one of the best investment destinations in the world.

More so, the government has consciously embarked on several investment climate reform programmes, through various agencies and parastatals, to make Nigeria the preferred investment destination for African and global investors. Such programmes include: establishment of a One Stop Investment Centre in the Nigerian Investment Promotion Commission, start-to-finish 24-hour business incorporation service, intellectual rights and copyright protection policy and establishment of trade and investment desks in major Nigerian embassies abroad, amongst others. In addition to the establishment of

List of Approved Free Trade Zones (FTZs) in Nigeria

S/N	Name	Location	Sponsor/ Developer	Land Size (Hectares)	Date of Designation	Specialty	Status
1	Calabar Free Trade Zone (CFTZ)	Cross River	Fed. Govt.	220	1992	Manufacturing, Oil & Gas, Logistic Services	Operational
2	Kano Free Trade Zone (KFTZ)	Kano	Fed. Govt.	463	1998	Manufacturing, Logistic Services, Warehousing	Operational
3	Tinapa Free Zone & Resort	Cross River	State Govt./Private	265	10/7/2004	Manufacturing, Trade, Tourism & Resort	Operational
4	Snake Island Int. Free Zone	Lagos	Nigerdock Plc	59.416	4/4/2005	Steel Fabrication, Oil & Gas, Sea Port	Operational
5	Maigatari Border Free Zone	Jigawa	State Govt.	214	2000	Manufacturing, Warehousing	Operational
6	Ladol Logistics Free Zone	Lagos	GRML		6/21/2006	Oil & Gas, Fabrication, Oil & Gas Vessels, Logistics	Operational
7	Airline Services EPZ	Lagos	Private		3/21/2003	Food Processing and Packaging	Operational
8	ALSCON EPZ	Akwa Ibom	Fed. Govt./Private	814.619	Jun-2004	Manufacturing	Operational
9	Sebore Farms EPZ	Adamawa	Private	2000	12/21/2001	Manufacturing Oil & Gas, Petrochemical	Operational
10	Ogun Guandong FT Zone	Ogun	State Govt./Private	10000	2/28/2008	Manufacturing	Operational
11	Lekki Free Zone	Lagos	State Govt.		12/4/2008	Manufacturing, Logistics	Operational
12	Abuja Tech. Village Free Zone	Federal Capital Terr	FCT	702	5/18/2007	Science & Technology	Under Construction
13	Ibom Science & Tech. FZ	Akwa Ibom	State Govt.	122.137	7/14/2006	Science & Technology	Operational
14	Lagos Free Trade Zone	Lagos	Eurochem technology Singapore	218	10/4/2002	Manufacturing Oil & Gas, Petrochemical	Operational
15	Olokola Free Trade Zone	Ondo & Ogun	State Govts./Private	10500	2004	Oil & Gas Manufacturing	Operational
16	Living Spring Free Zone	Osun	State Govt.	1607.86	10/12/2006	Manufacturing, Trading and Warehouse	Under Construction
17	Brass LNG Free Zone	Bayelsa	Fed. Govt./Private	304.245	2/2/2007	Liquified Natural Gas	Dev. yet to commence
18	Banki Border Free Zone	Borno	State Govt.	500		Manufacturing, Warehousing, Trading	The Sponsor yet to be committed
19	Oils Integrated Logistics Services Free Zone	Lagos	Private Oil Field Industry Support Service Ltd	1000	10/12/2004	Marine, Logistics, Support Services for offshore Oil Repairs	Operational License Suspended
20	Specialized Railway Industrial FTZ	Ogun	State Govt.		4/30/2007	Rail Cargo Transport	Dev. yet to commence
21	Imo Guangdong FTZ	Imo	State Govt.	1399.27	5/7/2007	Manufacturing	Dev. yet to commence
22	Kwara Free Zone	Kwara	State Govt.	355.587	7/10/2009	Trading, Warehousing	Physical Dev. Yet to commence
23	Koko Free Trade Zone	Delta	State Govt.	2327.29	12/2/2009	Manufacturing	Physical Dev. Yet to commence
24	Oluyole Free Zone	Oyo	State Govt.	1374.5	5/16/2000	Manufacturing	Physical Dev yet to Commence
25	Ibom Industrial Free Zone	Akwa Ibom	State Govt.		20/2/2012	Manufacturing, Oil & Gas, Trading Services	Physical Dev. yet to commence
26	Badagry Creek Integrated Park	Lagos	Kastec Engineering	581	2014	Fabrication	Under Construction
27	Ogindigbe Gas Revolution Industrial Park (GRIP)	Delta	NEPZA/NNPC/Delta	2506.03	2014	Petrochemical, Fertilizer, Manufacturing and Gas Processing related activities	Under Construction
28	Nigeria Aviation Handling Company (NAHCO)	Lagos	NAHCO	10	2014	Cargo Hub, Trans shipment and Warehousing	Under Construction
29	Nigeria International Commerce city	Lagos	Eko Atlantic FZ ltd	1000	2014	Financial institutions (local and international) leisure, real estate, shopping malls and corporate business, commerce	Under Construction
30	Ogogoro Industrial Park	Lagos	Digisteel	52	2014		Under Construction
31	Centenary City	Abuja	Centenary City Plc	1264.78	2014		Under Construction

Source: **NEPZA**

the Competitiveness Council, the government constituted the Doing Business and Competitiveness and Investor Care committees;working with the Department for International Development and the World Bank aimed at removing all barriers to industrial productivity. All these reforms are making Nigeria a more attractive investment destination.

Nigerian EPZ strategy, Are We there yet?

Since the adoption of the Export Processing Zone as an economic policy, Free/Export Trade Zones in the country have continued to increase both in numbers and in scope. The proliferation of the Zones perhaps underscores the potentials they possess in helping the nation attract foreign direct investment and also achieve the much desired economic growth/diversification. Specifically, between 1992 to date, the number of export zones has grown to about 31 with 10 more awaiting approval.

Also, the inclusion of the private sector as well as state governments has opened up more opportunities to the propagation of Free Trade Zones. Today, many Zones are being sponsored and developed bystates in partnership with private investors as a way of attracting investors into their regions in the hope of harnessing the benefits of EPZs.

Agreeably, the scheme has made significant progress in attracting foreign direct investments (FDI) into the country. According to the Nigerian Export Processing Zone Authority (NEPZA), the scheme has attracted a total sum of US$13.5billion from 1992 to date. The government is also targeting another US$68.1billion fresh Foreign Direct Investment from newly licensed free trade zones, with a strategy of fast-tracking the approval of more specialized Export processing zones as well as focusing on high profile investors and their value chains. The scheme has been able to attract companies like General Electric and other leading companies.

However, despite the increase in the number of Export Processing Zones in the country and the huge investments attracted, the result in achieving export diversification has been minimal if not dismal. A lot of the zones that have been granted approvals have remained moribund, value-added has been low, economic linkages and technology transfers have also been poor. To that extent, the scheme has not optimally exploited the country's rich human and natural resources to bring about significant change in Nigeria's export structure. For example, as at Sep-

List of Free Trade Zones (FTZs) awaiting approval

S/N	Name	Location	Sponsor/ Developer	Land Size (Hectares)	Specialty	Status
1	Ossiomo Free Trade Zone		Ossiomo Investment Ltd	1487	Refineries, Petrochemical plant, Gas processing plant, Metal extraction Industries, Metal Fabrication, fertilizer production, warehousing, Packaging and logistics Services.	At the Presidency
2	Enugu Power And Industrial Development Free Zone	Enugu	State Govt./Oil Data Consulting Company Ltd	403.562	Manufacture of high voltage power generation and distribution equipment and accessories, production of fertilizer from coal, and other value added industrial clusters.	At the Presidency
3	Warri Industrial Business Park	Delta	State Govt./ARCO Petrochemical Engineering Company Limited	329.1	Heavy & light Industries, Oil& Gas, shipping & logistics, R&D and Residential Real estate/ Leisure.	At the Ministry
4	Kogi Free Zone	Kogi	State Govt.	268.49	Manufacturing	At the Ministry
5	Baklang Free Zone		Baklang Offshore Support Services Conglomerate (BOSS)	75	Fabrication: ship, high value marine, oil & gas equipment, logistics services and manufacturing.	Appraisal On-going. Site inspection carried out
6	Madewell & Textile INC. Free Zone		Madewell Garments INC	552.534	Manufacturing activities vis-a-vis production of apparels and garments	At the Ministry
7	Eko Atlantic City Free Zone	Lagos	Eko Atlantic FZ Ltd	1000	Financial institutions (local and international), leisure, real estate, shopping malls and corporate business, commerce	At the Ministry
8	Ogidigbe Free Zone		NEPZA	2506.03	Petrochemical, Fertilizer, Manufacturing and Gas Processing related activities	Appraisal On-going. Site inspection carried out
9	Airport Free Zones	Lagos/Port-Harcourt/Kano /Enugu	NEPZA/ Federal Ministry of Aviation	1742.24	warehouses, processing of manufactured goods, tourism and hotel services, light industries	Appraisal On-going. Site inspection carried out
10	Sahara offshore Logistics Base Free Zone		Sahara energy Resources	20.6	Oil & Gas Processing, Fertilizer, Plastics & Chemical, Warehousing, Trans-shipment & Distribution	Appraisal On-going. Site inspection carried out

Source: NEPZA

tember, 2014, Nigeria's export was dominated by mineral product with oil and gas contributing more than 90 per cent of total exports while the country is still heavily dependent on imported goods. Undeniably, the country is yet to harness the benefits of the scheme to its fullest.

A number of factors have been identified as impediments that have retarded the efficacy of the scheme. Some of the challenges facing free zones in Nigeria include: policy reversals and inconsistencies resulting from inadequate knowledge of the scheme; weak infrastructures and power supply; weak regulatory environment due to conflicting and overlapping laws and procedures; security challenges in some regions; non-availability of long-term funds as well as inadequate consideration to export zones scheme in trade policy mix. The seeming failure in this realm appeared to have informed the recent review of Nigeria's policy on the existing zones. The focus of the review is to tackle these challenges and reposition the Zones and make them efficient and functional to maximize the benefits of the scheme.

Optimizing EPZs,the way forward

Export Processing Zoneremains one of Nigeria's most viable liberal market policies that guarantees her economicintegrationinto the global market. The successes recorded in some of the zones in the country and indeed acrossthe globe, clearly demonstrate that it is one of the country's untapped treasure-troves. By creating Export Processing Zones, the country is able to lure investors in export-oriented industries which in turn will spur the transfer and adoption of appropriate technologies needed to harness the nation's abundant and untapped resources. The economic linkages will create jobs for the country's teeming workforce as well

as generate foreign exchange earnings.

However, to effectively harness the potential and benefits of Export Zones, there is need to maintain consistent policies regarding Export/ Free Zones. Government should be seen to be unswerving in her policy stance as it relates to goods allowable, incentives, waivers and other benefits. This might require a special consideration of Free Trade Zones during the process of policy formulation to be sure such policies do not repudiate existing incentives for the Zones. More so, government must ensure a review and harmonization of all laws and regulatory framework with clearly defined duties and responsibilities for all her agencies to avoid overlapping functions.

In addition, the business environment should be made very conducive to be able to attract investors into these Zones. Specifically, there is need for security and political stability as such is necessary to attract foreign investments. Provision of adequate infrastructure in and around the zones especially electricity and accessible roads, rail lines, sea ports and other infrastructures should also be given top priority by developers as well as government.

Finally, government should place special emphasis on high value-added activities in the zones especially manufacturing for exportation. Such zones are generally better integrated into the domestic economy and thus provide sources of far more significant gains for the country as well as place the country on the path to economic diversification.

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TYPES OF INDUSTRIES PERMISSIBLE IN NIGERIA EXPORT PROCESSING ZONES

- Electrical and electronic products
- Textile products
- Wood products
- Leather products
- Plastics products
- Petroleum products
- Rubber products
- Cosmetics
- Garments
- Chemicals products
- Metal products
- Educational materials and equipment
- Communication equipment and materials
- Sports equipment and materials
- Machinery
- Handicraft
- Optical instruments and appliances
- Medical kits and instruments
- Biscuits and confectioneries
- Printed materials, office equipment and appliances
- Paper materials
- Food processing
- Pharmaceutical products
- Oil & gas activities

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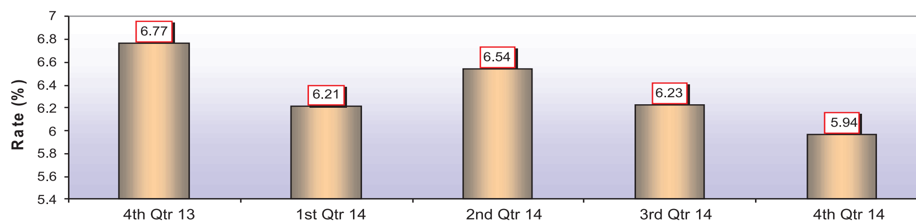
MACROECONOMIC ENVIRONMENT

The Nigerian economy recorded mixed performance in the fourth quarter of 2014. Some of the performance indicators opened the quarter on a wave of optimism but fell dramatically to all-time lows at the end of the quarter. Gross Domestic Product (GDP) growth rate moderated in the fourth quarter 2014 while inflationary pressure eased and remained in the single digit region. The Monetary Policy Rate (MPR) was raised to rein in inflation. The nation's currency, the naira lost value against major world currencies. External reserves fell but remained in comfort zone. Bearish sentiments persisted in the capital market, with investors remaining cautious. In the international commodities market, crude oil prices plunged.

GROSS DOMESTIC PRODUCT

Gross Domestic Product (GDP) grew by 5.94 percent in the fourth quarter, lower than the 6.23 percent recorded in the preceding quarter, according to the National Bureau of Statistics (NBS). Real GDP growth in the quarter under review was driven by the non-oil sector. The oil sector experienced production and price challenges in the quarter under review. The non-oil sector recorded 6.44 percent growth in real terms while the oil sector grew by 1.18 percent in the fourth Quarter of 2014. In 2015, the Nigerian economy, when measured by Real Gross Domestic Product (GDP), is expected to expand by 5.54 percent, again supported by growth in the no-oil sector.

GDP Growth Rate (4th Qtr.13 - 4th Qtr.14)

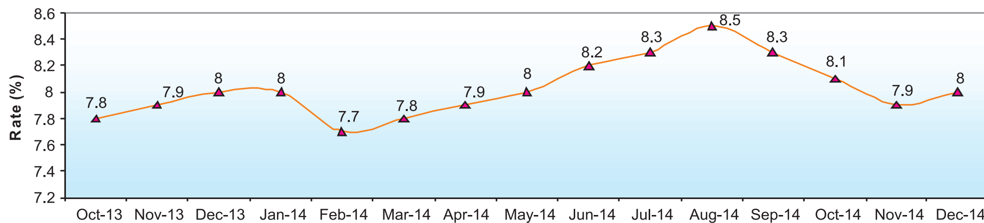


Source: National Bureau of Statistics

INFLATION

Year-on-Year inflation rate remained in the single digit region in the fourth quarter of 2014. Inflation rate has been in the single digit region for eight consecutive quarters (two years). Earlier in October, the headline rate eased to 8.1 percent from 8.3 percent in the preceding month as result of lower food prices due to the harvest season. Inflation eased further for a third straight month in November to 7.9 percent due to lower prices of vegetables and coffee, tea and cocoa. However, inflationary pressure resurfaced in December, closing the year at 8 percent due to the year-end festive period. The prices of meat, fish, bread and cereals edged slightly higher during the yuletide. Nevertheless, core inflation slowed for the first time since August 2014. In the months ahead, inflation risk remain due to the devaluation of the naira. The lagged impact of the deprecia-tion is expected in the first half of 2015. However, prices are likely to ease by the end of the year as a result of harvesting period.

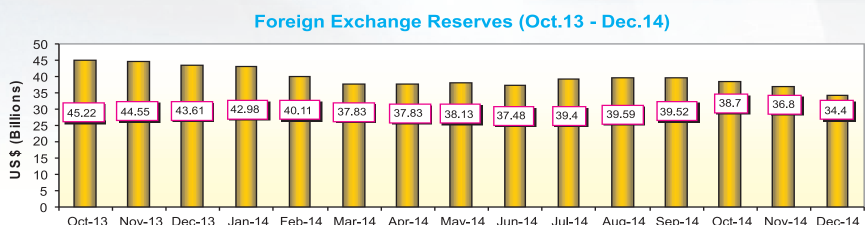
Inflation, Year-on-Year (Oct.13 - Dec.14)



Source: National Bureau of Statistics

EXTERNAL RESERVES

The nation's foreign-exchange reserves fell in the fourth quarter of 2014, due to plummeting oil prices. External reserves closed the year at a two year low of $34.4billion after shrinking by $9.1billion following massive interventions aimed at easing pressure on the naira. The stock of external reserves is however capable of financing about seven months' worth of imports. A significant drop in revenue from oil as well as continuous withdrawals depleted Nigeria's reserves by 30 percent since hitting $48.8billion in April 2013. In the short to medium term, the monetary authority will continue to resort to the external reserves to protect the domestic currency. Consequently, analysts project a bottoming of about $32-$33billion.



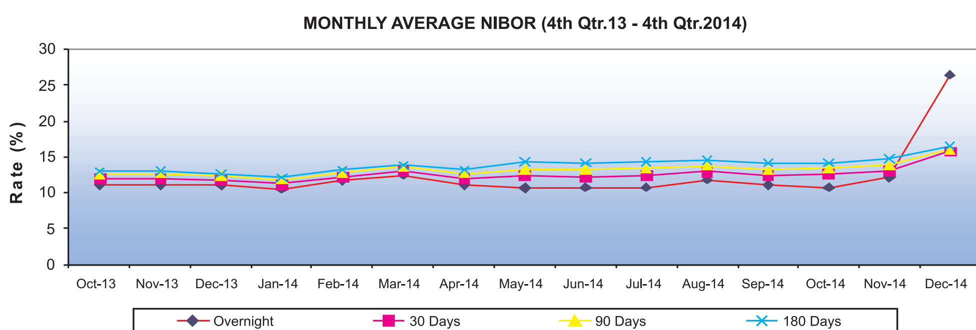
Source: Central Bank of Nigeria

INTEREST RATE

In a proactive move much anticipated by analysts, the Monetary Policy Committee (MPC) in its November 2014 meeting, took a hawkish stance and raised its key interest rate – the Monetary Policy Rate (MPR). The MPR was raised by 100 basis points to 13 percent, the first change since October 2011. The MPC also adjusted the cash reserve requirement (CRR) on private sector deposits to 20 per cent, from 15 per cent. The CRR on public sector deposits was unchanged at 75 per cent.

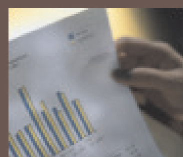
The average interbank rate witnessed significant swings in the fourth quarter 2014. In October, the call and OBB rates remained stable at 10.50 percent. However, the OBB and overnight rate rose to 20 percent and 14.2 percent, respectively in November, due to the increase in MPR and CBN's withdrawal of N568billion as CRR debit from banks. The pressure was nevertheless matched with T-bills maturities of N415billion resulting in rates crashing to 13 percent. It was however short-lived as the OBB and overnight surged to 60 percent and 44 percent respectively in December, due to liquidity pressure from RDAS funding and another round of CRR debit of N327billion.

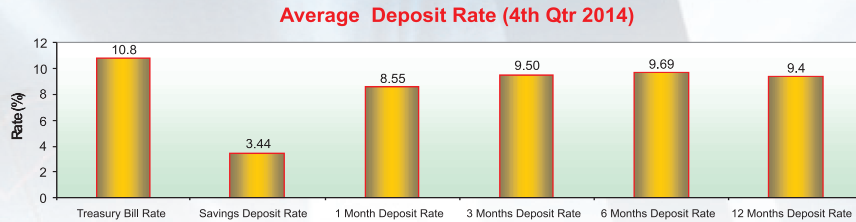
The average Prime Lending Rate (PLR) dropped slightly during the period, hovering around 16 percent as at end December 2014. Returns on the average deposit rate went up across most investment horizons, with volatility higher on the 90 Days and 365 Days tenors.



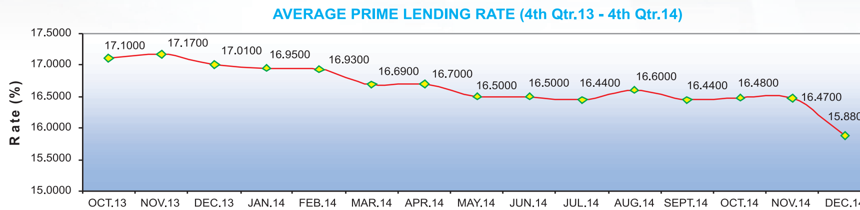
Source: FMDQOTC

Facts & Figures





Source: FMDQOTC



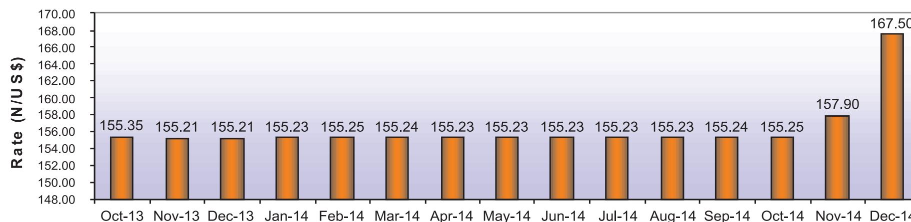
Source: FMDQOTC

EXCHANGE RATE

The nation's currency, the naira, tumbled to its weakest level on record in the fourth quarter 2014, slipping against major world currencies. It dropped in value when the CBN devalued the mid-point of the naira's official trading band from N155/$1 to N168/$1 and widened the band from +/- three per cent, to +/- five per cent. Earlier in October, the naira remained relatively stable despite pressure from lower oil prices. The smooth ride was however interrupted in November due to favourable developments in the United States, resulting in foreign investors exiting the local market. The naira consequently hit an all-time low of N184.40/US$ in December. To ease the pressure, the apex bank introduced a number of measures such as imposing a 10kobo margin on funds bought through CBN's intervention and allowed a period of two days to utilize the fund; banned the sale of dollars to importers of telecoms equipment, power generators and finished products at its foreign exchange auction; restricted banks and discount houses from placing more than N7.5billion each as deposit with CBN; and reviewed downward the foreign exchange trading position of authorized dealers to zero percent from 1 percent of shareholders funds.

Following the 7.74% Naira devaluation, the USD/NGN traded within a range of N181 to N184 at the inter-bank, but closed the quarter at N183.48. In its twice weekly auction, the apex bank offered about $6.75billion and sold $6.90billion during the period. The premium however inched up slightly between the official and interbank market from 5.0 percent as at end October 2014 to 9.0 percent in December.

MONTHLY AVERAGE EXCHANGE RATE (N/US$)



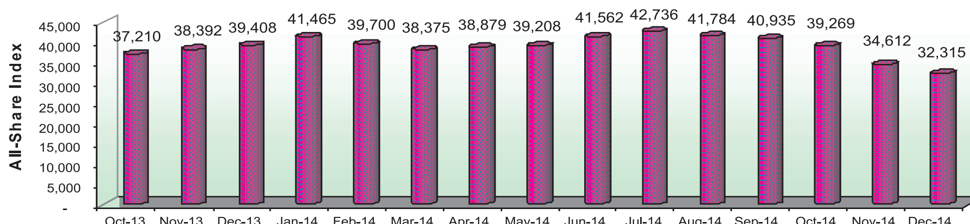
Source: Central Bank of Nigeria

Facts & Figures

CAPITAL MARKET

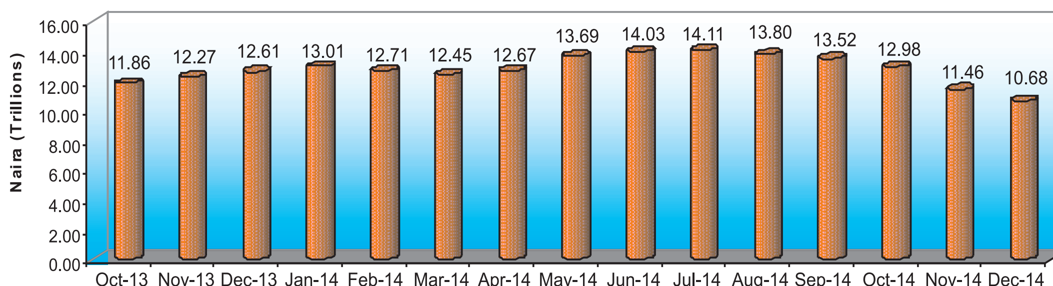
Equities in the capital market suffered major setback in the fourth quarter 2014. It witnessed its slowest growth in two years with a loss of -15.9 percent return. The All-Share Index (ASI) and market capitalization finished lower at 34,657.15 and N11.47trillion, respectively, from 41,210.10 and N13.60trillion in the preceding quarter. With the general election drawing nearer, political uncertainties made investors to remain cautious. Many investors exited the stock market for treasury bills and bonds, considered to be relatively safer, sending margins further down. Sentiment was further dampened as a result of CBN's naira devaluation, tighter monetary policy and falling oil prices. On a brighter note however, there were more foreign inflows than outflows in December 2014. To resuscitate the market, the Federal Ministry of Finance exempted VAT on stock market transaction in October. A number of quoted companies such as Nigerian Breweries, Seplat and Nestle paid impressive dividends of N1.25; N9.00 andN10.00, respectively. In a show of confidence, Presco, Oando and UBA raised capital by Rights Issue. In the international capital market, activities in emerging market bonds remain attractive despite concerns over liquidity.

ALL SHARE INDEX (ASI) (4th Qtr.13 - 4th Qtr.14)

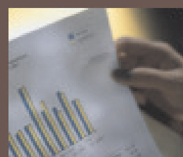


Source: Nigerian Stock Exchange

NSE MARKET CAPITALISATION (4th Qtr.13 - 4th Qtr.14)



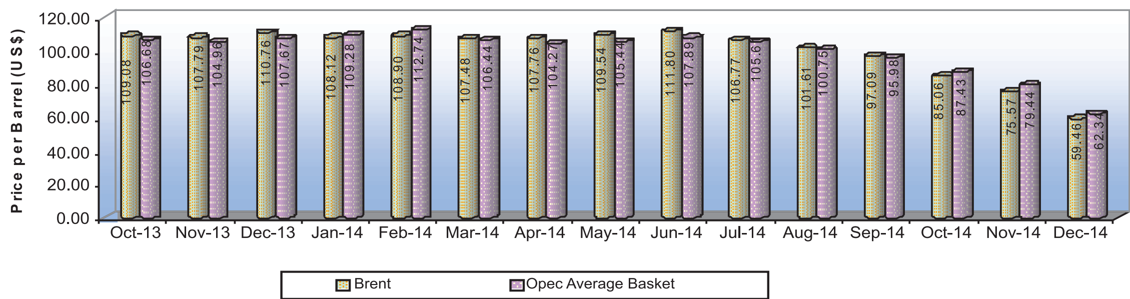
Source: Nigerian Stock Exchange



OIL & GAS

Crude oil prices fell sharply in the fourth quarter of 2014 owing to supply and demand imbalances. After reaching monthly peaks of $112 per barrel in June, crude oil lost about 47 percent, collapsing to $59 barrels per day (bpd) in December, the lowest in 5 years. Nigeria's brand of crude oil, bonny light, traded within an average band of $91-$53 per barrel in the quarter under review. Industry analysts attribute fall in crude oil prices to higher inventories; the boom in U.S. shale oil (at 8.6 million barrels a day), highest level in nearly 30 years; the coming on line of Libyan oil; slowdown of world's second largest oil consumer – China; and the inability of OPEC to agree on production cuts in the face of glut. In its 166th meeting in Vienna, Austria, on 27 November 2014, OPEC members decided to maintain the current production level of 30million barrels per day, fueling speculation that prices may remain low for some time.

Oil Prices: Monthly Average Price Movements (4th Qtr.13 - 4th Qtr.14)



https://www.worldwildlife.org/media?threat_id=oil-and-gas-development