

Nigerian Breweries Plc: *Consolidating Growth*

September 05,
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FSDH Equity Research Report

Executive Summary

HOLD

Nigerian Breweries Plc (**Nigerian Breweries**) is a subsidiary of the internationally established Heineken N.V. of the Netherlands, having 54.10% stake in the equity of Nigerian Breweries and is the largest brewing company in Nigeria. Nigerian Breweries was originally incorporated, as 'Nigerian Brewery Limited', on November 16 1946. Three years later; it recorded a milestone, producing its first bottle of STAR Lager from its Lagos Brewery. In 1973, Nigerian Breweries became a public company and was officially listed on the floors of The Nigerian Stock Exchange (NSE) on September 5, 1973. Since incorporation, it has consistently expanded its business activities, commissioning new breweries in Aba, Kaduna, Ibadan, Enugu and Ama, comprising five operational breweries in total from which its high quality products are distributed across Nigeria. Furthermore, it has promoted the creation of various ancillary businesses, including companies that manufacture bottles, labels, cartons, and crates, in order to ensure adequate supplies of the raw materials necessary for sales and distribution.

Nigerian Breweries produces and offers beer under the **Star** and **Gulder** brands, lager under the **Heineken** brand, malt drinks under the **Maltina** and **Amstel Malta** brands, premium stout under the **Legend** brand, a sparkling soft drink under the **Fayrouz** brand, and a recently launched energy drink, **Climax**.

During the year under review, the company successfully completed the acquisition of **Sona Systems Associates Business Management Limited**, which currently own two breweries in Nigeria (Sango Otta and Kaduna), and **Life Breweries Company Limited (Onitcha)**. The successful integration of the three additional breweries to the company's operations led to an increase brand portfolio and consequently an increase in the earnings potential of the company. With the acquisition, Nigerian Breweries has the rights to Goldberg Lager and Malta Gold (Sona Systems) and Continental Life Lager (Life Breweries). Furthermore, Nigerian Breweries has sought to build and consolidate its connection with its customers, launching various programmes designed to boost consumer affinity and maximize sales opportunities.

Total shareholders' fund of Nigerian Breweries grew to N78.07bn in 2011 from N50.17bn in 2010, translating to an increase of 55.60% over the period. The increase in total shareholders' fund was primarily driven by 80.26% growth in retained earnings from N34.73bn in 2010 to N62.61bn in 2011. The growth in the retained earnings was as a result of the improved performance in the bottom line recorded during the period. Despite challenging business climate, with increased competition from other players in the industry, particularly Guinness Nigeria Plc, Nigerian Breweries was able to maintain its leadership position as well as boost its revenue and deliver good returns to all stakeholders of the company.

Turnover increased from N111.75bn in 2007 to N230.12bn in 2011, representing a CAGR of 19.79% and increased by 23.81% between 2010 and 2011. The growth in turnover was primarily as a result of major improvements to the company's supply structure, increased investment in the company's brands and capacity expansion. The number of times capital employed could generate revenue decreased from 2.67x in 2010 to 1.60x in 2011. We expect the ratio to improve as the economic fortunes of the country begin to improve. In addition, Nigerian Breweries' various initiatives, such as the expansion and modernization of plants, in addition to various acquisitions plan of the company. The performance of Nigerian Breweries in the last five years has been impressive despite the harsh macroeconomic environment in which the company carried out its operations.

An investment in the shares of Nigerian Breweries in January 2007 has grown by 263.98% as at the date of this report. Applying two relative valuation methods, we arrived at a fair value of **N126.13** per share. The current share price only has about 6.5% upside potentials both in terms of dividend payment and capital appreciation to the fair value. Therefore our current rating on Nigerian Breweries based on the current market price is a **HOLD**.

Current Price	N123.00
Fair Value	N126.13

Beta	0.83
Alpha Coefficient	0.15
R²	16.19%
Z-Score	5.38

1.0 Corporate Information

Nigerian Breweries Plc (Nigerian Breweries) is a subsidiary of the internationally established Heineken N.V. of the Netherlands, having 54.10% stake in the equity of Nigerian Breweries and is the largest brewing company in Nigeria. Nigerian Breweries was originally incorporated, as 'Nigerian Brewery Limited', on November 16 1946 three years later; the company recorded a milestone, producing its first bottle of STAR Lager from its Lagos Brewery. In 1973, Nigerian Breweries became a public company and was officially listed on the floors of The Nigerian Stock Exchange (NSE) on September 5, 1973. Since incorporation, Nigerian Breweries has consistently expanded its business activities, commissioning new breweries in Aba, Kaduna, Ibadan, Enugu and Ama, comprising five operational breweries in total from which its high quality products are distributed across Nigeria. Nigerian Breweries' commitment to long-term, lucrative business development saw the company establish a Research and Development Centre, in 1987. Furthermore, it has promoted the creation of various ancillary businesses, including companies that manufacture bottles, labels, cartons, and crates, in order to ensure adequate supplies of the raw materials necessary for sales and distribution. Over the years, Nigerian Breweries has bolstered its position as one of the most renowned brands in the breweries industry, with good quality beverages that are popular across Nigeria.

Nigerian Breweries and is the largest brewing company in Nigeria.

The long-term successes of Nigerian Breweries' trade stem predominantly from the company's focus on key capacity investments, on a minimization of manufacturing costs and on the maximization of production efficiency; these are supported by a push to increase investments in the company's brands, which serves to make Nigerian Breweries' products more appealing to a larger number of consumers. The company has built a solid and lasting relationship with consumers based on knowledge of the local cultures and markets in which it operates.

Nigerian Breweries is a socially conscientious and responsive organization that acts with the improvement of its host communities and environments in mind. The company's mission statement – "to be the leading beverage company in Nigeria, marketing high quality brands to deliver superior customer satisfaction in an environmentally friendly way" – underlines its deep commitment to corporate social responsibility.

1.1 Business: Nigerian Breweries' major business activities involve the brewing, marketing, and selling of alcoholic and non-alcoholic beverages, such as lagers, stouts, non-alcoholic malt drinks, and soft drinks. The company has a strong portfolio of brands, which are renowned beverages across various parts of the country. Nigerian Breweries produces and offers beer under the **Star** and **Gulder** brands, lager under the **Heineken** brand, malt drinks under the **Maltina** and **Amstel Malta** brands, premium stout under the **Legend** brand, a sparkling soft drink under the **Fayrouz** brand, and a recently launched energy drink, **Climax**.

The company has a strong portfolio of brands, which are renowned beverages across various parts of the country

Table 1: Shareholding Structure as at December 31, 2011

Shareholders	No of Shares Held	% of Shareholding
Heineken Brouwerijen B. V	2,853,760,692	37.74
Distilled Trading International B. V	1,237,500,160	16.36
Stanbic Nominees Nigeria Ltd	641,140,009	8.48
Others	2,830,161,479	37.42
Total	7,562,562,340	100.00

According to the Register of members, only companies within the Heineken N.V. Group held more than 10% of the Issued Share Capital as at 31st December, 2011.

Table 2: Company Summary

Ticker	
Sector	Breweries
Date of Incorporation	16 th November, 1946
Date of Listing	5 th September, 1973
Financial Year End	December
Number of Fully Paid Share	7,562,704,432
Current Capitalization(NGN)	930,212,645,136
NSE Capitalization (NGN)	7,753,524,458,193
% of NSE Capitalisation	12
52 Week high NGN	123.00
52 Week low NGN	76.18
YTD Return (%)	33.45
52 Weeks Average Volume Traded	2,763,646
Trailing EPS NGN	5.08
Trailing P/E ratio (X)	24.19

Table 3: Directors' Shareholding as at December 31,2011

Director	Position	No of Shares
Chief Kolawole B. Jamodu, OFR	Chairman	431,704
Mr. Nicolaas A. Vervelde	Mgr. Director/CEO	Nil
Mr. Olusegun S. Adebajji	Non Ex-Director	200,000
Mr. Hubert I. Eze	Sales Director	41,383
Mr. Victor Famuyibo	Human Resource Director	Nil
Mr. Jasper C. Hamaker	Finance Director	Nil
Mr. Paul Hamers	Non Ex-Director	Nil
Mr. Thomas A. de Man	Non Ex-Director	Nil
Mr. Frank N. Nweke, Jr	Non Ex-Director	4,400
Mr. Atedo N. A Peterside	Non Ex-Director	15,000,000
Mr. Hendrik A. Wymenga	Technical Director	Nil
Mr. Ishmael E. Yamson	Non Ex-Director	Nil

2.0 Review of Nigerian Economy

Available data from the National Bureau of Statistics (NBS) shows that the Real Gross Domestic Product (GDP) in Nigeria grew by 6.17% in Q1 2012, compared with 7.13% recorded in Q1 2011. The NBS noted that the growth surpassed its previous forecast of 5.34%, which indicated that the economy is more resilient than otherwise anticipated. Nevertheless stronger growth is expected in Q2 2012 as a result of sectoral reforms in the non-oil sector.

GDP in Nigeria grew by 6.17% in Q1 2012, compared with 7.13% recorded in Q1 2011

The analysis of the sectoral growth rate in Q1 2012 shows that there was a decline in both the oil and non-oil sector of the economy. A further analysis of the non-oil sub-sector shows that only solid minerals and building & construction recorded high growth rates in Q1 2012 over Q1 2011. The increase in building & construction was due to increased activities in the power sector, as well as road and rail construction by the three tiers of government and other private institutions. Meanwhile, Telecommunication & Post sector recorded the highest real GDP growth rate of 32.83%, followed by Building & Construction: 13.25%; Solid Minerals: 11.69%; Hotel & Restaurant: 11.45%; Real Estate: 9.39%; Wholesale & Retail: 8.35%; Business & Other Services: 7.68%; Manufacturing: 5.15%; Agriculture: 4.15%; Finance & Insurance: 3.53%; others stood at 4.77%, while Crude Petroleum recorded a decline of 2.32%.

Telecommunication & Post sector recorded the highest real GDP growth rate of 32.83%,

Although the Nigerian economy has been recording robust growth rates in the last few years, a critical look at the figures published by the NBS shows that the Nigerian economy real GDP growth rate, has been decelerating since the beginning of 2011 in the face of high unemployment rate currently at 23.90%. GDP growth rate in Q1, 2011 was 7.13% lower than 7.36% in Q1, 2010; 7.61% in Q2 2011 lower than 7.69% in Q2 2010; 7.3% in Q3 2011 lower than 7.86% in Q3 2010; 7.68% in Q4, 2011 lower than 8.36% in Q4, 2010 and finally 6.17% in Q1, 2012 lower than 7.13% in Q1 2011. The growth rate in Q1, 2012 is the lowest in the last 9 quarters and it is worrisome because agriculture which accounted for an average of 40% of the real GDP in the last 9 quarters, recorded the lowest growth rate of 4.15% as against 5.54% in Q1 2011 and 5.43% in Q1 2010. Its contribution to real GDP in Q1 2012 was also the lowest in last 9 quarters. Various factors have been given for the declining growth rate. Some of which are: the poor infrastructure in the economy; security challenges in the country which has reduced free mobility of goods and people; vandalism of petroleum pipelines in the country; weak purchasing power and high interest rates regime in the economy. Also, the CBN has been supporting some sectors of the economy through the provision of credits at rates that are below the market rates in order to boost outputs. Other critical sectors of the economy such as wholesale and retail trade, manufacturing, construction and real estate that access funds at market rates are finding it difficult to survive.

The poor infrastructure in the economy; security challenges in the country which has reduced free mobility of goods and people; vandalism of petroleum pipelines in the country; weak purchasing power and high interest rates regime in the economy.

On average, wholesale and retail trade is the second largest sector of the Nigerian economy and thus developments in this crucial sector affect other macroeconomic variables in Nigeria.

Our discussions with some multinational companies operating in Nigeria reveal that some of them are already seeking funds from their parent companies to fund their operations in Nigeria as a way of avoiding the high interest rate regime in Nigeria. This is one of the strategies they have adopted to lower finance cost which they may not be able to pass on to their customers in the form of an increase in the price of goods. We appreciate the fact that some of the factors causing the declining GDP growth rate may not be addressed by pure monetary policy tools, but a relaxed monetary policy stance may improve the situation to prevent Nigeria from joining the league of countries already in recession. In the “Economic & Financial Market: Review and Outlook for HY2 2012”, FSDH Research released a GDP growth rate forecast of 6.5%-7% for 2012.

The CBN has over time justified the persistent increase in the anchor interest rate in 2011 in order to bring down inflation rate to its target of single digit. It also argued for a regime of maintaining a real positive return on fixed income securities in Nigeria so as to attract foreign investors to the domestic market to supply foreign exchange. Inflation rate stood at 12.8% as at July 2012, higher than the single digit target of the CBN. FSDH Research is of the opinion that inflation rate will remain in double digit to end the year 2012. The cause of the current inflation rate can be linked to the shortage in production of basic needs, security challenges in the country, pass through effect of prices of commodities in the international market, high finance charge for manufacturing industries, and the effects of the partial removal of fuel subsidy.

In our opinion, raising interest rate to maintain stability in the foreign exchange market has not been effective in Nigeria because of the high import dependent and mono-export nature of the Nigerian economy. Recent evidence shows that the attractive yields on marketable securities in Nigeria have not been able to attract the needed foreign funds to bring about the desired stability and appreciation in the value of the Naira. The major determinants of supply of foreign exchange in Nigeria are oil output and crude oil price as oil accounts for over 70% of the total export proceeds in Nigeria. While Nigeria has control over domestic oil output, being an oil producing nation, it has no control over the quantity it sells in the international market, being a member of the Organization of the Petroleum Exporting Countries (OPEC). It also has no control over the price, which is determined by the state of the global economy. Favourable oil output in Nigeria which averaged about 2.16mb/d and good oil price which averaged US\$115.12/b year to date, have supported the supply of foreign exchange into Nigeria in the recent

time. Developments in the non-oil sector of the Nigerian economy and appropriate policies should help to diversify the segment Nigeria's earnings and increase the supply of foreign exchange. Meanwhile, the current measures put in place by major central banks around the world may salvage the advanced economies from the ongoing crisis. And this may sustain the price of oil at the international market in the short to medium term.

On the demand side, the structure of the Nigerian economy warrants the importation of basic necessities which have no local substitutes. In addition, the massive corruption connected with the importation of refined petroleum products in Nigeria, contributed to the huge demand pressures on the foreign exchange in Nigeria. We think that the fight against fraud associated with the importation of fuel into the country (which is outside monetary policy), the demand pressure for foreign exchange will drop and it will be very easy for the CBN to keep the value of the Naira stable.

Finally, there is a correlation between the growth in external reserve and the movement in oil price. This is because oil dominates the exports and the foreign exchange earnings in Nigeria. The increase in the level of reserve in recent months can be attributed to the favourable crude oil price, improved oil output, foreign capital flow into Nigeria, and reduced speculative demand for dollars and fiscal discipline. As at September 04, 2012 the country's external reserves stood at US\$39.35bn, representing an increase of 19.53% from December 2011 figure of US\$32.92bn. This level of reserves can support stable exchange rate in the short-term. Therefore, the combination of improvement in oil market, accretion to external reserves and managed float strategy of the CBN should keep the value of foreign exchange stable in the short-run.

3.0 Review of Nigerian Manufacturing Sector

The Nigerian manufacturing industry is relatively small in relation to the size of the domestic economy. The sector has not grown remarkably over the years due to a series of factors: the neglect of the sector in favour of oil, an unreliable power supply, and the country's deficient infrastructure, among others. The Nigerian government maintains that the industry is the main instrument of rapid growth, structural change and self-sufficiency, and it has begun to pursue the necessary policies to improve the performance of the manufacturing industry.

As at Q1 2012, the manufacturing sector grew by 1.12%, as against the growth rate of 1.13% recorded in the corresponding period of Q1 2011. The sector also contributed 5.15% to the real GDP as at Q1 2012, as against the contribution of 6.16% in Q1 2011. Recent specific factors that have impeded the

growth of the sector are the adverse impact of the petrol subsidy removal on consumer purchasing powers, rising commodities prices in the international market, poor infrastructure in Nigeria, the lack of credit to the real sector from the banking industry and the restrictive monetary policy of the CBN, all of which adversely affected production, finance, distribution and overhead costs of manufacturing companies in Nigeria. All these factors lowered the bottom-line of the operators in the sector. Further analysis of the operating environment shows that in order to meet their electricity needs, manufacturing companies invest heavily in alternative sources of power. The cost of acquiring and maintaining this equipment increases the cost of doing business by no small measure. As noted earlier, the price hike in petrol prices in early 2012 placed additional burden on the operations of manufacturing companies as raw materials; cost of labour and transportation cost went up. This is also in addition to the weak purchasing power arising from this as consumers' incomes were impacted adversely.

The increasing reliance on the importation of basic food items such as wheat, rice and sugar places a high cost on manufacturing operation in the country as it increases the cost of raw materials for manufacturing firms. Manufacturing firms sometimes shift some of these costs to their customers in form of increases in the price of goods, while the firms bear a portion of it. The extent of this shift also depends on the elasticity of demand for the product in question to price. Sometimes we notice a drop in demand, as a result of increases in price.

Some of the measures currently being implemented to reposition the sector are: reforms in the power (electricity) sector to improve generation and distribution; Public-Private Partnership (PPP) initiatives for infrastructure development and management; import substitution strategies; giving tax break or holiday to certain categories of manufacturers and efforts to improve lending to the sector at concessionary terms.

Some of the opportunities that the operators can tap into are: abundant natural resources and raw materials; large market size; regional agreements that encourage trade across borders and export incentives available in the country.

The growing middle class of Nigeria, whose tastes and life style are changing for high quality consumer goods and products, presents an important opportunity for operators in the Fast Moving Consumer Goods (FMCG) industry to grow their consumer base.

4.0 Review of Nigerian Brewery Sector

The Nigerian brewery sector is characterized by two dominant players, responsible for about 80% of the industry market share based on turnover. These companies are Nigerian Breweries Plc and Guinness Nigeria Plc. They are responsible for the production of several nationally recognized brands which has created a stiff but healthy competition within the sector.

Recent factors in the Nigerian environment prove favourable for the brewery industry. Performance within the brewery industry is dependent on consumer income and spending habits. The increased power output hitting historical peaks in the month of August 2012 have increased the purchasing power of Nigerians. Nigerians spend less of their income on alternative sources of power generation and are able to direct a larger proportion of disposable income towards consumption of food and beverages. Also, the increased power generation in the country helps lower the cost of production and boost the profit margin of companies within the brewery sector. These companies enjoy a large target market with Nigeria boasting a young population of about 160million people. However, recent specific factors have impeded the growth of the sector. The aggressive security challenges in some part of the country impede the movement of goods and services thereby affecting business operations in distressed areas.

5.0 Nigerian Breweries' Corporate Governance

Nigerian Breweries adopts high standards of corporate governance and, in conformity with the Code of Best Practice in Corporate Governance, the Directors have established a number of Committees to supervise the company's corporate governance mandates.

The corporate governance structure of the company consists of:

- Executive Committee
- Remuneration Committee
- Nomination Committee
- Audit Committee

The Executive Committee comprises the Executive Directors and two other Senior Managers occupying strategic roles in the business. It is responsible for pinpointing the company's priorities, allocating resources, setting overall corporate targets, and formulating and monitoring divisional strategies and plan. Headed by the Managing Director/Chief Executive Officer (CEO) of the company, the Executive Committee manages the daily affairs of the business. The Remuneration Committee handles the tasks of reviewing executive remunerations and determining specific remuneration

packages for the company's various Directors. The Nomination Committee is responsible for making recommendations to the Board on candidates for appointment as Directors, while the Audit Committee, composed of three Shareholders' representatives and three Directors' representatives, reviews the Company's overall risk management and control systems, financial reporting arrangements and standards of business conduct.

Nigerian Breweries is a socially responsible corporate citizen with an admirable record of corporate philanthropy in the key areas of education, the environment, and sports, among others

Nigerian Breweries is a socially responsible corporate citizen with an admirable record of corporate philanthropy in the key areas of education, the environment and sports, among others. Over the years, Nigerian Breweries has been highly active in supporting Nigeria's national developmental aspirations, by continuing to identify and respond to the major challenges confronting the nation in line with the company's corporate philosophy and values. In 1994, the company established an Education Trust Fund of N100mn to take a more active part in the funding of educational and research facilities in higher institutions, in an effort to provide and encourage academic excellence in Nigeria. Additionally, Nigerian Breweries donates money towards both university and secondary scholarship programmes for the children of its employees. Nigerian Breweries is also the foremost sponsor of sports, by variety, in the country with sponsorship covering a wide range of sports, from "Ayo" to "Chess" and from "Badminton" to "Soccer". The company is also involved in nurturing and promoting musical and movie talents, through a range of platforms.

5.1 Strategic Focus

Nigerian Breweries has a clear goal to fuel the growth of its products through fast, exciting innovation and expansion. As the Nigerian subsidiary of a multi-national brand, Nigerian Breweries is able to draw on the expertise of its parent company, Heineken, and to work seamlessly with a network of global and regional production centres that provide a key source of technical support.

During the year under review, the company successfully completed the acquisition of **Sona Systems Associates Business Management Limited**, which currently own two breweries in Nigeria (Sango Otta and Kaduna), and **Life Breweries Company Limited** (Onitcha). The successful integration of the three additional breweries to the company's operations led to an increase brand portfolio and consequently an increase in the earnings potential of the company. With the acquisition, Nigerian Breweries has the rights to Goldberg Lager and Malta Gold (Sona Systems) and Continental Life Lager (Life Breweries). Furthermore, Nigerian Breweries has sought to build and consolidate its connection with its customers, launching various programmes designed to boost consumer affinity and maximize

The company successfully completed the acquisition of Sona Systems Associates Business Management Limited and Life Breweries Company Limited

sales opportunities.

It is expected that the acquisitions will result in superior revenue opportunities, enhanced operating efficiencies, and economies of scale, particularly in purchasing and distribution. Nigerian Breweries is also involved in the development of new Sorghum Hybrids, with the potential of increasing the quality of malt produced and the output of its sorghum growers. Such advancements will help to stimulate the sorghum industry and shape a sustainable malting process, which will guarantee the production of high quality sorghum malt that should consistently meet specifications for beverage making in the company's breweries.

Nigerian Breweries is also involved in the development of new Sorghum Hybrids, with the potential of increasing the quality of malt produced and the output of its sorghum growers.

Nigerian Breweries recognizes that its employees are crucial assets in the company's pursuit of continuing success, and, in this vein, the company offers a number of overseas and local training programmes, as well as an exchange programme (with Heineken International), for employees to participate in. Nigerian Breweries intends to continue to leverage on its improved capability via looking for cost saving opportunities to make the company more fit to compete and adapt to a changing and challenging operating environment. This is critical to the company in order to deliver sustainable growth and profitability.

Other focus areas of the company are:

- Internal cost-cutting strategies in order to continue to offer competitive pricing;
- Intensifying marketing efforts, to foster consumer affinity, brand recognition and off-take for all brands;
- Combining organic growth with inorganic growth;
- Major investment in capacity expansion, reflecting a continuous investment in high production capacity;
- Leveraging on the technical know-how of its parent company;
- Boosting revenue mainly by volume as opposed to price hike.

4.0 SWOT Analysis	
Strengths	Weakness
<ul style="list-style-type: none"> ➤ Strong roots in local market and culture ➤ Increased production capacity, operating efficiencies and brand portfolio ➤ Streamlining and optimization of production processes ➤ Diversified and international management ➤ Existing taste and preference for products by consumers ➤ Strong promotional and community base projects which makes customers remain loyal to products 	<ul style="list-style-type: none"> ➤ Inability to meet existing consumer demand ➤ Inadequate local source of raw materials
Opportunities	Threats
<ul style="list-style-type: none"> ➤ Enhanced revenue opportunities from acquisitions ➤ Large market size ➤ Stable macroeconomic environment ➤ Strong alliance with parent company 	<ul style="list-style-type: none"> ➤ Reduction in purchasing power in the country due to rising unemployment ➤ High commodity prices for raw materials ➤ Intense competition within the industry ➤ Competition of telecommunication products for consumers' disposal income ➤ Crisis in some regions of the country ➤ Growing religious organizations that are opposed to taking alcoholic drinks in Nigeria

5.2 Product Analysis

Nigerian Breweries manufactures and distributes numerous well recognized brands in the Nigerian market. It holds a dominant stake in the brewery industry with leading brands in the beer, Malt and soft drink sector.

Beer Sector

As the legal alcoholic drinking age in Nigeria is 18 years, Nigerian Breweries potential target market is large as Nigeria boasts of a high number of young people as a proportion of the estimated population of 160 million people. Most brands within the beer sector are faced with direct substitutes, companies within this sector are forced to differentiate themselves through brand quality and brand differentiation to win and sustain consumers' limited resources. Beer consumption in Nigeria is also regional and popularity of a particular brand may depend on availability within that region. Beer brands under Nigerian Breweries portfolio include Star, Heineken, Gulder, Goldberg and Life Continental lager beer.

Star

Star is a major player within the beer sector. The Star brand has gained an increased brand recognition and consumer loyalty among Nigerians through the various Corporate Social Responsibility (CSR) initiatives within the Nigerian community. Most notably- STAR MegaJam, STAR Quest and STAR Trek. Star also uses these platforms to maintain brand acceptance, further differentiate itself in the eyes of consumers and as an avenue for young adults to showcase their talents. Star's most direct substitute is Harp larger beer, produced by Guinness. However, Star remains the better performing brand as a result of its effective marketing strategy, and commitment to the community.

Heineken

Heineken is a leading international premium brand that is currently packaged in four varied sizes to serve various celebratory needs. Heineken recently extended the Heineken brand with the Heineken Magnum (champagne bottle) which contains 150cl of Heineken larger beer. This bottle was designed for sharing and to accommodate the celebratory nature of Nigerians.

Gulder

Gulder was first introduced in 1970 as a strong flavoured beer. Gulder closest substitute is Satzenbrau Pilsner Lager, produced by Guinness. Gulder remains the more popular brand. Just like Star brand, Gulder engages in several community building events to build consumers' affinity and promote brand loyalty. Examples of these events include: Gulder ultimate search and Gulder celebrity showdown.

Malt Sector

Maltina is a leading malt drink in Nigeria fortified with calcium and vitamin. It currently differentiates itself from competitors by offering variant flavors of Maltina (strawberry, pineapple and exotic flavors) as well as varied packaging sizes to accommodate consumer needs(Maltina sip-it, 33cl can and bottle). Maltina's direct competitor is Malta Guinness. Maltina competes favourably well with Malta Guinness in the market place as a result of the combined effects of its community events and successful brand differentiation strategy. Maltina sponsors the popular Maltina Dance all reality show and the Maltina sharing happiness promo.

Amstel Malta

Amstel Malta is a low sugar malt drink that caters to a more health conscious consumer. It is packaged in a 33cl can and bottle to better suit consumers' needs. Amstel has no direct substitute within the Nigerian market. Amstel Malta continues to increase brand reach and consumer engagement through the Amstel Malta Showtime sponsorship platform.

Legend Extra Stout

Legend extra stout faces stiff competition from the more dominant player, Guinness extra smooth in the stout industry. Guinness extra smooth is the leader in the sector as it enjoys greater brand recognition and consumer affinity.

6.0 Analysis & Recommendation

Our analysis was based on Nigerian Breweries' Group Account for the period ended 12 months December 31, 2011 compared with 12 months, December 31, 2010. For the computation of CAGR, the base period is 2007.

6.1 Capital Structure

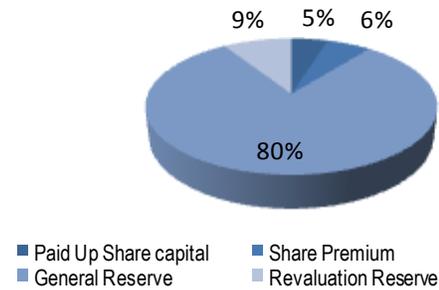
Total shareholders' fund of Nigerian Breweries grew to **N78.07bn** in 2011 from N50.17bn in 2010, translating to an increase of 55.60% over the period. The increase in total shareholders' fund was primarily driven by 80.26% growth in retained earnings from N34.73bn in 2010 to

N62.61bn in 2011. The growth in the retained earnings was as a result of the improved performance in the bottom line recorded during the period. The Compound Annual Growth Rate (CAGR) in the total shareholders' funds between 2007 and 2011 stood at 15.95%. The long-term assets of Nigerian Breweries stood at **N153.14bn** in 2011, up from N74.11bn in 2010 and representing growth of 106.65%. The growth in the long term asset was principally driven by the N50bn goodwill arising from the acquisition of Sona System and Life Breweries. The CAGR between 2007 and 2011 stood at 31.89%.

The current assets increased by 56.97% to **N63.24bn** in 2011 from N40.28bn in 2010 on account of a sharp increase in bank and cash balances, which increased by 73.52% to **N21.88bn** in 2011 from N12.61bn in 2010 and other debtor and prepayments which rose by 96.92% to **N12.69bn** in 2011 from N6.45bn in

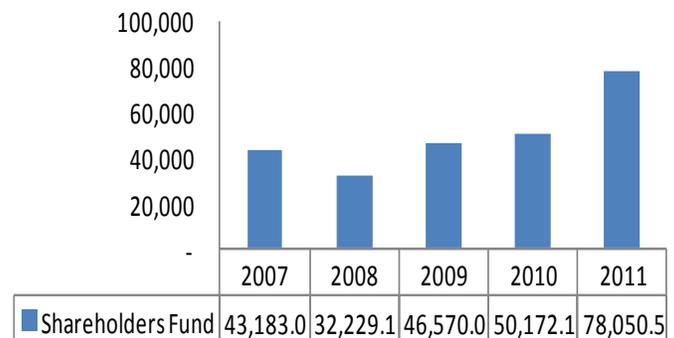
2010. Advances and prepayments rose by 96.91% to **N1.30bn** in 2011 from N660mn in 2010 while Stock also increased by 29.68% to **N27.53bn** in 2011 from N21.23bn in 2010. The stock comprises raw materials, products-in-process and finished goods, returnable packaging materials, non-returnable

Composition of Shareholders Fund (2011)

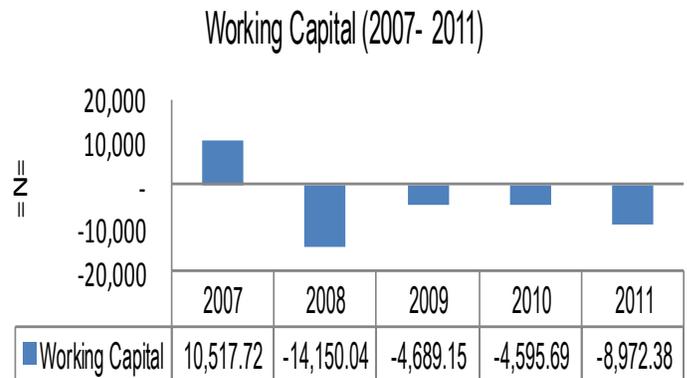


Total shareholders' fund of Nigerian Breweries grew to N78.07bn in 2011 from N50.17bn in 2010, translating to an increase of 55.60% over the period.

Shareholders Fund (2007-2011) N'mn



packaging materials, sundry materials and stock in transit, in the proportions **23.56%**, **14.27%**, **20.87%**, **15.04%**, **14.42%** and **11.85%** respectively. However, other debtors decreased by 32.03% to **N1.56bn**, from N2.29bn in 2010. Adding the long-term assets and the current assets together, the total assets grew by 89.15% to **N216.37bn** in 2011 from N114.39bn in 2010. The CAGR between 2007 and 2011 stood at 24.33%.



Net current liabilities stood at N8.97bn at the end of December 2011, an increase of 95.23% from net current liabilities of N4.60bn as at the end of the previous year.

As at December 2011, the total assets of Nigerian Breweries stood at **N216.37bn**, while total liabilities stood at **N138.31bn**. The short-term liabilities stood at **N72.21bn**, accounting for 52.21% of the total liabilities, while the long-term liabilities stood at **N66.10bn** accounting for 47.79% of the total liabilities. Its long-term liabilities are deferred taxation, staff gratuity & long service awards and long term debt representing 32.12%, 10.39% and 57.49% of long term liabilities respectively. The company recorded decline in its working capital, as a result of an increase in current liabilities over the current assets. Net current liabilities stood at **N8.97bn** at the end of December 2011, an increase of 95.23% from net current liabilities of N4.60bn as at the end of the previous year.

The capital employed (i.e. total assets less current liabilities) increased from N61.78bn in 2007 to **N144.16bn** in 2011, representing a CAGR of 23.92%, and achieved a growth of 107.40% between 2010 and 2011. The debt ratio, which is the proportion of the company's total assets that is financed by long term and short term liabilities increased marginally to **63.92%** in 2011 from 56.14% in 2010.

6.2 Liquidity

The company's current assets increased from N39.93bn in 2007 to **N63.24bn** in 2011, representing a CAGR of 12.18% and an increase of 56.97% between 2010 and 2011. Current liabilities increased from N29.41bn in 2007 to **N72.21bn** in 2011, representing a CAGR of 25.17% over the period and an increase of 60.89% between 2010 and 2011. The major contributors to the increase in current liabilities between the most recent two years are the amount due to related companies (up by 44.23% to **N30.80bn**) Other Creditors and Accruals (up by 14.54% to **N5.23bn**) and taxation (Up by 40.76% to N19.92bn).

The relationship between the current assets and current liabilities reflects a concurrent rise in current liabilities and current assets, but with the current assets increasing at a lower rate than the current liabilities, between 2010 and 2011. Consequently, the current ratio decreased marginally to **0.88x** in

2011 from 0.90x in 2010. The quick ratio however increased to 0.49x in 2011, from 0.42x in 2010. The net cash generated from operating activities increased by 15.00% from N39.15bn in 2010 to N45.93bn in 2011. Net cash used for investing

activities increased from N11.61bn in 2010 to N72.16bn in 2011 primarily due to the huge cash outlay used in the acquisition of the subsidiary companies. Net cash outflow from financing activities increased from an outflow of N26.34bn in 2010 to a net

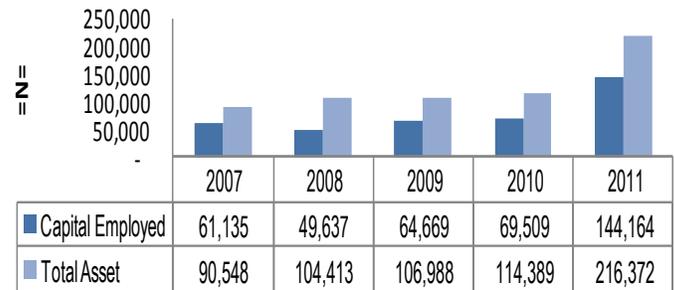
inflow of N35.49bn in 2011. The increase in cash inflow is attributed to the loan term agreement Nigerian Breweries entered with six Nigerian banks to finance its working capital. In the years 2010 and 2011, a net increase of N1.2bn and N9.26bn in cash and cash equivalents respectively; were recorded. Therefore, cash and cash equivalents, as at December 31 2011, stood at **N21.77bn**, representing an increase of 42.52% over the N12.51bn recorded at the end of 2010.

6.3 Profitability

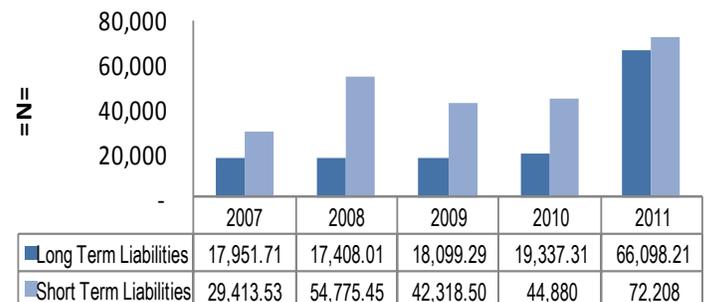
Despite challenging business climate, with increased competition from other players in the industry, particularly Guinness Nigeria Plc, Nigerian Breweries was able to maintain its leadership position as well as boost its revenue and deliver good returns to all stakeholders of the company. Turnover increased from N111.75bn in 2007 to N230.12bn in 2011, representing a CAGR of 19.79% and increased by 23.81% between 2010 and 2011. The growth in turnover was primarily as a result of major improvements to the company's supply structure, increased investment in the company's brands and capacity expansion.

Nigerian Breweries Plc maintained its leadership position in the industry and boosts its revenue.

Capital Employed vs Total Asset (2007 - 2011)



Long Term vs. Short Term Liabilities (2007-2011), N'bn



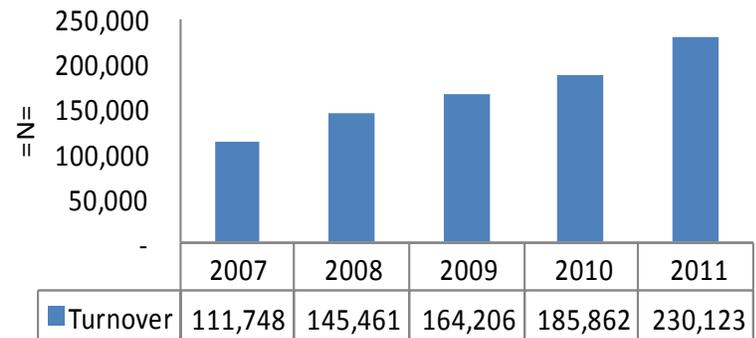
The cost of sales increased by 21.95% from N98.69bn in 2010 to N120.36bn in 2011, slightly lower than the growth in turnover 23.81%, leading to a growth of 25.92% in Gross Profit (GP), from N87.17bn in 2010 to N109.72bn in 2011. Selling & Distribution expenses increased

by 25.88% to N33.02bn in 2011 from N26.23bn in 2010, while Administrative expenses less depreciation increased by 34.60% to N12.42bn, from N9.23bn in 2010. The selling and distribution expense was buoyed by the several activities the company embarked on to boost sales.

Depreciation rose by 14.54% between 2010 and 2011. Earnings Before Interest, Tax, Depreciation and Amortization (EBITDA), increased by 24.44% from N51.97bn in 2010 to N64.67bn in 2011, while Earnings Before Interest and Tax (EBIT) increased by 25.98% from N44.97bn in 2010 to N56.65bn in 2011. Over the last five years EBITDA & EBIT recorded a CAGR of 18.44% and 19.96% respectively. The growth potential of Nigerian Breweries was limited, during the year under review, by the crude state of infrastructure (most notably, an intermittent power supply and a deficient transport network) in Nigeria and by the poor state of the country's finance environment. However, its Profit Before Tax rose from N44.88bn in 2010 to N56.37bn in 2011, representing a growth of

25.61% and a CAGR of 19.25% between 2007 and 2010. PAT stood at N38.03bn in 2011 from N30.33bn in 2010, representing a growth of 25.36%.

Turnover (2006 - 2011), N'mn



PBT vs. EBITDA (2007 - 2011), N'bn

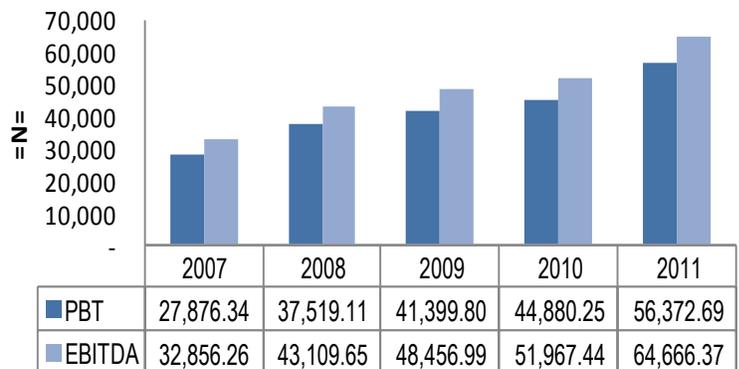


Table 5: Profit & Loss Account (N'mn)

	2011	2010	Change (%)	2009	2008	2007	CAGR (%)
Turnover	230,123	185,863	23.81	164,207	145,462	111,748	19.79
Cost of Sales	120,361	98,695	21.95	87,178	74,562	52,564	23.01
Gross Profit	109,762	87,168	25.92	77,029	70,900	59,184	16.70
Operating Profit	56,648	44,967	25.98	41,662	36,778	27,357	19.96
EBITDA	64,666	51,967	24.44	48,457	43,110	32,856	18.44
PBT	56,373	44,880	25.61	41,400	37,519	27,876	19.25
Tax	18,347	14,548	26.11	13,490	11,819	8,933	19.71
PAT	38,026	30,332	25.36	27,910	25,701	18,943	19.03

Balance Sheet (2007-2011), N'mn

	2011	2010	Change (%)	2009	2008	2007	CAGR (%)
Fixed Assets	98,428	73,800	35.35	69,003	63,558	50,195	18.34
Current Assets	63,235	40,284	56.97	37,629	40,643	39,931	12.18
Total Assets	216,372	114,389	89.15	106,988	104,431	90,548	24.33
Current Liabilities	72,207	44,880	60.89	42,319	54,775	29,414	25.17
Long Term Liabilities	66,098	19,337	241.82	18,099	17,408	17,952	38.52
Total Liabilities	138,306	64,217	115.37	60,418	72,183	47,365	30.72
Working Capital	(8,972)	(4,596)	95.23	(4,869)	(14,132)	10,518	
Total Equity	78,066	50,172	55.60	46,570	32,229	43,183	15.95

Although the retention of large proportion of earnings in 2011 to enable it partly fund the acquisitions led to the drop in returns on equity of Nigerian Breweries, the historical performance of Nigerian Breweries, still shows good performance to equity holders. The return on equity fell from 60.46% in 2010 to 48.71% in 2011. The return on assets stood at 26.18%, down from 39.31% recorded in 2010. Return on capital employed also decreased, from 64.69% in 2010 to 39.29% in 2011. Nigerian Breweries' gross profit margin increased slightly to 47.70% in 2011, from 46.90% in 2010; the company's EBITDA margin and PBT margin also increased marginally to 28.10% and 24.50% in 2011 from 27.96% and 24.15% in 2010, respectively. However, the contribution of employee to the company's profitability decreased between 2010 and 2011, as PBT per employee fell to N18.48mn in 2011 from N19.62mn in 2010, while the total costs per employee decreased from N7.49mn in 2010 to N5.53mn in 2011.

	2011	2010	2009	2008	2007
Gross Profit Margin (%)	47.70	46.90	46.91	48.74	52.96
EBITDA Margin (%)	28.10	27.96	29.51	29.64	29.40
PBT Margin (%)	24.50	24.15	25.21	25.79	24.95
ROE (%)	48.71	60.46	59.93	79.74	43.87
ROCE (%)	39.29	64.69	64.42	74.07	44.75
Current Ratio (x)	0.88	0.90	0.89	0.74	1.36
Debt Ratio (%)	63.92	56.14	56.47	69.13	52.31
Long Term Debt to Equity (%)	48.68	-	-	-	-
Interest Cover(x)	(205.98)	(520.65)	(158.69)	49.62	52.68
EPS(N)	5.03	4.01	3.69	3.40	2.50
DPS(N)	1.25	3.54	1.80	4.85	1.59
Net Asset Per Share(N)	10.32	6.63	6.16	4.26	5.71

6.4 Management Efficiency

The number of times capital employed could generate revenue decreased from 2.67x in 2010 to 1.60x in 2011. We expect the ratio to improve as the economic fortunes of the country begin to improve. In addition, Nigerian Breweries' various initiatives, such as the expansion and modernization of plants, in addition to various acquisitions plan of the company.

The number of times capital employed could generate revenue decreased from 2.67x in 2010 to 1.60x in 2011

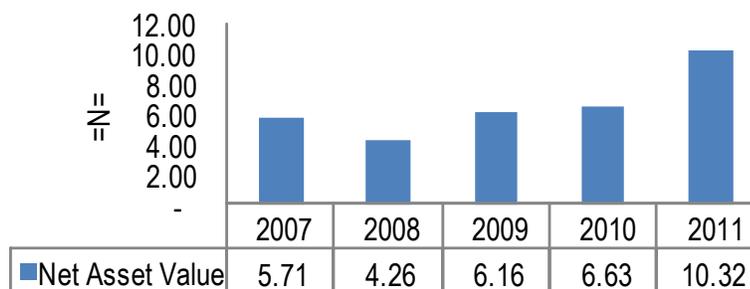
The Board of Nigerian Breweries is composed of members with established track records in their business endeavours. The diverse group of executive directors has varied experience from which to draw on and the exposure required to deliver superior value to their shareholders and positively impact other stakeholders.

6.5 Investment Analysis

The performance of Nigerian Breweries in the last five years have been impressive despite the harsh macroeconomic environment in which the company carried out its operations. The Earnings Per Share (EPS) increased by 25.36% between 2010 and 2011, rising from N4.01 in 2010 to N5.03 in 2011. The company paid a Dividend Per Share (DPS) of N3.00 to its shareholders for the year ended December 31, 2011. The DPS increased between 2010 and 2011, growing by 25% and reflecting the company's desire to reward shareholders as Nigerian Breweries begins to reap the benefits of their expansionary efforts. The average dividend payout in the last five years is 84%. The net assets per share (NAPS) increased from N6.63k in 2010 to N10.32k in 2011, representing a growth of 55% between the two years and a CAGR of 15.95% between 2007 and 2011.

The performance of Nigerian Breweries in the last five years have been impressive despite the harsh macroeconomic environment in which the company carried out its operations

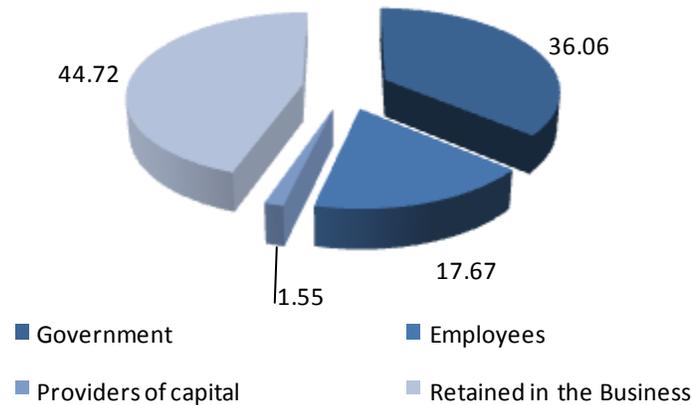
Net Asset Value (2007 - 2011)



6.6 Value Added Distribution

The wealth created by the efforts of the company’s employees stood at **N103.70bn** in 2011 from N83.66bn in 2010, representing a growth of 23.96%.The value added was distributed amongst the **government, employees, providers of capital and retained for expansion**, in the proportion of **36%, 18%, 2% and 45%** respectively.

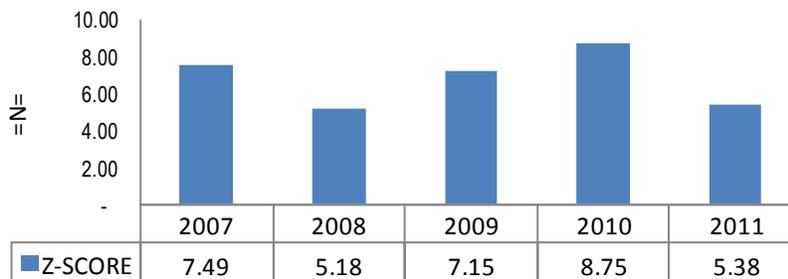
Distribution of Value Added (2011)



7.0 Bankruptcy Test – Altman Z- Score Model

We used the Z-Score model developed by Edward Altman to determine the probability of Nigerian Breweries going into bankruptcy within 2 years from December, 2011. The result of the test shows that the company scores a rating of 5.38, meaning that it is a safe company for all stakeholders based on the published financial for the period ended December, 2011. The 5-year Z-Score is presented on the table and chart below.

Z-SCORE (2007 - 2011)



Nigerian Breweries is a safe company for all stakeholders, based on 2011 Published Account.

	2011	2010	2009	2008	2007
OPBIT/Total Assets	0.26	0.39	0.39	0.35	0.30
Net Working Capital/Total Assets	(0.04)	(0.04)	(0.04)	(0.14)	0.12
Sales/Total Assets	1.06	1.62	1.53	1.39	1.23
Market Value of Equity/Total Liabilities	5.16	9.08	6.64	4.28	7.82
Accumulated Retained Earnings/Total Assets	0.29	0.30	0.29	0.16	0.30
Share Price (December)	94.42	77.10	53.02	40.85	49.00
Market Value of Equity	714,057	583,074	400,967	306,931	370,566
Z-Score	5.38	8.75	7.15	5.18	7.49

8.0 Q2 2012 Unaudited Result Update

The unaudited Q2, result of Nigerian Breweries Plc (NB) for the period ended June 31, 2012 showed that its Turnover (TO) increased by 23.90% to N136.51bn, compared with N110.20bn in the corresponding period of 2011

The unaudited Q2, result of **Nigerian Breweries Plc (NB)** for the period ended June 31, 2012 showed that its Turnover (T/O) increased by **23.90%** to **N136.51bn**, compared with N110.20bn in the corresponding period of 2011. The recent production expansion and aggressive marketing have helped turnover. Profit Before Tax (PBT) increased by 1.2% between Q2 2011 and 2012 to **N28.53bn**. The company made a tax provision of **N9.15bn** in Q2 2012, compared with N9.22bn in the corresponding period of 2011 leading to a marginal 2.2% increase in the company's Profit After Tax (PAT), which stood at N19.38bn in 2012, compared to N18.96bn in 2011. Meanwhile, we note that the strong growth in the topline did not trickle down to the bottom line due to foreign exchange losses and some restructuring expenses from the recent acquisitions.

The company's profit margins recorded mixed performance during the review period. The PBT margin decreased marginally to 20.90% in Q2 2012 from 25.57% as at Q2 2011 and from 24.50% as at the end of the financial year in December 2011. This shows that the company's total costs as a percentage of T/O stood at 79.10%, higher than 74.43% recorded in the corresponding period of 2011. PAT Margin stood at 14.20%, down from 17.20% in the corresponding period of 2011, and down from 16.52% as at FY 2011. The results also indicate that the T/O, PBT, and PAT in the Q2 2012 compared with the Full Year Audited T/O, PBT and PAT for the period ended December 2011 are 59.32%, 50.60% and 62.78%, respectively. Given the run rate, the company should be able to meet and surpass its previous year's topline and bottom line.

A cursory look at the balance sheet position as at Q2 2012 compared with the position as at full year December 2011 shows that the company's fixed assets increased during the review period. Its fixed assets increased by 3.18% to N123.23bn from N119.43bn in FY 2011. Stock decreased by 7.01% to N20.85bn in Q2 2012 from N22.42bn in FY 2011.

Cash and bank balances decreased, from N21.88 in FY 2011 to N4.50bn in Q2 2012. Working capital declined from a negative position of N22.88bn in FY 2011 to a negative position of N30.61bn in Q2 2011. The net assets decreased by 5.11% to N72.64bn in Q2 2011, from N76.56bn as at FY 2011.

9.0 Historical Return Analysis

An analysis of the historical return on the investment in the Ordinary Shares of Nigerian Breweries between January 2007 and September 05, 2012 revealed that the stock is a defensive stock. The total return during the period was made up of dividend payments that investors enjoyed on their investments and capital appreciation on the share price. Nigerian Breweries has been consistent in the payment of dividend, with an average dividend payment of N3.00 over the past five years.

Investment in the shares of Nigerian Breweries between 2007 and 2012 produced a total return of 263.98%

Our illustration using **N100,000** initial investment in January 2007 swelled to **N363,981** as a result of dividend earned and an increase in stock price. This resulted in a profit of **N263,981** and a return of **263.98%**. The number of shares the initial investment bought, net of transaction costs, was **2,666** units. The total dividend earned during the period was **N36,063**; no bonuses were issued. The share price appreciated by **241.67%**, from **N36.00** at the beginning of January 2007 to **N123** as at September 05, 2012

10.0 Valuation

10.1 Our Valuation Forecast Drivers

We considered the following factors in arriving at the forecasts we used for the valuation:

- Capacity expansion of the company, which was completed late 2011
- Acquisition of brewery firms which have excess capacity
- Growing demand for both non-alcoholic and alcoholic drinks in Nigeria
- Modernisation of plants, which will improve efficiency
- Investment in the development of high quality sorghum
- Enjoys economies of scale

Meanwhile, the major risk for its business is the crisis in some parts of the country leading to the closure of one of its plants. In arriving at a fair value for the ordinary shares of Nigerian Breweries, we used two variants of the Relative Valuation Method which are EV/EBITDA Multiple and P/E Multiple. We estimated **T/O**, **EBITDA** and **PAT** for December 2012. We project **T/O** of **N295. 24bn** representing a revenue growth rate of **28%** over 2011. We estimate EBITDA of **N98.97bn** using a growth rate of **33.52%**. We project **PAT** of **N46.80bn** based on a PAT margin of **15.85%**.

The estimated Forward Earnings Per Share (**FEPS**) generates **N6.19**. Applying Enterprise Value EV/EBITDA multiple of **10.01x**, a P/E multiple of **20.04x**, we arrived at **N126.03** per share using EV/EBITDA multiple and **N126.23** per share using price earnings multiple. A simple average of the two valuation methods gives a value of **N126.13** per share, which is our fair value. The highest and the lowest closing price of Nigerian Breweries since the beginning of the year 2012 are **N123.00** and **N91.10** respectively.

Our forecast forward 2012 EPS is N6.19 using a dividend payout ratio of 84%, we have a DPS of N5.18. The 2012 forward earnings yield will be 4.91% while the 2012 dividend yield will be 4.11%. The current share price only has about 6.5% upside potentials both in terms of dividend payment and capital appreciation to the fair value. Therefore our current rating on Nigerian Breweries to the current market price is a **HOLD**.

Table 8 :Valuation Summary

Method	Multiple	Result
EV/EBITDA Multiple	10.01x	126.03
P/E Multiple	20.4x	126.23
Simple Average/Fair value		126.13

Table 9: FSDH Research Earnings Forecast for Nigerian Breweries (2012-2016)

	Dec-12	Dec-13	Dec-14	Dec-15	Dec-16
Turnover(N'mn)	295,243	369,054	452,091	547,030	650,966
EBIT(N'mn)	90,767	118,995	145,768	176,380	200,127
EBITDA(N'mn)	98,970	127,345	154,251	184,995	208,875
PBT(N'mn)	68,817.68	91,449.36	112,025.46	136,757.49	157,954.91
Tax(N'mn)	-22,022	-29,264	-35,848	-43,762	-50,546
PAT(N'mn)	46,796.02	62,185.56	76,177.32	92,995.10	107,409.34
Dividend Payment(N' mn)	39,206.22	52,099.75	63,822.19	77,912.31	89,988.72
EBIT Margin (%)	30.74%	32.24%	32.24%	32.24%	30.74%
EBITDA Margin (%)	33.52%	34.51%	34.12%	33.82%	32.09%
PBT Margin (%)	23.31%	24.78%	24.78%	25.00%	24.26%
PAT Margin (%)	15.85%	16.85%	16.85%	17.00%	16.50%
EPS(N)	6.19	8.22	10.07	12.30	14.20
DPS(N)	5.18	6.89	8.44	10.30	11.90
Earnings Yield (%)	4.91%	6.52%	7.99%	9.75%	11.26%
Dividend Yield (%)	4.11%	5.46%	6.69%	8.17%	9.43%
P/E Ratio(x)	20.38	15.34	12.52	10.26	8.88
Number of Shares(mn)	7,562.70	7,562.70	7,562.70	7,562.70	7,562.70
Dividend Payout (%)	83.78%	83.78%	83.78%	83.78%	83.78%

Table 10: Annual Capital Growth & Returns Analysis of N100,000 Investment in Nigerian Breweries Plc since January 03, 2007

Value Receipt Period	2007	2008	2009	2010	2011	2012	Total
Holding As At January	2,666	2,666	2,666	2,666	2,666	2,666	
Bonus Shares Received	-	-	-	-	-	-	-
Cumulated Holding	2,666	2,666	2,666	2,666	2,666	2,666	
Dividend Earned	3,815	9,238	4,319	8,494	2,999	7,198	36,063
	05-09-12						
Accumulated Shareholding	2,666						
Increase in Shareholding (%)	0.00						
Price (N)	123						
Market Value (N)	327,918						
Total Dividend (N)	36,062.98						
Value of Investment (N)	363,980.98						
Cost of Investment (N)	100,000						
Profit (N)	263,980.98						
% Increase	263.98						

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