



Member of Uganda Securities Exchange
Regulated by the Capital Markets Authority

DFCU LIMITED RESEARCH NOTE

The Company

- Incorporated in 1964, DFCU Limited, as a company provides long term and mortgage finance. It is also the Holding Company of the following subsidiaries with which DFCU Limited are all collectively referred to as the DFCU Group:
 - DFCU Leasing Company Limited – 100%
 - DFCU Bank Limited – 100%
 - Rwenzori Properties Limited – 62.67%
 - Nakasero Properties Limited – 62.66%

DFCU Limited also holds equity investments in:

- Rwenzori Courts Limited – 16.45% and
- Centenary Rural Development Bank – 17.40%

Share Capital

- As at 31 December 2003, the total authorised number of ordinary shares was 250,000,000 with a par value of Ushs 20 per share. Issued and fully paid up shares are 198,880,729.

| | Ushs. |
|--|---------------|
| Authorised Share Capital 250,000,000 ordinary shares of Ushs 20 each | 5,000,000,000 |
| Issued and Fully Paid Up Share Capital 198,880,729 ordinary shares of Ushs 20 each | 3,977,614,580 |

Source: DFCU Limited

Shareholding structure

- DFCU is currently owned 60.03% by CDC Group plc, 21.5% by the IFC, an affiliate company of the World Bank, and 18.47% by GoU. After the Offer, the shareholding is expected to be 60.03% for CDC Group plc and 39.97% for the general public and institutional investors, both local and foreign. The GoU and IFC are both expected to offload their shares at the IPO.

| Shareholders | Number of Shares | 2003 % | 2002 % |
|---|------------------|---------|---------|
| CDC Group plc | 119,370,986 | 60.03% | 35.30% |
| DEG | - | - | 24.70% |
| International Finance Corporation (IFC) | 42,766,813 | 21.50% | 21.50% |
| Government of Uganda (GoU) – Uganda Development Corporation | 36,742,930 | 18.47% | 18.50% |
| | 198,880,729 | 100.00% | 100.00% |

Source: DFCU Limited

| FINANCIAL RATIOS | | | | |
|-------------------|--------|--------|--------|--------|
| December | 2000 | 2001 | 2002 | 2003 |
| EPS | 15.60 | 31.60 | 30.69 | 42.34 |
| DPS | 8.01 | 10.50 | 15.08 | 21.62 |
| ROA % | 4 | 6 | 4 | 5 |
| ROE% | 16 | 28 | 21 | 24 |
| NAV | 104.13 | 125.40 | 166.57 | 192.76 |
| Cost/Income Ratio | 53 | 53 | 59 | 46 |
| | | | | |

Source: DFCU Limited Audited Financials

Note: Past performance is not necessarily an indication of future performance

The Offer

- Up to 79,509,743 ordinary shares are being offered to the public. These shares include 36,742,930 from the GoU and 42,766,813 from the IFC. The offer is expected to open for a period of 5 weeks before 30 June 2004, following receipt of the requisite approvals from the Capital Markets Authority (CMA) and Uganda Securities Exchange (USE) and the Registrar of Companies.

Listing on the Uganda Securities Exchange (USE)

- Listing on the USE is expected to take place in August 2004.

Government of Uganda Divestiture Program

- The GoU's main objective of divestiture is to reduce the direct role of Government in the Ugandan economy and promote a correspondingly greater role for the private sector in order to increase efficiency in production and delivery of services and hence more sustainable institutions.
- Governed by the Public Enterprise Reform and Divestiture (PERD) Statute of 1993, DFCU Limited was listed in Class 4 of the Statute (whereby the Government of Uganda (GoU) is required to fully divest its interest in a company). A decision was made by the Divestiture and Reform Implementation Committee (DRIC) (as established by the above PERD Statute) that 36,742,930 shares of Government held shares were to be sold to the public and Company employees and that the Company be listed on the USE.

Nature of Business

- The DFCU Group provides commercial banking, equity, lease finance, term finance and mortgage finance. The Group also has a stake in various investment properties that earn rental income.

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▪ **Management and Employees**

The overall management of the business is vested in the Board of Directors, which is currently composed of 9 members. Each of the shareholders – CDC, IFC and GoU – has representatives on Board, 2 for CDC, 1 for IFC and two for GoU. There are 4 independent Board Members, including the Chairman and the Managing Director. There are 2 Alternate Directors, each representing GoU and CDC. The Board appoints the Managing Director, who is also a Board Member. The Board holds one annual general meeting, and such other meetings as may be necessary for the business.

The Group has 211 permanent and 8 temporary members of staff allocated as follows:

| DFCU Business Unit | Permanent Employees | Temporary Employees |
|------------------------------------|---------------------|---------------------|
| Bank | 135 | 3 |
| Leasing | 30 | 1 |
| Limited | 31 | 2 |
| | | |
| Rwenzori Properties Limited | 15 | - |
| Total | 211 | 6 |

Source: DFCU Limited

Risk factors and Investment considerations

- The significant risk factors affecting DFCU as a financial institution are enumerated below:

Monetary policy:

Decline in interest rates on risk free Government securities due to tightening of monetary policy and the issuance of longer dated Government paper by BoU. This has the effect of reducing interest income on Government securities as well as the prime-lending rate of the Bank

Interest Rate Risk:

Typically, banks are more exposed to downward trends in interest rates as the spreads between what they pay on customer deposits and what they lend out is narrowed. Also a certain percentage of bank funding will be interest free (current accounts) and when rates fall the net interest income reduces.

Funding and Liquidity Risk:

The Group relies on three principal sources of liquidity; deposits from customers, borrowings from multilateral

financial institutions and repayments of loans granted to customers. There can be no assurance that its business, which is to a certain extent subject to general economic and financial factors will generate enough revenues from

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operations to enable it meet its obligations nor that its existing financing arrangements will continue to render it able to respond to changes in general economic conditions.

Credit Risk:

The Group’s cashflow is subject to risks from non-performance by its customers on their loan risk obligations. Customers may default on their loan obligations to the Group due to bankruptcy, lack of liquidity, operational failure or other factors that are beyond the Group’s control. The foregoing could materially impact the Group’s operations.

Operational Risk:

The Group faces operational risk arising from errors in the processing of transactions, frauds related to unauthorised payments or disbursements and failure to properly record, account and evaluate transactions. No assurance can be given that such exposure will not result in customers and /or cause a disruption in the Group’s business, resulting in reduction in net revenue.

Competition

The market for financial and banking services in Uganda has become increasingly competitive over the years. Competitors may seek to increase market share more aggressively, which could result in a material adverse effect on the Group’s lending revenues, fees and commissions.

Regulatory:

The BoU could demand reductions or abolitions in certain tariffs thereby reducing Bank Income.

Legal Risk:

Although there are pending litigation claims against DFCU Limited, DFCU Leasing and DFCU Bank, the companies have a strong defense against the suits.

The Group

- *DFCU Limited*

DFCU Limited has been in existence since 14 May 1964 and is the parent company of the DFCU Group. It was started by the CDC of the United Kingdom and GoU under the name of Development Finance Company of Uganda Limited to support long term development projects whose financing needs and risk did not appeal to the then existing financial/commercial lending institutions.

The Company is a leading financial institution, which provides term finance and mortgage finance.

Through its subsidiaries, it provides for commercial banking services, equity, lease finance, and letting out property for the development of business in Uganda. Of

the services provided by the DFCU Group, term finance is the founding and longest business activity of the Group.

The Mortgage business was commenced by DFCU Limited indirectly through its investment in the Housing Finance Company of Uganda (HFCU) in 1984. (from which it divested in 2003). The Company then commenced its own direct mortgage business in July 2002. The portfolio has since grown to Ushs 12 billion at the end of 2003 and Ushs 13.4 billion as at February 2004.

- **DFCU Leasing Limited**

In July 1999, DFCU Limited acquired 100% shares in the Uganda Leasing Company Limited (ULC) which was incorporated in 1994 by the Commonwealth Development Corporation Limited (CDC) and the Government of Uganda.

ULC was the first independent leasing company in Uganda, set up to provide alternative medium term equipment financing to the private sector. Two other institutions, EADB and KTU Leasing followed suit in the late nineties with the later closing down its operations in 2001.

The shareholding was then restructured that same year to become part of the DFCU Group and was provided with substantial funding. Before this, ULC was cash strapped and unable to effectively meet the increasing demand for leasing products.

- **DFCU Bank Limited**

In May 2000, DFCU Limited bought out the share capital of Gold Trust Bank, which subsequently changed its name to become DFCU Bank Limited.

The bank with 12,000 customers and 27,000 accounts as at 31 December 2003, is now one of the fastest growing commercial banks in the country with 8 branches countrywide located in Masaka, Lira, Arua and Kampala .

- **Rwenzori Properties Limited/Nakasero Properties Limited**
These subsidiaries are investments in property companies held to earn rental income.

In December 2003, the properties were valued at a total of US\$ 13.5 billion or approximately USD 7.1 million by Knight Frank Chartered Surveyors on the basis of open market value.

The Branches

- Only the Leasing and Banking arms of the Group operate countrywide branches;

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| | Branch/Centres | Bank | Leasing |
|---|----------------|------|---------|
| 1 | Kampala (3) | Bank | - |
| 2 | Lira | Bank | Leasing |
| 3 | Arua | Bank | - |
| 4 | Hoima | -- | Leasing |
| 5 | Masaka | Bank | - |
| 6 | Mbale | - | Leasing |
| 7 | Mbarara | - | Leasing |

Source: DFCU Bank Limited and DFCU Leasing Limited

Source of Funds

- **Leasing**

Funding for Lease financing comes mainly from several developmental partners from which DFCU Leasing borrows for onward lending to the private sector e.g. EIB, FMO, KFW, OPEC, DEG and DFCU Limited.

- **Mortgage Finance**

Over Ushs 20 billion has been made available by the developmental partners including the NSSF, FMO, and OPEC to supplement the Group's own resources, further more, DFCU is looking at securitizing its mortgage portfolio in the future in order to mobilise additional funding from the local market.

- **Term Finance**

The EIB Apex scheme is the main source of funding for Term Finance. DFCU Limited's projection of utility of the EIB funds to 2006, is projected be at least 50% of total disbursements. DFCU Limited has over the years increased its utilization levels of the EIB funds progressively, and is projected to maintain and improve on this trend. To date, DFCU is the largest single user of EIB Apex funds.

- **Banking**

Local banks, while are able to mobilise funds through the inter bank market rely heavily on customer deposits to fund their core activities e.g. lending.

The Products

- **Leasing**

- Financial Lease

This facility is targeted at Small and Medium sized Enterprises (SME's) in the private sector. Typical lease facilities range from USD 1,000 to USD 500,000 and apply to many sectors of the economy like transport, agribusiness, health, construction and education. Leasing facilities can be provided for two to five years.

- Operating Lease

Recently launched to provide 'off balance sheet' financing for large corporate customers, this facility allows the

lessees to make use of the asset without ownership and is based on the concept of “pay as you go”.

➤ **Insurance Premium Financing**

Using this facility, DFCU Leasing pays the client’s annual insurance premium directly to the underwriter, enabling the insured to obtain immediate cover. The premium can be repaid in convenient monthly instalments over a period of 6 to 10 months

▪ **Mortgage Finance**

The following products are currently offered under Mortgage and are based on the specific needs of the customer and the appropriateness of the nature of funding:

- **Owner- occupier Mortgages** – purchase, completion, renovation or furnishing of own homes
- **Buy to let Mortgages** – For acquisition of property to let out to tenants as an investment.
- **Equity release Mortgages** – Enables one to borrow against existing property to finance other needs.
- **Commercial and Industrial Mortgages** – For buying or construction of industrial or commercial buildings in specified urban centres. This is however selective owing to risks inherent in rentals presently.

The above products are available for periods of three to fifteen years at competitive rates. DFCU Limited currently provides approximately 70% of the value of the property in the form of a mortgage, while the customer is expected to make a 30% equity contribution.

▪ **Term Finance**

Term finance is targeted at the SME market and aims to provide medium to long-term development finance. The facility can be availed for periods of up to 10 years with an appropriate grace period.

A form of collateral is generally required to secure the loan, with the borrower contributing at least 10% of the project or investment cost.

▪ **Banking**

The bank’s core business is the accepting of deposits from the public and advancing of loans and overdrafts to customers on a sustainable basis.

The following table gives a profile of the Bank’s products:

| Credit Products | Deposit Products | Other Products |
|----------------------|------------------------|-----------------------------|
| Corporate loans | Forex & local deposits | Transaction services |
| Personal Loans | Demand deposits | Custodial services |
| Overdrafts | Time deposits | Remittances & drafts |
| Letters of guarantee | Savings deposits | Treasury services |
| Letters of credit | | Primary dealership |
| | | Financial advisory services |
| | | ATMs |
| | | International T.T.’s |

Source: DFCU Bank

Competition

▪ **Leasing**

According to statistics available at the Uganda Leasing Association, it is estimated that DFCU Leasing currently controls 80% market share in the industry. Its major competitors are East African Development Bank (EADB), Stanbic Bank Uganda Limited, a recent entrant, and some major motor vehicle vendors, which make up the balance of the market share. The Association expects the market will widen with new entrants, thereby increasing the number of players (both lessors and lessees) and the range of transactions handled through leasing.

▪ **Mortgage Finance**

The dominant players in the market of specialist mortgage providers are HFCU and DFCU Limited. As there is very little public information on Uganda’s mortgage market outside of HFCU and DFCU Limited, this market information below is limited to these two institutions.

As at the end of 2003, the total mortgage market in Uganda was worth approximately 55.35 Billion, of which HFCU had a mortgage book of Ushs 43.35 billion (78.3%), while DFCU Limited had a mortgage book of Ushs 12 billion (21.7%). Some Insurance companies, real estate developers, large corporate and other smaller players provide mortgages to their captive market, clientele or staff, as the case may be.

▪ **Term Finance**

There are relatively few financial institutions providing term finance in Uganda. Of this limited number, DFCU is one of the major providers. There is a growing number of SME’s, which require DFCU type of funding.

Of particular significance is the increasing number of new schools seeking funding for expansion as a result of the UPE programme and the support of the Government policy that is encouraging more private schools in the country. From the interest expressed by DFCU customers, it is

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evident that there is effective demand for term finance in Uganda, which points to the potential for portfolio growth in the future.

▪ **Banking**

There are 15 commercial banks in Uganda, of which the main players are Stanbic Bank, Standard Chartered Bank, Barclays Bank, Citibank, Bank of Baroda, Centenary Rural Development Bank (CERUDEB) and DFCU Bank. Stanbic Bank is the largest bank in the market with over 50 branch outlets countrywide and is estimated to have more than 30% market share. The International Banks that have for long concentrated on serving large corporates are now increasingly finding that market overcrowded and have begun to target SME's with dedicated sales and service teams.

▪ **Capital Expenditure**

- In 2002, the Board of Directors approved CAPEX projects in excess of USD 2.5 million for the year 2003. It is estimated that the Group CAPEX needs for 2004 are budgeted at approximately USD 3.1 million in order to invest in improved banking premises and new branches, advanced Informational Technology (IT) systems and innovative products. IT is expected to absorb at least USD 1.6 million with Furniture and refurbishment costs amounting to around USD 1.1 million.

▪ **Borrowing**

- As at 31st December 2003, the Group's borrowings amounting to Ushs 73.571 billion have been amassed under favourable terms, in the ordinary course of business from various local and international institutions for the purposes of onward lending to the Group's customers.

▪ **Dividend Policy**

- The Group has paid dividends consistently since 1999. The dividend policy has been to achieve a 30 - 35% payout ratio of Group distributable earnings for the year, which is subject to the Board of Directors approval and the financial needs of the Company. It is the Board's intention to increase the dividend payout ratio going forward, with 50% being paid in respect of 2003.

- The offer for sale of 79,509,743 ordinary shares of DFCU will be sold to the public on an ex--dividend basis.

▪ **Strategic Direction and future Prospects**

- Dfcu is the fastest growing financial services Group in Uganda. The strategic plan for the Group entails organic growth in existing markets (SME sector and middle income) via existing activities, while seeking to expand the retail customer base with particular emphasis on growing liabilities.

In order to maintain the robust growth while exploring new opportunities, Management has reviewed the Group's

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position vis-à-vis the competition and the macro-economic environment.

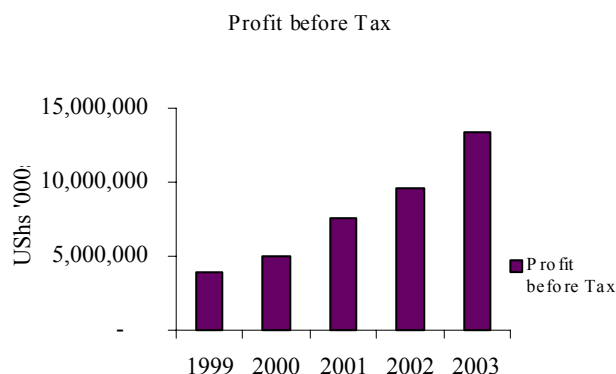
Economic conditions are not seen as an impediment to delivery against budget and forecasts but in an effort to eliminate operational efficiency, internal competition and duplication of costs, the Group in 2003, embarked on a bold organisational re-design to facilitate the attainability of the overall strategic objectives.

Upon completion of this re-design, it is believed that DFCU will have gained competitive advantage over its peers in the financial services sector through a more streamlined cost efficient operation.

To this end, the Management reviewed all internal processes with the express aim of creating an efficient operational environment, with enhanced risk management procedures. This was to be achieved by initially merging operationally, the business streams of Leasing, Term Finance and Mortgage and Banking while retaining the legal entities of the DFCU Group.

Performance

Profit before Tax grew by 236% from Ushs 3.97 billion in 1999 to Ushs 13.34 billion in 2003.

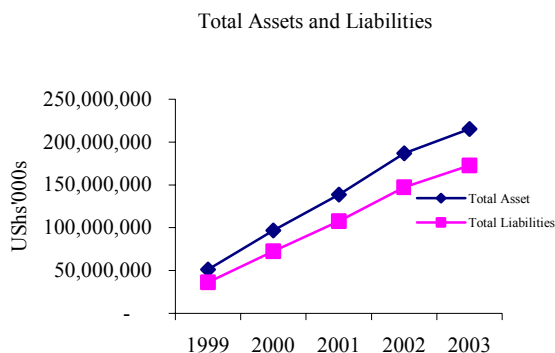


Source: DFCU Limited Audited Financials

Note: Past performance is not necessarily an indication of future performance

Total Assets and Liabilities.

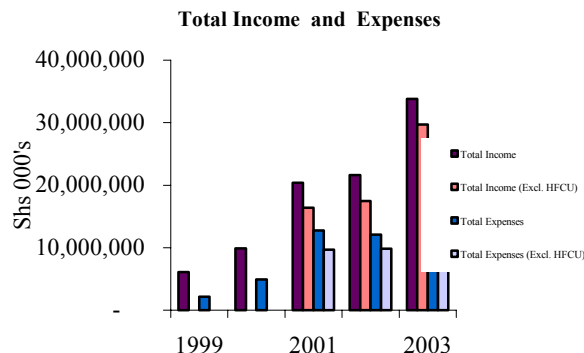
Total Assets grew 321% from Ushs 51.20 billion in 1999 to Ushs 215.38 billion in 2003, while Total Liabilities increased by 378% from Ushs 36.07 billion to Ushs 172.53 billion over the same period. The increase in Liabilities reflects both deposit growth which has driven the improving performance seen at DFCU Bank and increased wholesale funding which underpins the non-bank (i.e. Development Finance) activities of the Group.



Source: DFCU Limited Audited Financials

Note: HFCU is consolidated into the Group Balance Sheet for 2001 & 2002

Past performance is not necessarily an indication of future performance



Source: DFCU Limited Audited Financials

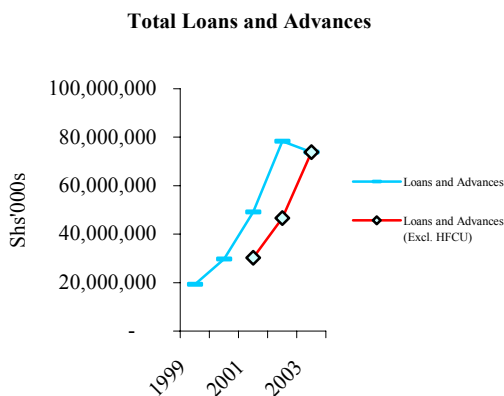
Note: Figures for 2003 reflect extraordinary income earned from the sale of DFCU Limited's equity interest in HFCU

HFCU is consolidated into the Group Profit and Loss Statement for 2001, 2002 & up to September 2003

Past performance is not necessarily an indication of future performance

Loans and Advances

Loans and Advances for the Group (including HFCU consolidated audited financials in 2002) grew 284% from Ushs 19.22 billion in 1999 to Ushs 73.86 billion in 2003. The decrease of 5.6% in 2002 – 2003 was due to the sale of DFCU's 50% holding in HFCU to the NSSF in September 2003. The Group (excluding HFCU) loans grew by 58.23% from Ushs 46.68 billion to Ushs 73.86 billion in the same period.



Source: DFCU Limited Audited Financials

Note: HFCU is consolidated into the Group Balance Sheet for 2001 & 2002

Past performance is not necessarily an indication of future performance

Total Income and Expenses.

Total Income grew 453% from Ushs 6.11 billion in 1999 to Ushs 33.79 billion in 2003. Total Expenses increased 856% from Ushs 2.14 billion to Ushs 20.46 billion over the same five year period. It should be noted that HFCU was consolidated into the Group's Profit and Loss Statement up to 30th September 2003.

Outlook and Recommendation

- The Ugandan economy is expected to maintain current growth in GDP levels of around 5%. The financial sector is also expected to register significant growth.
- While decreasing interest rates are expected to impact on interest income, we expect this to be more than compensated by increased number of potential customers who have been reluctant to borrow on account of the perceived high lending rates of over 25% which have prevailed in the last one year as they take advantage of lower lending rates to borrow as bank base lending rates begin moving downwards.
- With the new organisation structure to cut down on inefficiencies, enhanced risk management and marketing efforts and the brand image expected to be boosted by being listed on the USE, we expect the Group to improve on past performance in greater measure and 2004 should be a year of stronger earnings growth as the Group reaps the benefit of a better organised structure. Leasing, Term Finance and Mortgage Financing are all key growth areas in the entire East African region and are expected to contribute greatly to the bottom line.

RECOMMENDATION: Strong Buy

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Summary Financial Information

The tables below summarise the past Audited five year consolidated financial periods ended 31 December 2003. Key Financial Ratios have also been included.

Profit and loss account summary

| Figures in Ushs. '000s | 2003 | 2002 | 2001 | 2000 | 1999 |
|---|--------------|--------------|--------------|-------------|-------------|
| Net Interest Income | 15,930,269 | 12,109,251 | 9,716,942 | 5,072,473 | 2,160,427 |
| Fees and Commission Income | 6,006,881 | 5,092,787 | 4,174,836 | 1,465,384 | 529,368 |
| Other Income | 11,862,470 | 4,415,620 | 6,491,831 | 3,348,204 | 3,415,522 |
| Total Income | 33,799,620 | 21,617,658 | 20,383,609 | 9,886,061 | 6,105,317 |
| Operating Expenses | (16,094,667) | (12,815,418) | (10,887,151) | (5,303,588) | (2,669,882) |
| Non Operating Expenses | (4,366,642) | 738,840 | (1,862,933) | 411,040 | 534,365 |
| Profit Before Tax | 13,338,311 | 9,541,080 | 7,618,138 | 4,993,513 | 3,969,800 |
| Tax | (4,020,092) | (2,545,605) | (538,131) | (1,969,497) | (1,317,464) |
| Profit After Tax | 9,318,219 | 6,995,475 | 7,080,007 | 3,024,016 | 2,652,336 |
| Minority Interest | (897,332) | (892,312) | (809,908) | (104,386) | - |
| Net Profit Attributable to Shareholders | 8,420,887 | 6,103,163 | 6,270,099 | 2,919,630 | 2,652,336 |
| Earnings Per Share | 42.34 | 30.69 | 31.60 | 15.60 | 16.10 |
| Dividends per Share | 21.62 | 15.08 | 10.50 | 8.01 | 6.05 |

Source: DFCU Limited Audited Financials

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Balance sheet summary

| Figures in Ushs. '000s | 2003 | 2002 | 2001 | 2000 | 1999 |
|------------------------------|-------------|-------------|-------------|------------|------------|
| Total Assets | 215,376,776 | 186,911,379 | 137,590,132 | 96,949,394 | 51,206,511 |
| Total Liabilities | 172,525,916 | 147,188,599 | 107,443,684 | 72,499,252 | 36,066,870 |
| Minority Interest | 4,513,723 | 6,595,731 | 5,703,484 | 3,741,131 | - |
| Shareholders Equity | 38,337,137 | 33,127,049 | 24,442,964 | 20,709,011 | 15,139,641 |
| Total Equity and Liabilities | 215,376,776 | 186,911,379 | 138,627,107 | 96,949,394 | 51,206,511 |

Source: DFCU Limited Audited Financials

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Key financial ratios

| Figures in % | 2003 | 2002 | 2001 | 2000 | 1999 |
|--|--------|--------|--------|--------|-------|
| Cost to Income Ratio (excluding provisions) | 46 | 59 | 53 | 53 | 44 |
| Return on Average Assets | 5 | 4 | 6 | 4 | 6 |
| Return on Average Equity | 24 | 21 | 28 | 16 | 21 |
| Debt to Equity Ratio | 396 | 361 | 338 | 280 | 225 |
| Net Asset Value per Share | 192.76 | 166.57 | 125.40 | 104.13 | 82.50 |

Source: DFCU Limited Audited Financials

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Profit forecast

The forecast is made on the basis of August 2003 Management Accounts and is based on the best estimate assumptions of management for and on behalf of the Board of Directors, adopted by the Board.

| Figures in Ushs. '000's | As at 31 December 2004 |
|---|---------------------------|
| Net Interest Income | 18,632,769 |
| Fees and Commission Income | 7,080,718 |
| Other Income | 4,065,688 |
| Total Income | 29,779,175 |
| Total Expenses | (19,216,887) |
| Trading profit | 10,562,288 |
| Exceptional Item | 3,376,165 |
| Profit Before Tax | 13,938,453 |
| Tax | 4,335,690 |
| Profit After Tax | 9,602,764 |
| Minority Interest | 590,460 |
| Net Profit Attributable to Shareholders | 9,012,303 |
| Earnings Per Share | 48.28 |
| Dividends per Share | 15.86 |
| | |

Source: DFCU Limited

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“ SHARE PRICES CAN GO UP OR DOWN ”

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