SUMMARY OF PREVIOUS AUCTION

Marginal Rates:

12.75% APR 2023	10.00%
12.50% MAR 2035	12.50%
12.98% MAR 2050	12.98%

Amount:

12.75% APR 2023	5.00bn
12.50% MAR 2035	20.00bn
12.98% MAR 2050	25.00bn

SUMMARY OF CURRENT AUCTION

FGN APR 2023

Auction Date	22/04/2020
Settlement Date	24/04/2020
Maturity Date	24/04/2023
Next Coupon Date	27/04/2020
Clean Price	NGN108.97

FGN MAR 2035

Auction Date	22/04/2020
Settlement Date	24/04/2020
Maturity Date	24/04/2035
Next Coupon Date	23/09/2020
Clean Price	NGN109.53

FGN MAR 2050

Auction Date	22/04/2020
Settlement Date	24/04/2020
Maturity Date	24/04/2050
Next Coupon Date	27/09/2020
Clean Price	NGN102.91

FGN Bond Auction Scheduled 22nd April 2020

Issue on Offer/Summary

The Federal Government of Nigeria (FGN), through the Debt Management Office (DMO), will be conducting a bond auction on Wednesday 22nd April 2020. The total amount on offer is expected to be NGN60bn and all three (3) instruments on offer are re-openings.

12.75% FGN APR 2023	**NGN20bn**
12.50% FGN MAR 2035	**NGN20bn**
12.98% FGN MAR 2050	**NGN20bn**

Current Yield Analysis

Investors maintained a strong appetite for FGN bonds at the last primary market auction (PMA) with bid-to-cover ratios of 4.21x, 3.45x and 3.65x on the **12.75% APR 2023, 12.50% MAR 2035** and **12.98% MAR 2050** instruments respectively.This was in spite of heightened inflationary risks, coupled with a generally depressed yield environment which pushed average real rates of return on FGN bonds into negative territory (February 2020: -1.45%).

Bullish sentiment have also dominated the secondary bonds market since the last PMA as average yields declined from 10.38% (as at last PMA) to 9.98% as at 17th April 2020. We believe that the contraction in yields is induced by the demand for less risky assets in the wake of the outbreak of COVID-19.

On the domestic front, the outlook remains dampened, with oil prices falling to historic lows and the pandemic spreading further. Despite the historic 9.70mbpd supply cut deal reached by major global suppliers of crude oil, Brent prices have fallen by 58.97% since the start of the year, reaching a low point of USD27.08pb, as global storage nears capacity. The implications for revenues accruing to the FGN are not far-fetched. With a budget hinged on crude oil price at USD30pb, revenue shortfalls and a significant increase in deficits can be expected. Non-oil revenues which include VAT, income taxes, customs and excise duties are also expected to fall below expectations as the spread of the pandemic has forced a slowdown in economic activity around the country. A weak government revenue outlook is considered a key risk element which investors may factor into bid rates at the next auction.

With oil prices at extremely low points, expected government revenue is poised to fall short and a slowdown in economic activity with no target date for a pickup in sight, risks associated with Nigeria are expected to be much higher in this period. Nevertheless, we expect strong investor participation in the next bond auction given the paucity of investment options available. We however opine that higher rates would be required by investors to compensate for growing risks.

Bond Absolute and Relative Valuation

We analysed the issues on offer given the current yield environment, market liquidity, as well as a review of the recent past auctions, whilst also introducing market sentiment factor into our valuation, on which we advise bid yield ranges for both issues on offer.

Our advised rates for the instruments on offer are stated below;

Tenor	Offer Size	Advised Rates
12.75% FGN APR 2023	NGN20bn	**9.00% - 9.40%**
12.50% FGN MAR 2035	NGN20bn	**12.10% - 12.30%**
12.98% FGN MAR 2050	NGN20bn	**12.40% - 12.75%**

About Bonds

A bond is a fixed income debt instrument issued by the government (federal or state government) or corporate institutions with a definite date of maturity and a fixed interest payment (known as coupon) payable either semi-annually or annually. Unlike equities, bonds are issued with a guarantee of the initial investment and can have tenors as long as 20 years.

A treasury note refers to a government bond instrument with a term to maturity of 1 to 10 years while a treasury bond has a maturity of 10 years and above. Bonds issued by state governments of a country are referred to as municipal bonds while those issued by organizations are corporate bonds.

The government usually issue bonds at the primary market to raise domestic funds to meet its fiscal responsibilities. This can be done from time to time as the need arises. Nigerian FGN bond instruments are named by their maturity, coupon, tenor etc. such as 13.05% FGN AUG 2016 instrument.

How is Return Determined?

Bonds are mostly issued with a coupon otherwise known as **the periodic interest payable**. Bond instruments are usually issued at par; that is, N100 or N1,000 as is the case with Nigerian bonds. A 2-year bond issued at 12% annual coupon with a par value of N1000 implies that the issuer will make 3 semi-annual payments of N60, and a final N1060 on the maturity date.

Bonds can be purchased at both the primary and secondary markets, they are either quoted in price or yields. **There is an inverse relationship between the price of a bond and its yield to maturity (YTM).** At issuance, the yield on a bond instrument is most likely the coupon on that instrument. At the secondary market therefore, an investor can trade bonds by quoting a yield that reflects the variance between the par value and the current price based on the current market dynamics.

How does the Auction Process work?

Bond instruments are issued through a competitive bidding process at auctions as conducted by the Debt Management Office which serves as the representative of the government. An existing government instrument can be re-issued also at the primary market in which case the DMO re-issues based on the current market yield to maturity.

Bonds are auctioned at established rates which determine the return to investors.

Purchasing these instruments in the primary market and holding it till maturity would mean that the investor gets a fixed interest payment, however, there is a secondary market in which investors can trade these bonds to meet their immediate liquidity needs.

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