Treasury Bills: Strong Primary Market Demand Amid a Bearish Secondary Market

It was a generally uneventful month in the Treasury bills market as investors continued to register their dissatisfaction with rates at both the primary and secondary markets. At the primary market, the CBN, on behalf of the FGN, conducted two auctions in January during which bills worth a total of NGN419.65bn were offered to the investing public but only 68.91% on offer was realized. This was despite strong subscription rate (bid-to-cover:1.99x) by investors during both auctions. **Our view is that the FGN was wary of high borrowing costs which was also why 364-Day bills worth NGN125.14bn were redeemed at the first auction for the month**. Range of bids was noticeably high during the first auction but there was a significant decline at the second auction on the back of the latest decision of the Monetary Policy Committee. Nevertheless, average stop rates increased significantly across all tenors during the month.

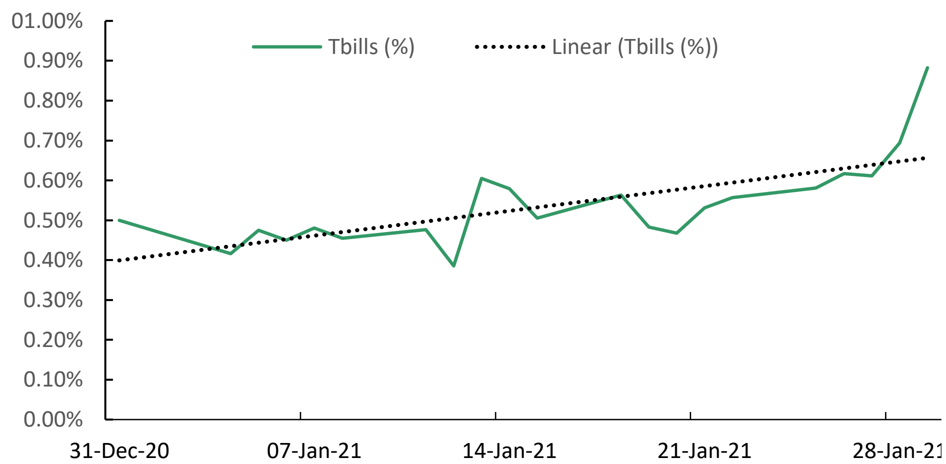
Summary of Treasury Bills Primary Market Auctions in January 2021

	91-Day	182-Day	364-Day	Total
Offer Size (NGN'bn)	20.26	81.19	318.20	**419.65**
Subscription (NGN'bn)	43.75	86.61	445.38	**575.74**
Allotment (NGN'bn)	27.30	72.85	189.05	**289.20**
Redemption (NGN'bn)	N/A	N/A	125.14	**125.14**
Bid-to-Cover	1.60x	1.19x	2.36x	**1.99x**
Average Stop Rates	0.53	1.17	1.75	
Prior Month Average Stop Rates	0.04	0.5	1.17	

Source: CBN, DMO

At the secondary market, the mood was largely bearish as average yield increased to 0.88% at the end of the month from 0.50% as at the end of December. The weakening demand for Tbills in the secondary market during the month is attributed to the low yield environment which when considered against the soaring inflation rate results in negative real returns. Investors have therefore shown preference for equities (which recorded a gain of 5.32% in January).

Chart 1: Upward Trend in Average Treasury Bills Yield in January 2021



Source: CBN, Meristem Research

Bonds: Investors Demand Higher Coupon Rates

There was one primary market bond auction during the month which attracted a total subscription NGN238.28bn against an offer size of NGN150bn composed of reissues. As with Treasury bills, marginal rates were higher in January than in December 2020, an indication that investors demanded for higher coupon rates relative to the previous month. However, the DMO maintained the original coupon rates on the instruments across all tenors.

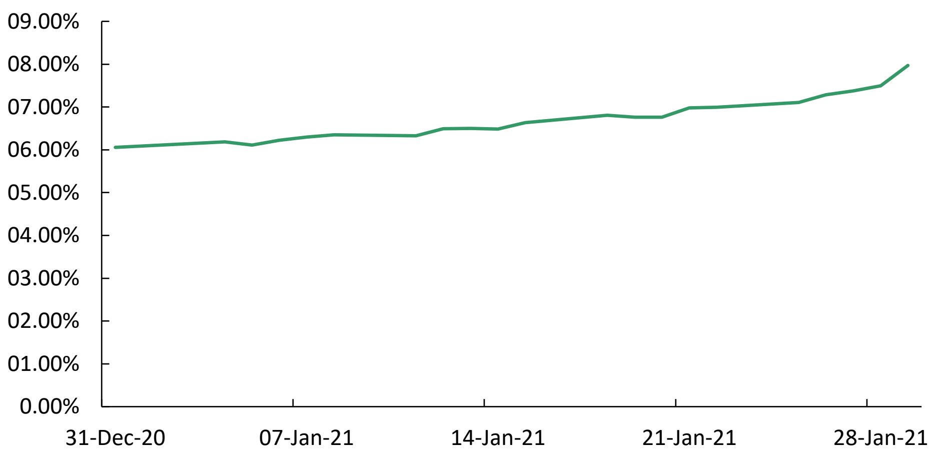
Summary of FGN Bonds Primary Market Auctions in January 2021

	MAR 2027	MAR 2035	JUL 2045	Total
Offer Size (NGN'bn)	50.00	50.00	50.00	**150.00**
Subscription (NGN'bn)	91.84	106.37	40.07	**238.28**
Allotment (NGN'bn)	70.90	83.43	16.03	**170.36**
Bid-to-Cover	1.30x	1.27x	2.50x	**1.40x**
Marginal Rates	7.98%	8.74%	8.95%	
Prior Month Marginal Rates		6.95%	7.00%	

Source: DMO

At the secondary market, demand for bonds waned as average bond yield increased to 7.97% at the end of January from 6.06% during the last trading session in December 2020. The bearish sentiment witnessed during the month was also due to low yields, which is inadequate to compensate for the prevailing inflation rate.

Chart 2: Upward Trend in Average Bond Yield in January 2021



Source: DMO, Meristem Research

Corporate Issuances and Eurobonds

Despite the relatively low yield environment, activities on the corporate end of the market have been rather muted so far in in the year. We note however that several corporates have not yet commenced a new budget cycle, and that issuances typically fall within the second half of the year. The only event of note was the conclusion of BUA Cement Plc's issuance of its NGN100bn Series 1, 7.50% Fixed Rate Bond. The bond which is due in 2027 was oversubscribed by NGN37.82bn.

On Eurobonds, FGN redeemed its USD500mn, 6.75%-JAN-2021 Eurobond which was issued in 2011. This is a positive development which demonstrates Nigeria's capacity to meet its obligations. In reaction, the market went bullish on Nigeria's outstanding Eurobonds as yields declined across tenors following this development. We note that the next FGN Eurobond maturity is due in June 2022 with an outstanding value of USD300mn. Considering the large-sized 2021 budget deficit (NGN5.60trn), the Federal Government plans to raise NGN2.50trn (USD6.60bn) from the international debt market this year. Although high debt servicing costs continue to cloud Nigeria's credit outlook, the recent payout to Eurobond investors and the relatively improved oil revenue outlook should count towards a better credit rating and hence a lower cost of borrowing.

Outlook

The current yield trend in the domestic treasury fixed income market is obviously a reversal of the downtrend witnessed last year. Nevertheless, the yield environment remains relatively depressed and is expected to remain so for at least the first half of the year. This position is further supported by the recent decision of the MPC to maintain status quo until March 2021. We also do not envisage any further significant increase in stop rates as system liquidity is expected to remain elevated over the near term. Thus, while demand at primary auctions will remain strong, driven by conservative investors such as Pension Fund Administrators, demand at the secondary market is expected to remain weak. We maintain our recommendation that investors should consider investment grade corporate bonds and commercial papers in their quest for above-average returns.

Contact Information

Brokerage and Retail Services
topeoludimu@meristemng.com (+234 905 569 0627)
abisoyeoludipe@meristemng.com (+234 708 0007861)
contact@meristemng.com

Investment Banking/Corporate Finance
rasakisalawu@meristemng.com (+234 806 022 9889)
seunlijofi@meristemng.com (+234 808 536 5766)

Wealth Management
funmilolaadekola-daramola@meristemng.com (+234 805 498 4522)
crmwealth@meristemng.com
Tel : +234 01 738 9948

Registrars
muboolasoko@meristemregistrars.com (+234 803 324 7996)
martinaosague@meristemregistrars.com (+234 802 303 1783)
www.meristemregistrars.com
Tel: +23401-280 9250

Trust Services
damilolahassan@meristemng.com (+234 803 613 9123)
crmwealth@meristemng.com

Group Business Development
saheedbashir@mersitemng.com (+234 802 454 6575)
ifeomaogalue@meristemng.com (+234 802 394 2967)
emekaikpechukwu@meristemng.com (+234 803 791 5731)
info@meristemng.com

Client Services
adefemitaiwo@meristemng.com (+234 803 694 3034)
blessingogwuche@meristemng.com (+234 706 896 5173)
car@meristemng.com

Investment Research
ahmedjinad@meristemng.com (+234 809 183 9487)
research@meristemng.com

Corporate websites: www.meristemng.com www.meristemwealth.com www.meristemregistrars.com

Meristem Research can also be accessed on the following platforms:

Meristem Research portal: meristem.com.ng/rhub
Bloomberg: MERI <GO>
Capital IQ: www.capitaliq.com
ISI Emerging Markets: www.securities.com/ch.html?pc=NG
Reuters: www.thomsonreuters.com
FactSet: www.factset.com

Disclaimer Notice:

Meristem and any of its associated or subsidiary companies or the employees thereof cannot be held responsible for any loss suffered by relying on the said information as this information as earlier stated, is based on publicly available information, analysts' estimates and opinions and is meant for general information purposes and should not be construed as an offer to buy or sell or a solicitation of an offer to buy or sell securities or any financial instruments. The value of any investment is subject to fluctuations, i.e. may fall and rise. Past performance is no guide to the future. The rate of exchange between currencies may cause the value of the investment to increase or diminish. Hence investors may not get back the full value of their original investment. Meristem Securities Limited is a member of The Nigerian Stock Exchange and is authorized and regulated by the Securities and Exchange Commission to conduct investment banking and financial advisory business in Nigeria. However, the company through its subsidiaries carries out stock broking, wealth management, trustee and registrar businesses which are regulated by the SEC and ICMR.