SUMMARY OF PREVIOUS AUCTION

Marginal Rates:

16.2884% MAR 2027	10.2500%
12.50% MAR 2035	**11.2500%**
9.80% JUL 2045	11.8000%

Amount:

16.2884% MAR 2027	NGN33.62bn
12.50% MAR 2035	NGN28.90bn
9.80% JUL 2045	NGN18.03bn

SUMMARY OF CURRENT AUCTION

FGN MAR 2027

Auction Date	24/03/2021
Settlement Date	26/03/2021
Maturity Date	17/03/2027
Next Coupon Date	17/09/2021
Clean Price	125.25

FGN MAR 2035

Auction Date	24/03/2021
Settlement Date	26/03/2021
Maturity Date	27/03/2035
Next Coupon Date	27/03/2021
Clean Price	117.78

FGN JUL 2045

Auction Date	24/03/2021
Settlement Date	26/03/2021
Maturity Date	24/07/2045
Next Coupon Date	24/07/2021
Clean Price	89.11

FGN Bond Auction Scheduled for 24th March 2021

Issue on Offer/Summary

The Federal Government of Nigeria (FGN), through the Debt Management Office (DMO), will be conducting a bond auction on Wednesday 24th of March 2021. The indicated total amount to be offered is NGN150bn. All instruments on offer are re-opening issues.

16.2884% FGN MAR 2027	**NGN50bn**
12.5000% FGN MAR 2035	**NGN50bn**
9.8000% FGN JUL 2045	**NGN50bn**

Current Yield Analysis

At the last Primary Market Auction (PMA) held in February 2021, marginal rates `were increased across all offered instruments in line with our expectation. Marginal rates on the 2027, 2035 and 2045 instruments were increased to 10.25%, 11.25% and 11.80% from 7.98%, 8.74% and 8.95% respectively at the previous auction as investors continued to demand higher rates. Although we see further scope for increase in rates, judging by historical standards, we are concerned about how far the government will be willing to go given the precarious nature of its revenue and its already high debt service burden. We however note that oil receipts have trended upwards so far in the year given the movement in oil price from USD51.80pb at year end 2020 to an average of USD61.04pb in Q1:2021. The current trajectory of inflation also presents a compelling case for higher rates at the next auction.

Meanwhile, selloffs in the secondary market persist, driving yields higher. Since the last PMA, the average bond yield has risen to 9.44% (as of March 19, 2021) from 9.21% (recorded on the date of the last auction). We maintain that while PMA rates continue to trend higher, the sentiment in the secondary market will remain bearish as investors seek to participate at the PMAs. We also note that inflows from non-bank OMO maturities (which contributed to strong demand witnessed last year) are no longer available to drive demand in the secondary market.

Please refer to page 5 for our disclaimer notice and other relevant disclosures

Bond Absolute and Relative Valuation

In valuing the **16.2884% FGN MAR 2027**, **12.5000% FGN MAR 2035** and **9.8000% FGN JUL 2045** re-opening offers with the current yield curve as the basis for discounting, we arrived at the following fair value, implied yield and an IRR for the instruments:

Instrument	Fair Value	Implied Yield	IRR
16.2884% FGN MAR 2027	125.25	10.49%	5.25%
12.5000% FGN MAR 2035	117.78	10.10%	5.05%
9.8000% FGN JUL 2045	89.11	11.10%	5.55%

Our valuation gives a fair-trading price ex coupon payment, the expected return on the bond considering its periodic interest payments and the expected return on the bond’s periodic payments. 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.

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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ISI Emerging Markets: www.securities.com/ch.html?pc=NG

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