SUMMARY OF PREVIOUS AUCTION

Marginal Rates:

16.2884% MAR 2027	10.5000%
12.50% MAR 2035	11.5000%
9.80% JUL 2045	12.0000%

Amount:

16.2884% MAR 2027	NGN44.01bn
12.50% MAR 2035	NGN86.29bn
9.80% JUL 2045	NGN131.80bn

SUMMARY OF CURRENT AUCTION

FGN MAR 2027

Auction Date	21/04/2021
Settlement Date	23/04/2021
Maturity Date	17/03/2027
Next Coupon Date	17/09/2021
Clean Price	116.81

FGN MAR 2035

Auction Date	21/04/2021
Settlement Date	23/04/2021
Maturity Date	27/03/2035
Next Coupon Date	27/09/2021
Clean Price	96.20

FGN JUL 2045

Auction Date	21/04/2021
Settlement Date	23/04/2021
Maturity Date	24/07/2045
Next Coupon Date	24/07/2021
Clean Price	72.46

FGN Bond Auction Scheduled for 21st April 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 21st of April 2021. The indicated total amount to be on offer 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

As expected, the DMO at the last bond auction in March 2021 offered higher rates to investors across all tenors. Marginal rates on the 2027 and 2035 instruments increased by 50bps each to 10.50% and 11.50% respectively, while that of the 2045 instrument increased by 20bps to 12.00%. While we note that the increase in rates is consistent with prevailing economic realities particularly with regards to inflation, we think there is yet room for improvement given the current rate of inflation (18.17% in March 2021) and its implication for real returns. On the other hand, the government is constrained in terms of revenue generation and we are concerned that government is increasingly borrowing just to refinance preexisting obligations. With less revenue available for government to engage in real value creating activities (which should ultimately expand its earning base), inflationary pressures will only continue to build up, causing real returns to remain negative and depressed. Nevertheless, we expect further uptick in rates over the near term, supported by relatively stable oil receipts. Meanwhile, investor interest has remained strong -especially towards the longer end of the curve- as overall bid-to-cover ratio increased to 2.22x from 1.26x at the last auction.

In the secondary market, the direction of yields continues to be influenced by the need to minimize capital losses especially on mark-to-market portfolios. Since the last auction date, average bond yield has risen by 176.00bps to 11.31% on 19th April 2021. Given our expectation for PMA rates over the near term, we do not expect selloffs in the secondary market to taper anytime soon.

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	109.17	12.20%	6.13%
12.5000% FGN MAR 2035	96.83	13.10%	6.55%
9.8000% FGN JUL 2045	73.57	13.73%	6.87%

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 the 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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