FMDQ SPOTLIGHT

FMDQ
...empowering the OTC markets

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New Stories

FMDQ 2015 Highlights and Outlook for 2016

FMDQ, unwaveringly committed to its vision of becoming No. 1 in Africa in the fixed income and currency markets by 2019 and its mission to empower the financial markets to be innovative and credible, in support of the Nigerian economy, continues to strive to ensure the realisation of these goals towards making the Nigerian financial markets globally competitive. Looking retrospectively to the start of 2015, FMDQ, in collaboration with its stakeholders, achieved a number of milestones towards the development of the Nigerian debt capital market (DCM). Among these achievements for 2015 are:

- **FMDQ e-Markets Launch** - In February, FMDQ e-Markets, a technology initiative was launched in line with FMDQ's agenda to be operationally excellent. FMDQ e-Markets, designed to suit the needs of different users in varying capacities - whether trading, investing, raising debt capital or seeking participation in the market - has proved to be an invaluable tool for various stakeholders, including FMDQ Members
- **Introduction of the Volatility Management Practice in the Foreign Exchange (FX) Market** – In its capacity as a market organiser, FMDQ, in February, introduced its Risk Management Framework to address volatility in the FX market, ensuring that the market remained opened at all times without any market shutdown
- **United Bank for Africa PLC Bond Listing** – FMDQ saw the listing of the pioneer corporate bond on the Exchange in March - United Bank for Africa PLC ₦345.0bn Medium Term Note Issuance Programme: Series 1: 16.45% UBA 30-DEC-2021 (₦30.5bn)
- **Launch of the Thomson Reuters Market Tracker Solution at the Central Bank of Nigeria (CBN) & FMDQ**– In April, Thomson Reuters launched its FX trade reporting solution for the CBN and FMDQ. This solution has helped enhance the supervisory role of Nigeria's regulators over the FX market, automated the regulatory reporting requirements of market stakeholders, and has aided the automated tracking of FX market volumes and real time activity
- **Co-Sponsorship of Annual Investor Conference in London –** FMDQ partnered with the Association of Assets Custodians of Nigeria (AACN) as a co-sponsor for the AACN's Annual Investor Conference in London in May. The conference themed 'Nigeria: Navigating Changes, Extracting Opportunities' provided an interactive forum for market participants from various sectors and nations to gain in-depth knowledge about the state of the Nigerian capital market and its outlook for the future
- **The Listing of ₦4.8trn FGN Bonds & Quotation of ₦2.8trn Nigerian Treasury Bills** – Another major accomplishment for FMDQ this year was the listing of ₦4.8trn FGN bonds and the quotation of ₦2.8trn Nigerian Treasury Bills, both outstanding as at July 13, 2015, on the OTC Exchange
- **Introduction of the Affiliate Membership Category** – FMDQ, in September, launched a new membership category - "Affiliate Members" - ideal for institutions and individuals with a keen interest in the FMDQ markets, and an association with the financial markets, but not in a full participatory role as either a Dealing, Associate or Registration Member of FMDQ
- **Quotation of ₦8.2bn Wema Bank PLC Commercial Paper (CP)** - FMDQ admitted, in September, the Wema Bank PLC ₦8.2bn Series 1 CP Notes under a ₦20.0bn CP Issuance

Programme (the Wema Bank CP) for quotation on the Exchange. The Wema Bank CP is the second CP, following the pioneer quotation of the Stanbic IBTC Bank PLC CP, to be quoted on FMDQ

- **Pioneer Listing of the Nigeria Mortgage Refinance Company PLC (NMRC) Bond** - FMDQ recorded yet another milestone achievement in the development of the Nigerian DCM as it listed the NMRC ₦8.0bn Series 1, 15-Year 14.9% Fixed Rate Bond under a ₦140.0bn Medium-Term Note Programme on its platform. The issuance and listing marked essential steps towards the development of not only the corporate bond market in Nigeria, but also the Nigerian housing market through the creation of long term funding for mortgage financing
- **The 2015 Nigerian Debt Capital Markets Workshop** – In October, FMDQ, in collaboration with the International Financial Corporation (IFC), and with the support of the Securities and Exchange Commission (SEC), Nigeria, organised a 2-day Workshop on the Nigerian DCM. The Workshop, which was themed "The Nigerian Debt Capital Markets – Towards a Brighter Future", was aimed at diagnosing the issues hindering the empowerment of the Nigerian DCM and propounding practical and implementable remedies to the issues, positioning the markets for unprecedented growth. A DCM Planning Committee was established to begin the implementation process following the Workshop, which was kick started with a Stakeholders' Meeting convened on November 12, 2015 where the Visioning Team and Planning Committee decided on a structure to implement resolutions from the DCM Workshop
- **FMDQ admits ₦17.7bn Nigerian Breweries PLC Commercial Paper** - In November, FMDQ welcomed the quotation of the Nigerian Breweries PLC ₦17.7bn Series 1 CP Notes under its ₦100.0bn CP Issuance Programme on the Exchange, the pioneer non-bank institution CP quotation on the Exchange
- **FMDQ admitted as a Member of the African Securities Exchanges Association (ASEA) and the International Capital Market Association (ICMA)** - FMDQ gained admission as a "Full Member" of ASEA. The admission, which is a positive step for FMDQ towards making the Nigerian capital markets globally competitive, provides, among others, a platform for unlocking the potentials in the markets through mutual networking and communication with various Member Exchanges in Africa. In addition, FMDQ, following ICMA's Executive Committee Meeting in October 2015, also received a firm approval on its membership application and was admitted into the Association
- **Other Fixed Income Securities Listings** – In the course of the year, FMDQ admitted other bonds for listing on the Exchange including**,** Stanbic IBTC Bank PLC ₦15.54bn Series 1 (Tranches A - 16.29% & B - 13.25%) under a ₦150.0bn Structured Note Programme; FCMB Financing SPV PLC ₦26.0bn Series 1, 7-Year 14.25% Fixed Rate Unsecured Bond under a ₦100.0bn Debt Issuance Programme; Fidelity Bank PLC ₦30.0bn 7-Year 16.81% Fixed Rate Subordinated Unsecured Bond; Transcorp Hotels Series 1 ₦10.0bn Series 1, 16% Bond under a ₦30.0bn Medium Term Debt Issuance Programme; Benue State ₦4.95bn 7-Year 16.5% Fixed Rate Bond Issue; and Cross River State ₦8.0bn Series 1, 7-Year 16.5% under a ₦40.0bn Debt Issuance Programme

Looking ahead into 2016, FMDQ, will continue to work collaboratively with its stakeholders to establish initiatives that would enhance the development of the Nigerian DCM. Some focus areas for 2016 include but will not be limited to:

- Offering a more diversified products portfolio including short-term and Islamic (Sukuk) bonds
- The quotation of bonds of private companies
- Integration of the FMDQ markets to include securities dealing and investment banking firms in the fixed income secondary markets
- Capacity building and financial markets education for the FMDQ markets stakeholders
- Financial markets support for economic development
- Nigerian debt capital market transformation
- The introduction of OTC Derivatives

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FMDQ Hosts Ms. Arunma Oteh, OON, Vice President & Treasurer of The World Bank

FMDQ, on December 2, 2015, was privileged to host Ms. Arunma Oteh, OON, a well-deserved Special Guest of Honour, during her first visit to Nigeria as the Vice President & Treasurer of The World Bank. The event, whilst commemorating Ms. Oteh on her new appointment at The World Bank, celebrated her as a visionary in the commendable decision she took as the erstwhile Director-General of SEC to licence FMDQ as an OTC market without an existing model to emulate, and also showcased the progress the Exchange had been made in the last two (2) years since inception towards the actualisation of the shared vision for the Nigerian capital markets.

Ms. Oteh, the first African to take on the position of Vice President & Treasurer at The World Bank, expressed delight and spoke passionately about FMDQ, "a baby" she midwifed a little over two (2) years ago, which now functioned effectively in line with the developmental Master Plan of the Nigerian capital market and also The World Bank and International Financial Corporation (IFC) agenda for the development of the Nigerian financial markets. Ms. Oteh said, "I am a proud Nigerian because FMDQ represents what I tell everybody about Nigeria. FMDQ has shown that it is an institution where everybody is determined for excellence, going the extra mile and pushing harder, and that has made FMDQ look different". She added that, "Nigeria must take its place in the world. At The World Bank, what we ask for are ideas that can stand the test of time and FMDQ must not relent in its efforts. I am waiting to see the liquidity in this market match what I see in other markets".

Bola Onadele. Koko, MD/CEO of FMDQ, said, "We will ensure that we deliver a world class OTC securities exchange that would be a model to all." He went further to thank Ms. Oteh for her support in getting FMDQ thus far, her passion and vision to seeing the Nigerian capital markets become as competitive as that of the more sophisticated markets and her desire to help shape the direction of where FMDQ aspires to be in the future.

The visit, which also had representatives from the IFC (Nigeria) present, served as an opportunity for discussions around establishing collaborative partnerships between The World Bank, IFC and the

Exchange towards the development of the Nigerian capital markets to world-class and globally competitive standards.

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FMDQ Holds Second Bi-Annual "Members Only" Meeting for 2015

FMDQ, in its capacity as a market organiser, hosted its Members to the second 2015 Bi-Annual "Members Only" Meeting held on December 11, at The WheatBaker Hotel, Ikoyi, Lagos. This Meeting, like the first which was held in July, had in attendance major players in the FMDQ markets, as represented by the respective FMDQ membership categories (Dealing, Associate & Registration Members), and commenced with a special welcome note from Ms. Tumi Sekoni, Head, Business Development Group. This was followed by presentations and discussions around various matters of importance anchored by FMDQ's Ms. Jumoke Olaniyan, Head, Market Development Group, Mr. Emmanuel Etaderhi, Head, Market Regulation Group, Mr. Dipo Odeyemi, Head, Market Operations and Technology Division, and Mr. Bola Onadele. Koko, MD/CEO.

The deliberations at the Meeting were centered on the following Agenda items;

- FMDQ Market Architecture Update, which examined Market Development Initiatives and Stakeholder Engagement
- FMDQ Debt Capital Market Development Program
- FMDQ New Membership Categories; the Affiliate and Specialist Dealing Members
- Proprietary Trading System(s)
- Resolutions on Deferred Decisions
- Other Business, including matters relating to Members' Compliance and Complaints Reporting, among others

The Meeting was very interactive and Members had the opportunity to deliberate on outstanding issues and make significant contributions towards the progress of the over-the-counter (OTC) and DCM in Nigeria. Key resolutions impacting the Members and the FMDQ markets as a whole were finalised.

The Meeting concluded with a networking cocktail reception.

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FMDQ Turnover & Dealing Members' League Table

The FMDQ OTC Market Turnover Report shows the turnover on all products traded on the FMDQ secondary market – Foreign Exchange (FX), Treasury Bills (T.bills), Bonds (Federal Government of Nigeria (FGN) Bonds, Other Bonds (Agency, Sub-national, Corporate & Supranational) & Eurobonds), Money Market (Repurchase Agreements (Repos)/Buy-Backs and Unsecured Placements/Takings). FX and Money Market Derivatives are embedded in the FX and Unsecured products categories respectively. These figures exclude primary market auctions in T.bills, Bonds and FX.
The data, collated from the weekly trade data submissions by FMDQ Dealing Members, represents trades executed between Dealing Members, Dealing Members & Clients, and Dealing Members & CBN.

FMDQ OTC Market Turnover (January – November 2015)

	Turnover (₦'bn)
Foreign Exchange	25,500
Foreign Exchange Derivatives	6,579
Treasury Bills	46,285
FGN Bonds	10,070
Other Bonds	121
Eurobonds	36
Repurchase Agreements/Buy-Backs	29,697
Unsecured Placements/Takings	11,621
Money Market Derivatives	101
	130,009
USD equivalent ('bn)	*661*
No. of Business Days	224
Average Daily Turnover	580
USD equivalent ('bn)	*3*

Note: USD/₦ @ 196.84

The FMDQ League Table shows the rankings of its Dealing Members across all products traded on FMDQ OTC securities exchange. The rankings represent the cumulative value across all products traded by the Dealing Members.

Top Ten (10) Dealing Members in FMDQ Market (January – November 2015)

Rank	Dealing Member
1	STANBIC IBTC BANK PLC
2	ACCESS BANK PLC
3	UNITED BANK FOR AFRICA PLC
4	FIRST BANK OF NIGERIA LIMITED
5	DIAMOND BANK PLC
6	SKYE BANK PLC
7	ECOBANK NIGERIA LIMITED
8	UNION BANK OF NIGERIA PLC
9	CITIBANK NIGERIA LIMITED
10	STANDARD CHARTERED BANK NIGERIA LIMITED

All Dealing Members maintained their positions on the League Table except for Citibank Nigeria Limited and Standard Chartered Bank Nigeria Limited, swapping 9th and 10th positions respectively, due to increased trading activity in FX and Repos/Buy-Back transactions. The top ten (10) Dealing Members account for 70% (₦91.0trn) of the overall turnover in the market, with the top three (3) accounting for 25% (₦22.7trn) of this sub-section of the market.

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FMDQ Learning

An Introduction to Collateral Debt Obligations

What is a Collateralised Debt Obligation?

A Collaterised Debt Obligation (CDO) is a type of security that pools together a diversified group of assets that generate regular cash flows, and repackages them to be sold to investors. The underlying pool of assets include mortgages, bonds, car loans, credit card receivables etc., which are essentially debt obligations that serve as collateral for the CDO.

Parties to a CDO

- **Investment Banks/ Securities Firms** – They approve the selection of collateral, structure the notes into tranches and sell them off to investors
- **Asset Managers (Collateral Managers)** – They select the collateral and often manage the CDO portfolios
- **Credit Rating Agencies** – They assess the CDOs, perform due diligence and rate various debts issued by the CDOs

- **Guarantors/Insurers –** They commit to reimburse investors for any losses on the CDO tranches, typically the most senior tranche in a CDO, in exchange for premium payments
- **Investors –** They include pension funds, hedge funds etc.

How it works

The CDO process starts when commercial banks approve loans (mortgages, car loans, credit card loans etc.) to borrowers. These loans get sold to investment banks, to be repackaged into securities and then sold to special purpose entities (SPEs) or special purpose vehicles (SPVs). The SPEs/SPVs are set up by the banks to purchase the assets, thereby removing the loans from the banks' balance sheets. In order to fund the purchase of the assets from the banks, the SPEs/SPVs divide the securities into tranches and sell to various investors. See Figure 1 below.

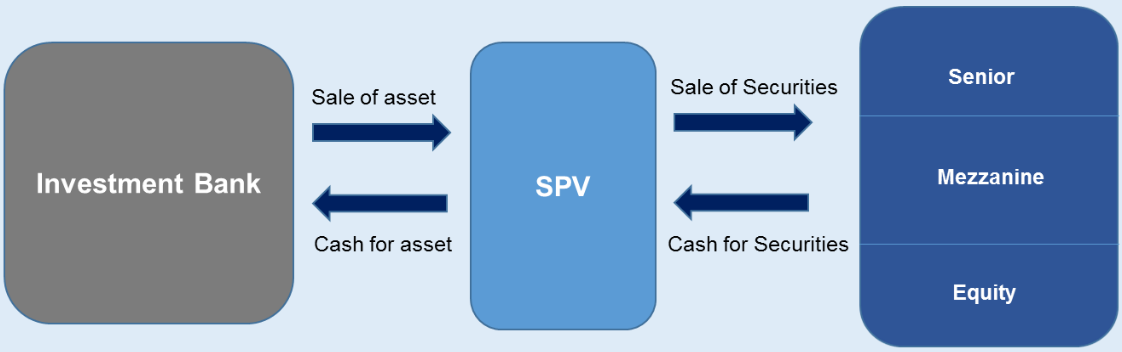

Figure 1: Typical CDO process

The CDO is split into different risk classes known as tranches, which different types of investors fit into according to their risk appetites. The senior tranches are the safest investments and carry the lowest risk as they are repaid first in the event of a default. As a result, the senior tranches of a CDO generally have a higher credit rating and hence offer investors the lowest yields. Pension funds and other risk averse investors tend to fall into this category. The equity tranche is the highest risk portion of the CDO as it is the first position to bear any losses occurring in the underlying asset pool, and receives income only after all other tranches of the security have been discharged. The equity tranches are offered the highest interest rates to compensate for their higher default risk. Hedge funds tend to fall in this category. Ultimately, the principal and interest payments from the loans are re-directed to the investors. It is the promised repayment on the loans that gives the CDO value.

The cash flows generated by the underlying assets are like a waterfall; payments are prioritised first to highest tranches, and the balance paid out to tranches that appear progressively lower in the hierarchy[1]. If cash flows should prove insufficient, the lower tranches may not be paid at all. This subordination structure allows investors choose the level of exposure that suits their needs. In this

[1] Greg Kyle and Alex Russell (2013) Understanding Collaterised Debt Obligations.

way, the credit risk of the underlying securities is unbundled and sold piece-by-piece to investors according to their preferences.

Benefits of a CDO

- CDOs allow banks and corporations remove assets from their balance sheets. By selling off assets, a bank frees up capital for new investments
- CDOs allow investors with varying risk appetites purchase a share of and also achieve exposure to a diversified group of assets in order to lay claim on the specific risk and return characteristics that the cash flows from tranches within the CDOs will produce

Drawbacks of a CDO

- A major drawback is the complexity of the CDO. Buyers may not know exactly what they are buying or the real value of their purchase and this could lead to market panic if investors lose confidence and the CDO becomes more difficult to re-sell
- The loan originators may be less disciplined in adhering to lending standards as they have little incentive to collect when loans in the package fall due, as these loans are now owned by other investors
- Due to the complexity of CDOs, investors tend to rely on the banks selling the CDOs without carrying out enough research and performing their own due diligence

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