FMDQ SPOTLIGHT

FMDQ
...empowering the OTC markets

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New Stories

FMDQ becomes a Member of the African Securities Exchanges Association

In line with its mission to empower the financial market to be innovative and credible in support of the Nigerian economy, and in support of its agenda for the transformation of the Nigerian market with a view to upgrading it to international standards, FMDQ OTC Securities Exchange (FMDQ) is pleased to announce its admission in May 15, 2015, as a 'Full Member' Exchange of the African Securities Exchanges Association (ASEA). This status was ratified at the Association's Annual General Meeting (AGM), which opened the ASEA Conference on November 15, 2015 in Johannesburg, South Africa.

As a Full Member of ASEA, FMDQ is entitled to vote during the Association's AGM, fully participate in ASEA events and be featured in ASEA publications. FMDQ is also afforded the privilege of nominating a representative for election to the ASEA Executive Committee.

This admission is a positive step towards making the Nigerian capital markets globally competitive and provides, among others, a platform for unlocking the potentials in the markets through mutual networking and communication with various Member Exchanges in Africa. Membership of ASEA is an important reference for many international investors and the membership status reflects and reiterates FMDQ's commitment to implementing the highest standards in line with international best practices.

ASEA is the premier Association of 24 securities exchanges in Africa. The Association works with its Member Exchanges to enhance their global visibility and competitiveness, with a view to attracting capital inflows to the African capital markets. It also provides an authoritative information portal with aggregated statistics on African markets and Exchanges respectively, boosting market development and capacity building among Member Exchanges and initiating strategic alliances on behalf of its Member Exchanges.

FMDQ, as an OTC securities exchange and self-regulatory organisation with a key mandate to foster sustainable development in the Nigerian financial market, is resolute in driving its "GOLD" agenda – Global Competitiveness, Operational Excellence, Liquidity and Diversity – in support of the Nation's economic development.

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FMDQ appoints Daisy Ekineh as an Independent Non-Executive Director

Whilst striving to meet the expectations of its diverse stakeholders, FMDQ continues to put in place an effective corporate governance structure to facilitate proper oversight of its business by the Directors and the Management of the Company. To this end, following the "No-objection" received from the Securities and Exchange Commission (SEC), the FMDQ Board of Directors is pleased to announce the appointment of Ms. Daisy Ekineh as an Independent Non-Executive Director, effective October 30, 2015. With over 30 years of capital markets experience, Ms. Ekineh, a former acting Director-General of SEC from May 2009 to January 2010, is currently the Chief Operating Officer of Global Mandate Consulting Limited. Whilst at SEC, she, at various times, served as Executive

Commissioner (Operations) and Director, Securities and Investment Services, where she was responsible for the regulation of all public offers of securities, mergers & acquisitions among others.

As a capital market doyen, Ms. Ekineh has played a critical role in driving several policy initiatives in the Nigerian capital market, having served in several Committees, including the Technical Committee of the Bond Market Steering Committee, the Nigerian Economic Summit Group (Non-oil and Non-agriculture Sub-Committees) and as the Chairman of the Information Sharing Sub–Committee of the Financial Services Regulation Coordinating Committee (FSRCC). She contributed significantly in designing the Capital Market and Regulation Strategy of the Financial Sector Strategy (FSS) 2020. A one-time Chair of the African & Middle East Regional Committee of the International Organisation of Securities Commissions (IOSCO), her experience and expertise in capital markets regulation and operations will serve towards the realisation of FMDQ's market development and governance agenda for the transformation and alignment of the Nigerian Fixed Income and Currency (FIC) markets with global standards.

To ensure equitable representation, FMDQ's 13-man Board of Directors was constituted along stakeholders' influence, thereby allowing participation from its diverse stakeholder groups. The Directors have been strategically selected to provide broad yet specialised representation considering the Company's dual functions as a securities exchange (market organiser) and self-regulatory organisation.

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FMDQ Listings & Quotations

FMDQ admits ₦17.70bn Nigerian Breweries PLC Commercial Paper

In November 2015, FMDQ welcomed the pioneer non-bank institution commercial paper (CP) quotation on its platform. Having successfully met the quotation requirements as contained in the FMDQ Commercial Paper Quotation Rules, and obtained the approval of the FMDQ Board Listings and Quotations Committee, the **Nigerian Breweries PLC ₦17,709,445,000.00 Series 1 Commercial Paper Notes under its ₦100,000,000,000.00 Commercial Paper Issuance Programme (The Nigerian Breweries CP)** was admitted for quotation on FMDQ.

As is the tradition with the OTC Securities Exchange, a Quotation Ceremony was held in commemoration of the milestone, with the issuer, Nigerian Breweries PLC (NB PLC), represented by the Finance Director, Mr. Mark Rutten, as the guest of honour. In attendance also, were the sponsors of the issue on the platform, FMDQ Registration Members (Quotations) and joint issuing houses, Stanbic IBTC Capital Limited and FBN Capital Limited, represented by Mr. Kobby Bentsi-Enchill (Head, Debt Capital Markets) and Mr. Kayode Akinkugbe (Managing Director/CEO), respectively.

Whilst congratulating NB PLC for quoting the first CP of a non-bank, real sector institution on FMDQ, Mr. Bola Onadele. Koko, Managing Director/CEO of FMDQ noted that as a securities exchange, FMDQ promotes credibility for quoted CPs through a highly efficient registration process. He further added that CPs quoted on the OTC securities exchange gain access to the full complement of an FMDQ quotations service, which includes but is not limited to global visibility through their inclusion on the FMDQ Bloomberg E-Bond trading system and on the quotations page of the FMDQ website, as well as improved transparency characterised by continuous disclosure of relevant information (such as issuer, issuance type, outstanding value and issuer history) on the quoted CPs.

Ahead of the signing of the FMDQ Quotations Register and the presentation of the CP Quotation Certificate, Mr. Rutten, whilst making his address, said that NB PLC was excited about the future of the planned CP issuance activity on FMDQ and the ever-growing benefits this would bring to the Nigerian capital markets.

Speaking about the transaction, following the presentation of the CP Quotation Tombstones to the Registration Members, Mr. Bentsi-Enchill stated that “Increasing the number of CP issuances is the first step towards creating liquidity in secondary market trading of CPs. The second, and equally important step, is the quotation of the securities on FMDQ OTC Securities Exchange. We are exceptionally pleased to have worked with NB PLC in setting up its maiden CP Programme and successfully raising ₦17.70bn in the first series. We are also pleased to sponsor the quotation of the CP on the FMDQ OTC Securities Exchange. The decision by NB PLC to complement its short-term funding via issuance in the money and capital markets is certainly laudable, and in so doing the Company has demonstrated leadership as a pacesetter in the domestic debt capital markets.”

Mr. Akinkugbe expressed his delight at having partnered with NB PLC in establishing its ₦100.00bn CP Programme, the largest ever by a Nigerian non-financial corporate, and successfully arranging the first tranche of ₦17.70bn amidst general market volatility. He further stated that “the success of the transaction speaks to the high confidence the investing public has in the NB PLC brand and recognition of the issuer’s remarkable track record in the beverage industry. In addition, it is a reflection of the joint lead issuing houses’ distribution capability and depth in the fixed income market. We expect that the quotation of the NB PLC CP on FMDQ will provide investors with transparency, efficient price determination and improved liquidity.”

As a securities exchange and self-regulatory organisation with a commitment to facilitate growth and development in the financial market and Nigerian economy at large, FMDQ is committed to promoting an efficient, transparent and well regulated market, which will attract and retain domestic and foreign investors.

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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 & the Central Bank of Nigeria (CBN).

FMDQ OTC Market Turnover (January – October 2015)

	Turnover (₦'bn)
Foreign Exchange	23,755
Foreign Exchange Derivatives	6,263
Treasury Bills	42,128
FGN Bonds	8,733
Other Bonds	119
Eurobonds	35
Repurchase Agreements/Buy-Backs	27,598
Unsecured Placements/Takings	11,187
Money Market Derivatives	101
	119,920
USD equivalent ($'bn)	*609*
No. of Business Days	204
Average Daily Turnover	588
USD equivalent ($'bn)	*3*

Note: USD/₦ @ 196.81

The FMDQ League Table shows the rankings of its Dealing Members across all products traded on FMDQ OTC securities exchange – FX, FX Derivatives, T. bills, Bonds (FGN Bonds, Other Bonds and Eurobonds), Money Market (Repos/Buy-Backs and Unsecured Placements/Takings) and Money Market Derivatives. The rankings represent the cumulative value across all products traded by the Dealing Members.

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Top 10 Dealing Members in FMDQ Market (January – October 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	STANDARD CHARTERED BANK NIGERIA LIMITED
10	CITIBANK NIGERIA LIMITED

All Dealing Members maintained their positions on the League Table except for United Bank for Africa PLC (UBA) and Diamond Bank PLC (Diamond Bank), swapping 3rd and 5th positions respectively, due to increased trading activity in T. bills, Unsecured Placements & Takings and Repos/Buy-Back transactions. The top ten (10) Dealing Members account for 72% (₦86.0trn) of the overall turnover in the market, with the top three (3) accounting for 27% (₦32.4trn) of this sub-section of the market.

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Upcoming Events

Second FMDQ ‘‘Members Only’’ Bi-Annual Meeting for 2015

As part of its commitment to develop the Nigerian financial market and in recognition of the crucial roles its various stakeholders play in this development, FMDQ is thrilled to host its Members to the second 2015 FMDQ Bi-Annual "Members Only" Meeting for the year scheduled to hold on December 11, 2015. Following on from the first bi-annual "Members Only" meeting for 2015 which held on July 2, where the FMDQ Market Architecture Report was presented and reviewed by all stakeholders present, the second Meeting will focus on, among other agenda items, determining and finalising resolutions and deferred decisions from previous Members Meetings.

The Meeting will, as is customary, provide the opportunity for different players in the FMDQ market, represented by Dealing, Associate and Registration Members of the OTC Exchange, to deliberate on and make contributions towards the development of the markets. Outcomes of the just-concluded Nigerian Debt Capital Markets Workshop will also be discussed.

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FMDQ Learning

An Introduction to Total Return Swaps

What is a Total Return Swap?

A Total Return Swap (TRS) is an agreement in which one party makes periodic floating rate payments to a counterparty in exchange for the total return realised on a reference asset, which includes both the income it generates and any capital gains. It is a means of transferring the total economic exposure, including both the market and credit risks of the underlying asset between two parties. The payer of the TRS can eliminate all the economic exposure of the asset without having to sell it, while the receiver of the TRS, on the other hand, can access the economic exposure without having to buy the asset. The reference assets can be indices, bonds (emerging market, sovereign, bank debt, mortgage-backed securities, corporate, municipal, etc.), loans, equities, real estate receivables, lease receivables, commodities etc.

Features of a TRS

- *The Total Return of a reference asset* includes all cash flows that stream from it as well as the capital appreciation or depreciation of the reference asset.
- *The Floating Rate* is a reference interest rate, e.g. the Nigerian Inter-bank Offered Rate (NIBOR) plus or minus a spread.
- *The Total Return Receiver (TRR)* is the party that agrees to make the floating rate payments and receive the total return. The TRRs are usually aggressive hedge funds, specialty asset managers and collaterised loan obligation special purpose vehicles (SPVs), who accumulate leveraged credit spreads and sell off tranches to investors[1].
- *The Total Return Payer (TRP*) is the party that agrees to receive the floating rate payments and pay the total return. The TRPs are usually large institutions such as investment banks, commercial banks, mutual funds, securities dealers and insurance companies.

Other market participants in a TRS include: Fund of Funds, Private Equity Funds, Pension Funds, Credit Card lenders, University Endowments, Governments, Non-Governmental Organisations and special purpose vehicles such as Collaterised Debt Obligations and Real Estate Investment Trusts[2].

Structure of a TRS Transaction

In order to purchase the reference asset, the TRP must borrow capital. The dealer will raise cash from the capital market at a funding cost (usually linked to the inter-bank offered rate) and this cash will flow right out again to purchase the reference asset[3]. The asset provides both interest income and capital gains or losses, depending on its price fluctuations. See Figure 1 below.

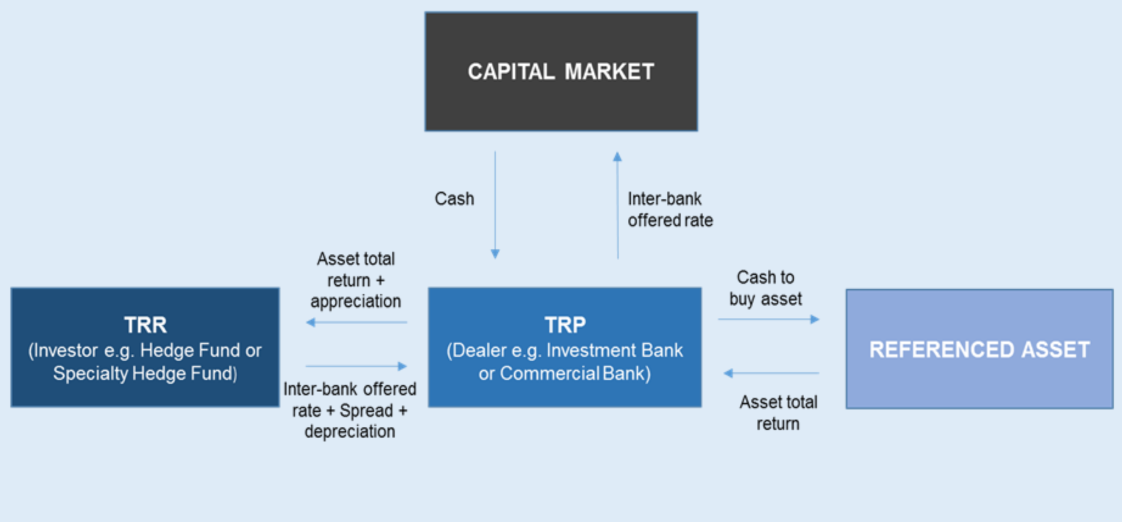

Figure 1: Typical Structure of a TRS Transaction

[1] Frank J. Fabozzi (2008) Handbook of Finance, Financial Markets and Instruments
[2] Robins et al (2013) Total Return Swaps: From the Obscure to the Legal Spotlight
[3] Frank J. Fabozzi (2008) Handbook of Finance, Financial Markets and Instruments

From the illustration above, it can be seen that a TRS has two payment legs between the payer (TRP) and receiver (TRR); the reference asset or a basket of assets exists on the "*total return leg*" and the interest payment, linked to the inter-bank offered rate, exists on the "*funding leg*".

On the "*total return leg*", the payer has a long position in the reference asset, holding it on its balance sheet, so it buys protection on the asset and agrees to pay the receiver all the future returns of the reference asset plus any appreciation in its value. In exchange, on the "*funding leg*", the receiver seeks exposure to the returns of the reference asset or basket of assets, but does not want to acquire or hold in its balance sheet. The receiver will sell protection on the reference asset by taking a synthetic long position in the asset, agreeing to make regular floating cash flow payments to the payer (inter-bank offered rate +/- a spread) including any depreciation in the value of the asset and compensation for any default losses.

Benefits of a TRS

- One of the major benefits of a TRS is **leverage**. A TRS allows the receiver to synthetically generate higher returns using leverage, while avoiding transaction and administrative costs associated with buying the assets or entering into repurchase agreement (repo) transactions
- A TRS can be viewed as a form of credit protection that offers more risk reduction than a CDS[4]. With a TRS, the reference asset owned by the dealer is protected from declines in value as the investor must reimburse the dealer for any decline in the value of the reference asset
- Diversification is another draw to a TRS. The receiver can achieve the same economic exposure to a diversified basket of assets in one swap transaction that would otherwise take several cash market transactions to achieve[5]
- It is highly flexible as it can be based on virtually any asset or series of assets
- It can also be used as a synthetic funding instrument offering improved financing costs. The payer may be able to lock in profits by entering into a TRS transaction. This occurs whenever the payer has a funding cost that is less than the payment it receives in the TRS. The receiver is also able to obtain good financing rates as their exposure to the reference asset is financed at a spread to the inter-bank offered rate, which is a lower cost than if they financed an outright purchase of the reference obligation[6]
- The investor (TRR) can also take advantage of the dealer's (TRP) better judgement in acquiring the reference asset

Drawbacks of a TRS

The major drawbacks associated with a TRS lies in the risks associated with them. They include:

- **Interest Rate Risk**, which is borne by both parties to a TRS. Payments made by the receiver to the payer are normally floating rate (inter-bank offered rate +/- a spread). If inter-bank offered rate increases during the life of the TRS, the receiver's coupon payments will increase. Likewise, if inter-bank offered rate decreases, the payer's coupon receipts will decrease
- **Investment Return Risk** is another drawback of a TRS usually borne by the receiver. As a result of the payer holding the reference asset on its balance sheet, the receiver assumes the

[4] A Credit Default Swap (CDS) has the major purpose to protect the investor against default risk. If the issuer of the reference asset defaults, the CDS provides a payment, however if no default occurs no payment is received
[5] Frank J. Fabozzi (2008) Handbook of Finance, Financial Markets and Instruments
[6] Robins et al (2013) Total Return Swaps: From the Obscure to the Legal Spotlight

risk of capital losses as it has to make guaranteed payments to the payer to offset any drop in asset value

- **Counterparty Risk** could occur if a Hedge Fund, for instance, makes multiple TRS investments in similar assets. Any significant drop in the value of those assets would leave the Fund in a position of making ongoing coupon payments plus capital loss payments against reduced or terminated returns from the asset(s)
- **Liquidity Risk** could exist if the terms of the TRS contract specify the physical delivery of the reference asset and the asset defaults during the life of the TRS. This could pose a problem acquiring the reference asset at a reasonable valuation in the open market

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