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Domestic Bond Market and International Financing in Nigeria

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Abstract

This article examined the pivotal function of Nigeria's local bond market in improving foreign funding opportunities. Africa's largest economy faces various challenges concerning external debt and economic stability; the paper asserts that a strong domestic bond market can substantially diminish dependence on foreign debt, alleviate currency risk, and facilitate long-term financing for essential infrastructure projects. It underscores the many advantages of a robust domestic bond market, including enhanced government accountability, institutional advancement, and increased financial inclusion. The study highlights many constraints obstructing the expansion of the domestic bond market and presents practical solutions, including the enhancement of regulatory frameworks, the promotion of investor education, and the diversification of financial products. By concentrating on these sectors, Nigeria may establish itself as an appealing locale for both domestic and foreign investors, eventually fostering more sustainable economic development and enhanced access to global capital markets. This research highlights the need of cultivating a robust domestic bond market as an integral component of a holistic approach to enhance Nigeria's economic resilience and developmental results.

Keywords:

Bonds, Domestic Bond Market, Capital Market, Government Bond, International Financing Bond Market Development.

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1.0 Introduction

In market economies, the fixed income security (bond) market is a significant part of the capital market. Its significance stems from the fact that it offers businesses cheap, long-term funding while also providing individual investors with opportunities for long-term investments. For deficit budgets, governments employ it because of the cheap cost of funding. Another factor that contributes to the growth of the domestic capital market is the plenty of liquidity provided by the local bond market. According to the theory, the national yield curve may be lowered and liquidity can be generated when both local and international investors participate in the domestic debt market.

The long-term debt instruments issued by governments and companies are traded on a bond market. This is a financial commitment of a company over an extended period of time that commits to repaying a certain amount of funds at certain intervals in the future (Olowe, 2017). Speculative financial instruments known as bonds offer to commit to making payments at regular intervals for a certain duration (Mishkin, 2007). Bond prices plays a crucial role in the economy as it allows governments and enterprises to must take out loans in order to fund their endeavours, since this is the market where interest rates are determined. Especially noteworthy is the role that the bond market plays (as the route in which the economy's savings are converted into medium- and long-term investment) is massive in both industrialised and developing nations.

Banks are vulnerable to financial hazards owing to the heavy load of financial intermediation (Nwiado, 2013). As a result, we rely too much on bank-dominated financing rather than market-based sources like bond, stock, or debenture capital. Banks are good at providing "patience finance," according to Eichengreen and Luengnamamifehai (2006), but bond market sources of funding are available only on a long-term basis, making the bond market the polar opposite of what banks are good at. This leads us to believe that the establishment of a domestic bond market is a primary objective of all developing economies, including Nigeria's. Michael (2021) argued that this means that governments that want fiscal autonomy must actively work to build their bond markets.

An efficient financial market is one of the most important factors in a country's economic development and progress. There are two main parts to the financial market: the money market and the capital market. The money market is where short-term loans are raised, while the capital market is where long-term loans are raised. A well-integrated financial system that can withstand shocks from outside sources and thrive in a market economy are both encouraged by the financial market. Developing domestic debt markets, particularly the bond market, is essential for countries aiming to reach this milestone. These markets should diversify investors, activate the secondary market, achieve reliable custodial and settlement systems, and improve effective regulation (Herring & Chatusripitak, 2000). Nigeria is one of several countries that has borrowed money from outside sources since its local debt market is not well-developed.

With the issuance of 4 billion Eurobonds on the international debt market, Nigeria's external debt reached N38 trillion in 2021, allowing the government to claim an external reserve of more than $40 billion (Nairametrics.com, 2023). The nation's debt service in 2018 alone was over 2.3 trillion naira, while the total amount owing was over 21.5 trillion naira. An increase in the ratio of debt service payments to total government spending will discourage investment and slow economic development (Efuntade et al., 2020). According to IJASEPSM (p.34), the debt service ratio and exchange rates are both adversely impacted by external loan financing. The Naira/dollar exchange rate depreciates by 1.3% to 2.4% for every 10% rise in the government deficit, according to all analyses conducted by the Nigerian federal government. Additionally, the currency rate is depreciated by around 5% for every 10% rise in the debt service ratio (Ojo & Okuruomu, 1992). Budget deficits occur when the government is unable to satisfy its financial obligations due to a lack of funding. The government has turned to borrowing money from other countries.

A number of economic problems have resulted from this, including the country's high debt load, low investment inflows, low industrial output, productivity, and technological progress; high inflation; a balance of payment imbalance; high unemployment; high poverty; and a poor exchange rate (Nzotta, 2014). Foreign debt, according to Yusuf and Mohamed's (2021), is a barrier to growth in the long run, but has a growth-inducing effect in the short run. Their research indicates that domestic debt really boosts GDP in the long run, while having a detrimental impact in the near term. Debt overhang impact confirmation, however, occurs in both the long and short term as a result of payments leading to growth retardation. Improved economic growth and development necessitates vigilantly monitoring the changes in debt factors.

The capacity of the bond market to attract investment capital from both local and international sources is one of the three pillars upon which healthy financial markets rest, all of which contribute to economic development. Surprisingly, however, the Nigerian bond market—like most emerging bond markets—has not yet met the standards set by this mandate. This is due to the market's notoriously poor corporate governance, weak regulatory framework, economic instability, and weak corporate mechanisms (Kemboi & Tarus, 2012). In addition to the market's long-standing issues with a shallow and inefficient bond market, Nigeria's economy has a structural problem with banks dominating the market rather than the other way around.

On reality, this issue has led to an excessive dependence on banking financing, which has become the banking sector a replacement for the bond market rather than a supplement. As a result, Nigeria is now "vulnerable" on the international market. Banks in Africa have both strong ties to borrowers and weak ties to business and political leaders, according to Eichengreen and Luengnamemitchai (2006), who highlighted the issue of bank dominance in most African countries' economies. As a source of funding, the bond market is accessible only to the biggest, longest-established companies about whom the finest information is available, but on the other hand, transactions take place at arm's length, often between anonymous buyers and sellers. An effective banking system and a well-developed bond market are two sources of diversification that a financially mature economy should have, as the banking sector is in a prime position to provide patient financing.

The unpredictability of interest rates and currency fluctuations is another significant obstacle in Nigeria's bond market. In the 1980s", the average exchange rate of the Naira per U.S dollar was 0.6100%, with a maximum rate of 7.391%; and in the 1990s, it was 6.391 percent. From an initial level of 8.03783%, the average exchange rate rose to 92.6934%. There has been little stability in the Nigerian currency rate so far (CBN, 2011). There has been consistent interest rate volatility in Nigeria over the years, therefore the country's currency rate and interest rates are essentially the same. The underdevelopment of the Nigerian bond market can be caused, in part, by the unpredictability of interest rates and currency exchange rates. Since Nigeria has relied so largely on foreign grants and concessional loans from donor agencies to pay for capital expenditures and government deficits, it appears difficult for the country and other African nations to fund essential projects through bond markets as alternative sources of funding. Foreign direct investment (FDI) seems to be a less appealing option for participating in the Nigerian local currency bond market. Both domestic and international investors in Nigeria's bond market are hit hard by the country's unfavourable exchange rate regime, which makes matters worse.

Any economy, but especially one in development like Nigeria's, relies heavily on the bond market. The bond market is a subset of the capital markets that facilitates the raising of long-term investment money. According to Mu, Phelps, and Stotsky (2013), the bond market facilitates investment by both savers and borrowers, which aids in economic growth, company expansion, and long-term viability. Ogilo (2014) agreed that a bond document shows the borrower's obligation to repay the principal and interest within a specified time frame. Bond market innovations, according to Oke, Dada, and Aremo (2021), make the process and supply of operating long-term capital more efficient. A country's financial system is a barometer of its progress, productivity, and capital accumulation, according to King and Levine (1993).

The domestic bond market is pushing for a change in the government's funding strategy, away from short-term and towards long-term. The long-term funding through the bond market is a predictor of economic growth in Nigeria, according to Nnamdi (2015). Bond markets improve corporate governance standards worldwide and act as intermediaries between supply and demand, as Kin (2000) found. Companies can earn money through the bond market, and the government can use that money to fund infrastructure projects and increase output. But in terms of savings, cash flow, and risk mitigation, it's a win-win for the issuer and the borrower. Undoubtedly, the bond market lays the groundwork for economic growth in less developed economies like Nigeria's. Nevertheless, investors' optimism was dampened by the devastating coronavirus pandemic in 2020, causing the Nigerian bond market to grow at a snail's pace (DMO, 2020).

It is believed that Nigeria's capital market has excellent growth potential, given the country's status as a developing nation. According to Alajekwu and Achugbu (2012), the Nigerian financial market can pool savings from extra economic agents and send them to productive units, where they can be put to good use. This means that bond markets, which are a part of any capital market, could be a key indicator of economic growth in developing countries like Nigeria by directing money from profitable sectors to those that are struggling. The bond market is the macroeconomic mechanism that converts savings unit funding into investments with medium to long term maturities.

There are many different kinds of bonds traded on the Nigerian bond market, including sovereign, green, corporate, sukuk, and government bonds. A combination of factors, including a steady rise in the budget deficit due to falling oil prices and the global impact of the COVID-19 pandemic, has led to an increase in the federal government's reliance on bond markets as a source of funding. Bond market investments offer diversification opportunities and lower overall portfolio risk, according to Alajekwu and Ezeabasili (2012). Bond market investments have been able to forecast US economic growth in the past, according to Harvey (1989), but according to Chidi-Okeke, Ogbonna and Okeke (2020), bond market investments, interest rates, and inflation rates cannot predict Nigeria's human development index in the future.

Equally encouraging is the positive and statistically significant correlation between bond capitalisation and GDP growth (Ogboi, et. al., 2016; Kapingura & Makhetha-Kosi, 2014; Nnamdi 2015). According to Olaniyan and Ekundayo (2019), the capital market will become more efficient once the government issues more bonds to the public. According to Herring and Chatusripitak (2001), a lacklustre bond market makes it harder to raise funds. Mailafia (2014) argued that lack of financial and market re-engineering, risk management, illiquidity thin market and low coupon rates might limit bond market development and expansion.In the same way. Aman, Naimand Isa (2019a) also verified that unpredictable climate stopped international investors from infusing capital into a country’s local market. Frankel (1993) argued that infrastructure development may be affected in the absence of a bond market. Most of the studies given above failed to assess the amount to which Nigeria’s economy is sensitive in the long-run to a completely decomposed structure of the Bond Market as well as the extent to which they do encourage or assist Nigeria’s economic development process. An articulation of the foregoing consequently, forms the primary challenge of this research in country’s local market.

Globally, bond market plays huge significance in guaranteeing sustainable economic development. Bond markets are recognised by many researchers as a "major" actor in the economic transformation process of a nation (Ogboi, Njogo, Nwankwo, Nkwede, Uguru, Nkwegu, 2016). Over the years, long-term developmental initiatives are sponsored by government utilising cash from the money market (banks). This in no little degree has produced high inflation on the economy. The riskiness associated in financial mismatch caused by employing short-term money to support long-term initiatives of the government has exposed banks to financial risks and other related effects.

Bond market throughout the years has remained to be source of financial leverage to capital shortages emerging economies as a tool for long term capital accumulation and allocation; yet, many nations have yet to investigate this potential route of wealth production. Bond

Market indisputably may improve the potentials of an economy to utilise other natural funds to support industries with large economic multipliers in order to raise living standards for all citizens monetary system. The growth of bond markets is driven by the desire to promote a Local market for currency bonds (LCY).

General pre-conditions, key components, and constraints for a successful local currency bond market development have been identified as a diagnostic framework, in response to a request for assistance from the G20, the IMF, the World Bank, the EBRD, and the Organisation for Economic Co-operation and Development (OECD) regarding bond market development. The money market and its derivatives market are just two examples of the many interconnected markets that the diagnostic framework made possible. Important factors in the growth of the local bond market include;

i. Participation in and responsibility for the change initiative

ii. Part two. Adherence to the expectations of the anchor market

iii. Relationships to stable financial markets, responsible debt management, and monetary policy

iv. Interbank liquidity and

v. A dependable and solid system for clearing and settlement in the market.

IMF and World Bank (2016), EBRD and OECD (2013).

Government bond market development initiative launched by the World Bank group backs the growth of LCBMs (Local Currency Bond Markets) to boost the development of nations attractiveness for local and international investment for efficient fixed income markets which are crucial to assist economic progress and eliminate poverty. Smooth operating governments are able to maintain policy efforts with the support of fixed income markets, which also benefit savers and capital market financing, encourage investment possibilities according to risk-return preferences industries, vital infrastructure projects, and businesses while decreasing their dependence on foreign cash taking out loans and getting bank loans. Investment is necessary for long-term economic growth and development, according to several research. All areas, including infrastructure, labour, plant, and equipment, must be considered in this investment. Whereas most developing countries, like Nigeria's, have relied on short-term bank loans for the majority of their funding, these initiatives need longer-term investments.

From a global viewpoint, a robust financial system makes it easier to create investment opportunities by giving investors the resources they need, both monetarily and technically. The financial market, which is a part of the financial system, relies on a healthy bond market to function efficiently and effectively. Creating a bond market may help with financial stability, economic recovery, and economic change. Facilitating investments in capital creation by meeting financial demands in the long run to corporate and public sector lenders

(Hakansson, 1999; Peiris, 2010; Tendulkar (Hanacock, 2004; Akinsokeji, Adegboye & Edafe, 2016).

With the many advantages of a more efficient market, encouraging growth in the domestic bond market is more important by the day. Capital is better allocated via domestic bond markets because they provide access to alternative financing sources, diversify investor groups, and spread risk across them, all of which contribute to better risk management. As a subset of the financial market, the domestic bond market contributes to a country's overall financial system growth (Adelegan & Radzewicz-Bak, 2009).

2.0 Conceptual Framework of Domestic Bond Market and International Financing in Nigeria

An explanation of the connection between the domestic bond market in Nigeria and international finance systems is the overarching goal of the conceptual framework. It will delve into the ways in which these two factors influence one another, the expansion of the economy, and the security of the country's finances.

The growth of the domestic bond market and foreign participation in it have an effect on the development and growth of the capital market in Nigeria, which in turn improves financial stability. "Financial stability and economic growth are promoted by a vibrant and deep local currency domestic bond market," Peiris (2010) said. Monetary policy can also benefit from a well-functioning domestic bond market. Since Nigeria is the biggest economy in the West African area, a well-functioning and secure domestic bond market there is crucial for the whole subregion. Sovereign Nigeria State regained confidence to re-enter the International Financial capital markets in order to raise debt for her capital projects after the Paris and London Clubs forgiven her debt in the fourth quarter of 2005. Prior to this, Nigeria could not participate in the international debt market until 2003. First issued in 2003, a 20-year domestic bond was Nigeria's first sovereign (FGN) debt via the Debt Management Office (DMO), which had been installed in 2000. Eight corporate bonds with a combined face value of ₦92.8 billion were sold by the Debt Management Office on the domestic capital market between 2008 and 2010. After then, a large number of international investors continued to pour money into Nigeria's local fixed income market.

In January 2016, the Nigerian Eurobond will mature. There are a number of critical functions that foreign involvement in the US bond market performs in the growth of developing market economies. The national yield curve is lowered when foreign investors participate in the domestic bond market, which adds liquidity to the domestic capital market. The domestic bond market is more liquid because foreign investors trade the instrument more frequently than local private and institutional investors, who tend to buy and hold. Internationalisation of domestic capital markets in emerging market economies (EMEs) is another benefit of foreign participation. It draws private sector borrowing away from the Domestic Market.

For instance GT Bank in January 2011 raised a $500 Eurobond 10 year 7.9 percent coupon on the foreign capital market away from the local market. While it is arguable that foreign involvement in domestic bond markets has been beneficial to their growth, there are a number of negative concerns associated with excessive foreign investment. When there are a lot of foreign investors in the U.S stock market, it can make local bond markets more unstable during times of financial crisis. As an example, consider the financial crises that hit Russia and the Asian Tigers in 1998. There are three submarkets within the global bond market. One is the domestic bond market, which deals with debt traded inside a country's borders. The second is the foreign bond market, where non-resident corporations issue debt securities (Batten, Hogan, & Szilagyi 2009). Last but not least, there's the Eurobond Market, where bonds produced in one currency are put in another country by international bank syndicates.

Bonds are a kind of fixed-income financial instrument that firms and governments use to raise funds for various projects. When a person purchases a bond, he is effectively lending money to a financial institution at an agreed-upon interest rate. Government bonds and corporate bonds are the two main types of bonds. Governments issue bonds to support government projects and/or fulfil its budget deficit. Because these bonds are backed by the government, they pay a fixed amount of interest and are, therefore, virtually risk free. Government bonds usually mature in 1 bto 50 years. In some cases, interest earned is non-taxable (Okumagba, 2006). Corporate bonds are issued by corporate enterprises to obtain cash and they pose bigger risks than government bonds and so earn higher interest.

The term "Bond Market" usually refers to a financial marketplace where investors may buy and sell debt securities called bonds before they mature. In a capital market, the section where Bonds are issued and exchanged is often regarded as the debt market (ADP, 2000). As with most other markets, Bond Markets contain main and secondary markets. The primary market allows borrowers to obtain cash by issuing securities to investors, while the secondary market offers investors with the flexibility to restructure their assets by adjusting the mix, maturity or degree of ownership. A major purpose of Bond Market is thus to bring issuers and investors together and to assist the development of creating a continuous flow of long term funds at the correct price (Okumagba, 2006).

All bond markets share a common structure and set of fundamental components, including issuers seeking long-term funding, investors looking to invest savings or other liquid assets in interest-bearing securities, intermediaries that connect the two parties, and an infrastructure that facilitates securities transactions, guarantees legal ownership of securities and transaction settlement, and provides price discovery information (ADP, 2000). As with other capital markets, bond markets rely on the regulatory environment for their fundamental structure (Hue, 2000; IMF, 2001). According to APEC (1999), bond markets that are considered efficient have a competitive structure, low transaction costs, low degrees of fragmentation, a strong and secure market infrastructure, and a lot of different types of market players. Two main categories of bonds are traded on the Nigerian stock exchange. One kind is government bond, while the other is business bond.

2.1 Brief on the Domestic Bond Market in Nigeria

The parties to a bond arrangement are the lender (the investor) and the borrower (the issuer). The bond grants the investor the right to receive payments from the borrower at regular intervals. Bonds are a kind of fixed-income security since they promise the bearer a definite amount of money at regular intervals based on some formula (Bodie, Kane & Marcus, 2014). In accordance with Fabozzi (2006), a bond is a kind of financial instrument that stipulates the repayment of the principal amount plus interest to the investor or lender over an agreed upon duration. You are required to repay the principal by the maturity date. Ajayi (2013) states that bonds are a way for corporations or governments to raise money for certain projects or budgets. The normal duration of this kind of award is more than a year. Upon completion of the set period, the 'IOU' may be redeemed at the interest rate that has been previously established.

In the bond market, investors buy and sell bonds and other debt instruments. Academics studying public and corporate finance may use it to find long-term investors with spare cash to lend. The debt market, credit market, or fixed income market are all terms that describe it. Debt issued by corporations and bonds issued by governments make up the bulk of the bond market. According to Okeke-Chidi et al. (2020), a bond market that is operating successfully may diversify financing and credit risk away from banks while also efficiently mobilising funds to drive the private sector and support worthwhile activities. According to Onalapo and Adebayo (2011), the bond market in Nigeria is much smaller and less developed compared to the banking sector and the stock market. Nevertheless, the bond market in Nigeria, and government bonds in particular, have grown rapidly since the establishment of the Debt Management Office (DMO) and the reforms that followed in the years after 2000, when the DMO and the Securities and Exchange Commission began working together. The market is dominated by government bonds. For instance, monthly government bonds are mostly issued by the Federal Government of Nigeria. State Government Bonds, Municipal Government Bonds, and Corporation Bonds are issued by subnationals (local and state governments) and business groups when required.

In 2012, the Nigerian Bond Market was composed of 86.0% FGN bonds, 10.6% state bonds, and 3.4% corporate bonds (George, 2013; Okeke-Chidi, et al., 2020). There are a variety of bond market instruments available in Nigeria, including development stocks, treasury bonds, industrial loan stocks, unsecured zero coupon redeemable convertible stock, AMCON bonds, and state and local government bonds. The main institutions in the bond market are the Central Bank of Nigeria, the Nigerian Exchange Limited, the Security and Exchange Commission, and the debt management office (DMO). Despite its recent expansion, the Nigerian bond market continues to confront formidable challenges.

Mailafia (2014) argued that financial innovation, determining the direction of Bond Market innovation, and maintaining a balance between risk minimisation and market innovation are the major problems of Bond Market development. Lack of a bond auction trading platform, high interbank rates, illiquidity, budget delays, and a lack of a robust policy to support the fast expansion of corporate bonds are the limitations cited by the majority of writers

(Adelegan & Radzewicz-Bak, 2009; Andrianaivo& Yarty, 2010; Grandes & Peter, 2013). The following issues were highlighted by Ajayi (2013) as being plaguing the Nigerian bond market: insufficient market transparency, shallow issue sizes, ease of access to equity funding, high implied borrowing costs, regulatory hurdles, liquidity, and a supervisory and legal framework. These facts cast doubt on the premise of market segmentation theory, which states that investors have different characteristics and goals when it comes to assets with different maturation dates (Okeke-Chidi, et al., 2020).

Factors impacting the growth of bond markets in nations that issued bonds actively in 1990 were studied by Claessens, Klingebiel, and Schmukler (2007). They concluded that GDP is one of the most important variables in bond market growth. The more flexible the exchange rate system was, the less the amount of foreign money that was issued. Public bond market growth was also positively affected by fiscal burden, banking sector development, capital account openness, and inflation performance. In their 2009 study, Adelegan and Radzewicz-Bak analysed the variables that contributed to the expansion of public and corporate loan markets in twenty-three SSA nations between 1990 and 2008. Determinants of debt market capitalisation that are positive and significant include public debt, exchange rate volatility, investment profile, absence of capital controls, and fiscal balance. Determinants that are negative and significant include bureaucratic quality and interest rate spread.

Their research on corporate debt shows that although factors like fiscal balance, domestic bank lending, and exchange rate volatility are positive and essential, factors like interest rate volatility and GDP per capita are negative and substantial. Rinqui (2010) looked at what drives growth in the Kenyan bond market for corporations. He made use of sixty companies registered on the Nairobi Securities Exchange between the years 2000 and 2012. He performed correlation analysis to find out how the study's variables were related to one another. The results showed that several macroeconomic variables, the size of the banking sector, the regulatory framework, the political climate, the investor base, and the length of time it takes to issue bonds all have a role in how the bond market evolves.

A well-functioning bond market was studied by Onaolapo and Adebayo (2011) to determine its impact on the Nigerian economy. An example of a country whose economic activity is totally reliant on government spending forecasts is Nigeria, which their study focused on because of the country's excessive dependence on government estimations for corporate operations. Despite the bond market's potential to serve as a source of alternative funding for the Nigerian economy, they hold the view that it is only brought to light when official financial projections fall short.

Many developing countries are more susceptible to financial crises because their bond markets are ineffective (Herring & Chatusripitak, 2000). Unlike in other developing regions, bond markets in Sub-Saharan Africa (SSA) are still in their early stages. The only exception to this is South Africa, where bond market development has lately seen a substantial expansion of the corporate bond market. The expansion of bond markets, especially in developing countries, has been the subject of more studies as a consequence (Okeke-Chidi, Ogbonna, Okeke & Chris-Eiiogu, 2020). With the many advantages of a more efficient market, encouraging growth in the domestic bond market is more important by the day. Capital is better allocated via domestic bond markets because they provide access to alternative financing sources, diversify investor groups, and spread risk across them, all of which contribute to better risk management. As a subset of the financial market, the domestic bond market contributes to a country's overall financial system growth (Adelegan & Radzewicz-Bak, 2009).

One corner of the financial world that has not changed is the bond market. Despite consistent expansion, particularly in the last few years, Africa's bond markets are still in their early stages of development. With their massive holdings, bond markets should provide a refuge for investors seeking low-or no-risk investments (Cassimon, Essers & Verbeke, 2016). But most African nations' bond markets are still in their early stages of development, with modest market capitalisations in comparison to more developed markets (Kapingura & Makhetha-Kosi, 2014; Mu et al., 2013). The domestic financial sector's resiliency may be attributed to this. Financial stability, development, and growth are all enhanced in nations with robust capital markets (Peiris, 2010). As a result, expanding the Bond Market is crucial to the indisputable expansion of the economy.

Public trust is being eroded due to inflationary pressures in the economy, and another concerning problem is the breadth and depth of the Nigerian bond market. Even though the market is relatively little, there is a double whammy: current private and corporate bonds are being squeezed out by government bonds. Private investors and non-bank investors are also impacted by the crowding out effect. Not to mention the maturity and pricing arbitrariness issues, which may further undermine market trust. The empirical literature shows that most studies have concentrated on the growth of stock markets and economies, but no one has yet looked at what drives the development of Nigeria's bond market. This is despite the fact that there are three fundamental problems with this market: 1) the lack of corporate bonds available, 2) the market's current state of underdevelopment, and 3) the fact that banks in the country would rather use the capital market to raise money than the bond market. As an example, during the 2005 bank recapitalisation in Nigeria, which is widely seen as the largest "industry convergence in the history of banking in Africa," no bank borrowed money from the bond market. Considering the aforementioned open-ended issues in the Nigerian bond market as well as the contentious and ambivalent findings on the factors that influence bond market growth, this research is motivated to examine, from a macroeconomic standpoint, what really drives bond market development in Nigeria.

Nigerian banks seem to be competing with the Nigerian bond market for fund provision, while also losing market share due to the country's dependence on banks for financing (Hawkins, 2002). This is because the banking sector undoubtedly acts as the bond market dealer/marker. Also, a large supply of government bonds results from fiscal balance, which might drive down corporate bond prices. A skewed trajectory in corporate bond prices could have a ripple effect on the bond market as a whole. Similarly, savings comprise a substantial share of investable money in the Nigerian setting, and savings are fundamentally a main determinant for company investments. In Nigeria, for example, bond investing is a common use of national providence funds and pension savings accounts. Consequently, the domestic bond market in Nigeria may be underdeveloped due to the mishandling of aggregate deposits in the country. In light of this, it is crucial to address the age-old topic of what drives bond market growth. Thus, it is prudent to do research to determine the elements that, from a macroeconomic perspective, promote the growth of the bond market in Nigeria, and more specifically, to identify the effect of these factors on bond development.

Investors are hesitant to put money into Nigeria's domestic bond market because of its poor condition. It goes without saying that issuers in the Nigerian Bond Market aren't motivated to put money into the market, which leads to low participation, less liquidity (particularly in dollars), strict regulation, undiversified portfolios, dealers with inadequate funds to support their investments, and no hedging instruments or markets. Authorities charged with overseeing the capital market in Nigeria, including the NSE, the Central Bank of Nigeria, the Securities and Exchange Commission, and the Debt Management Office, have failed to make sufficient strides in facilitating its expansion. And the government has not done anything to foster an atmosphere where financial growth may flourish. Delays in bond market growth may be attributed to factors such as the presence of several market regulatory agencies, a lack of coordination, and the dominant effect of a banking sector that has become too large. When contrasted with the bond markets in the United States, Europe, and Asia, the Nigerian market performs far worse.

Compared to other developing bond markets in Latin America and Asia, the Nigerian bond market suffers from a lack of liquidity, diversification, depth, institutional investors, infrastructure, capitalisation, listed companies, and instruments. In support of this idea, Cassimon, Essers, and Verbeke (2015) pointed out that LCBMs have a hard time expanding their investment size and fundamental financial market infrastructure. Furthermore, the market's activities are not adequately regulated. Companies in Nigeria are unable to get the cash they need to invest more in human and physical capital due to the market's shallowness, inefficiency, and lack of liquidity (Smaoui, Grandes & Akindele, 2017). Furthermore, with the exception of South Africa, the bond markets in Africa only manage to invest between fifteen and eighteen percent of their GDP in government securities, they said. About 80% to 90% of the market capitalisation rate across all markets is accounted for by this. A possible explanation for the low number of outstanding government bonds in Nigeria might be the country's financially undeveloped system compared to wealthy nations, together with its high inflation rate.

When it comes to raising capital, the Nigerian government and enterprises rely heavily on the domestic bond market. The Security and Exchange Commission (SEC) and the Central Bank of Nigeria (CBN), the country's top bank, are mostly responsible for regulating this market. Institutional investors (both local and international), banks, insurance firms, and individual investors make up the bulk of this market's investor base. Similarly, the most common bond kinds in this market are: Federal Government Bonds, which the Nigerian government issues to fund public spending. The purpose of issuing state bonds is to raise money for various state-sponsored projects and infrastructure. Companies may raise capital for many purposes, including growth, refinancing, and general operations, by issuing bonds to the public.

There are two parts to the Nigerian domestic bond market—the primary market and the secondary market—and they both contribute to the smooth operation of the economy. Getting a handle on these two parts of the Nigerian economy might teach you a thing or two about the capital markets and how they work. The domestic bond market in Nigeria facilitates the issuing of debt instruments by both public and private enterprises, making it an essential part of the country's capital market. There are corporate bonds and bonds issued by the government (FGN bonds). It is common practice to finance budget shortfalls using FGN bonds, which are seen as risk-free since they are backed by the Federal Government. Although corporate bonds may provide larger yields, they also come with a higher level of risk.

2.2 Nigerian Primary Bond Market in View

Investors may purchase freshly issued bonds in the primary bond market. Bonds allow issuers, including enterprises and the Nigerian government, to attract investors both large and small. Here are some of the most important aspects of this market:

i. **Issuers**: The federal government, state governments, and private entities are the principal issuers in Nigeria.

ii. **Financial Tools**: Standard bond kinds include corporate bonds, sukuk (Islamic bonds), state bonds, and federal bonds.

iii. **Bond Auction**: The Debt Management Office (DMO) normally holds auctions to issue government bonds. Investors put up bids indicating how much they want to buy and how much they are ready to pay for it.

iv. **Yields and Maturity**: Bonds might be very short-term (one to five years) or very long-term (five to thirty years). Interest rates, inflation, and the issuer's perceived risk all have a role in yields.

When it comes to funding government operations and projects, the primary bond market is vital. These initiatives help build our nation's infrastructure and fuel economic growth. It also acts as a channel for offering a variety of investment possibilities to both individual and institutional investors, which helps to diversify their portfolios.

2.3 Nigerian Secondary Bond Market in View

Bonds that have already been issued may be purchased and sold on the secondary bond market. Because of the market's liquidity, bondholders don't have to wait for the bond's maturity date to sell their holdings. Bonds in Nigeria are exchanged on the unique over-the-counter (OTC) market, usually via broking companies, banks, and other types of financial institutions. Just like any other market, this bond market offers liquidity; investors may sell their bonds before they mature, but the price they get back depends on the market. It should be noted that changes in interest rates, credit ratings, economic indicators, and market sentiment cause fluctuations in the Secondary Bond market. The following are among the most preferred trading platforms in this market:

i. **Efficient Markets:** Bond prices are more accurately reflected in the secondary market, which helps to find the actual worth of bonds by taking into account investor sentiment and current economic data.

ii. **Risk Management:** By trading on the secondary market, investors may control the risk of interest rates and duration. Bond prices tend to decline when interest rates increase, giving buyers a chance to snag bargains.

An essential part of Nigeria's financial system, the domestic bond market allows for investment options and helps the nation create wealth. Investors may better manage the complexity of bond investing in Nigeria, harness opportunities, and evaluate risks by comprehending both the main and secondary markets. Over time, both markets might become even more successful with the help of ever improving market infrastructure, regulatory frameworks, and investor education.

2.4 International Financing in Nigeria: Overview

Critical infrastructure, social programs, and private sector growth in Nigeria rely on international finance, which is why it is fundamental to the country's economic success. If we want to make the most of the possibilities that come with foreign investment, we need to solve problems like making debt manageable, keeping regulations stable, and putting projects into action efficiently. Maintaining global interest and involvement in Nigeria's development path would need persistent attempts to improve the investment environment, governance, and economic resilience. The term "international financing" is used to describe the inflow of capital into Nigeria from outside the country. Various kinds of international financing in Nigeria are discussed here, along with their respective functions within the country's economic goal-driving framework, the obstacles they face, and the overall effects on the economy.

Forms of International Financing in Nigeria

i. **FDI:** When foreign corporations put money into Nigerian enterprises or start new businesses, that's called foreign direct investment (FDI). Oil and gas, telecoms, agriculture, and real estate are some of the industries that draw foreign direct investment. Tax breaks and regulatory assistance are two ways the Nigerian government seeks to entice foreign direct investment.

ii. **FPI:** When international organisations invest in financial assets like stocks and bonds, this is called foreign portfolio investment. Portfolio investors can find a home in Nigeria's capital markets, specifically the bond market and the Nigerian Stock Exchange. Increased liquidity and bolstering of capital market development can be achieved through the influx of investment portfolios.

iii. **Bilateral and Multilateral Loans:** In order to fund development projects, Nigeria engages in loan negotiations with a number of different countries and international institutions. Notable partners include multilateral organisations such as the World Bank and the African Development Bank (AfDB), as well as bilateral partners such as China, Japan, and the US. Roads, electricity, and social development (health, education) are common recipients of these loans, as are economic stabilisation and other vital sectors.

iv. **Grants and Development Assistance:** Some initiatives or programs, especially those pertaining to health, education, and poverty reduction, get funding from foreign governments and international organisations. Agencies such as USAID, DFID (UK), and the UN give technical help and funds for developmental efforts.

v. Money sent back by Nigerians working outside the country is a substantial source of funding, even though it isn't the typical way that countries get their money. Consumer spending, business investment, and household income security are all bolstered by remittances for Nigerian households.

2.5 Roles Of International Financing in Nigeria

a. Infrastructural Development: To fix Nigeria's enormous infrastructural gaps, money must come from outside the country. The efficient execution of projects like as road building, electricity generating, and water delivery often depends on funding from outside sources. International investments boost productivity, create employment, and encourage innovation, all of which contribute to economic development.

b. Financial Stability: When the Nigerian economy is struggling, it may get a helping hand from foreign investors and loans. Development aid and technical support boost local ability in many areas, which in turn improves public service delivery and governance. This is known as capacity building. There are a lot of advantages to obtaining funding from outside sources for Nigeria's economy, but there are also a lot of disadvantages. Some of the most significant restrictions on foreign funding for Nigeria are as follows:

i. **The Long-Term Viability of Nigeria's Debt:** This issue becomes more pressing as Nigeria takes out additional loans from foreign sources. Fiscal difficulties and reduced financing for essential social services are possible outcomes of high levels of debt.

ii. **Economic Volatility:** Changes in oil prices or other external factors might impact Nigeria's capacity to pay its foreign debt or to entice investors to stay put.

iii. Foreign investment might be discouraged by factors such as political instability, regulatory changes, and corruption, which can create difficulties for investors. Attracting and maintaining foreign finance depends on policies that are consistent and transparent.

iv. The repatriation of monies and the profitability of overseas investments are both affected by the volatility of the Nigerian naira relative to other major currencies.

v. Internationally financed projects have implementation challenges such as inefficiency, inadequate capability, and governance concerns, which may cause delays and cost overruns.

2.6 Domestic Bond Market Interaction with International Financing

Various factors, including economic climate, regulatory frameworks, and investor mood, influence the intricate and multi-faceted relationship between the domestic bond market and international financing. Financial stability, investment climate, and economic development in Nigeria are all susceptible to this relationship.

For developing nations aiming for long-term prosperity in today's interconnected world, the relationship between domestic bond markets and foreign funding has become an important issue. With its increasing fiscal issues and urgent need for infrastructure development, a well-functioning domestic bond market is of utmost importance for Nigeria, one of the biggest economies in Africa. Because of its heavy dependence on foreign borrowing to cover its budgetary needs, Nigeria is vulnerable to the risks connected with interest rate volatility, currency fluctuations, and shifting global financial circumstances. One possible solution to these problems is to increase financial resilience, diversify funding away from foreign debt, and use the domestic bond market as a steady source of income. The government may fund necessary projects and encourage a stronger economy by tapping into local savings and investments.

Another benefit of a healthy domestic bond market is the encouragement of various financial instruments and the development of institutional investors, both of which contribute to the general public's propensity to save and invest for the future. Problems do exist in Nigeria's bond market, however. Growing it will be difficult because to problems including insufficient regulatory frameworks, low levels of investor engagement, and poor financial knowledge. In order to make the domestic bond market more appealing to foreign investors and realise its full potential, it is essential to resolve these hurdles. An extensive analysis of the interplay between the domestic bond market in Nigeria and foreign funding will be laid out in this introductory section. It will help shed light on how Nigeria can use its domestic bond market to boost economic stability and promote sustainable growth in the midst of a constantly changing global financial landscape by examining the advantages of a strong bond market, pointing out current obstacles, and suggesting strategic ways to improve it.

The following opportunities arise as a result of the interplay between the U.S bond market and foreign financing:

i. **The Dynamics of Capital Flows:** The domestic bond market facilitates both domestic and international capital formation. A more stable bond market and higher returns may entice investors from across the world.

ii. **Currency Rates and Currency Risk:** The allure of domestic bonds to investors from other countries might be affected by changes in currency rates. A severe decline in the value of the naira may cause bond market outflows or discourage foreign investment.

iii. The stability and performance of the domestic bond market may impact investment choices, which in turn affect international finance decisions. If Nigeria's bond market were more active and healthy, it might raise the country's credit rating and make borrowing money from outside sources easier.

iv. **Differences in Interest Rates:** The movement of money may be influenced by the difference in interest rates between the local bond market and foreign markets. Foreign investors may be enticed by higher domestic bond rates, while capital flight may be encouraged by lower returns.

v. **Participation from International Investors:** When the domestic bond market is strong, foreign investors may buy bonds, which increases liquidity and lowers borrowing costs for domestic issuers.

vi. It may become more difficult for governments and businesses to acquire funds overseas if investors are lured away from foreign financing choices by attractive rates on local bonds. This phenomenon is known as the crowding out effect.

vii. **Interest Rate Trends:** Investors' preferences for local vs foreign bonds may be impacted by a rise in domestic interest rates brought about by inflation or economic instability, which in turn can boost bond yields.

viii. To lessen need on foreign funding, a stable currency might entice foreign investors to participate in the local bond market.

ix. **Policy Alignment:** Bond market attractiveness to local and international investors is influenced by the Central Bank's interest rate and inflation policies, which in turn influence foreign financing choices.

x. **Economic Impact and Development:** Economic growth may be fostered by the issuance of domestic bonds, which play a pivotal role in financing social programs, capital projects, and infrastructure development.

xi. Currency, interest rate, and market volatility risk may be reduced with a diversified financing strategy that includes both local bonds and foreign funds.

xii. **Debt Sustainability:** By effectively managing its foreign and local bond markets, Nigeria can make its debt more sustainable and less dependent on risky sources of external funding.

xiii. **A Framework for Regulation and Policy:** Bond market stability, lower borrowing rates, and the attraction of foreign capital are all crucial outcomes of government policy. Here, the government's economic plan and the openness with which it distributes funds are crucial.

xiv. **SEC and CBN regulations:** Attracting both domestic and foreign investors depends on a domestic bond market that is both legitimate and well-regulated.

2.7 Obstacles and Limitations

a. Unpredictability in the Market: The bond market and foreign finance are susceptible to fluctuations in the market caused by political unrest, economic downturns, and changes in global economic circumstances. Nigeria is vulnerable to economic shocks from outside sources due to its small pool of indigenous investors and heavy dependence on foreign money.

b. Credit Rating and Perception: Investors' actions may be influenced by their views of risk, and Nigeria's capacity to obtain money locally and globally is impacted by its credit rating.

If Nigeria wants to see its economy expand, stabilise, and thrive, it must see how its domestic bond market interacts with foreign finance. To strengthen and diversify its financial system, Nigeria might issue domestic bonds to raise capital and solicit investors from across the world. To get the most out of both funding options, however, you have to fix the problems and make sure the regulations are helpful.

2.8 Strengthening Nigeria's Domestic Bond Market For Enhanced International Financing

Despite being Africa's biggest economy, Nigeria has encountered several obstacles on its path to long-term prosperity. Its dependence on foreign funding has been a major factor in these difficulties, leading to currency instability, pressures from external debt, and less budgetary freedom. To tackle these difficulties, the potential for a strong domestic bond market is enormous, since it can fund national development initiatives and make the country more appealing to international investors. Raising the profile of Nigeria's domestic bond market as a means to better access foreign funding is the overarching goal of this advocacy document.

Significance of a Strong Domestic Bond Market

1. Reduction of Reliance on Foreign Debt: Less dependence on foreign debt is one of the main benefits of a thriving local bond market. The government may avoid foreign currency risk while funding deficits via bond issuances by drawing on domestic deposits and institutional investors. By taking this action, Nigeria's economy may become more stable and less susceptible to external economic shocks.

2. Institutional Development and Financial Inclusion: Pension funds, insurance firms, and mutual funds may all benefit from a robust bond market, which can help them expand. Bonds and other diversified and secure investment products are necessary for these institutions to manage risk and diversify their holdings. In addition to strengthening the financial system overall, a healthy bond market encourages financial inclusion by opening up government funding to individual investors.

3. Long-Term Financing for Development Projects: Critical infrastructure projects in Nigeria, such as roads, railroads, electricity, and healthcare, may be financed reliably and over the long term using domestic bonds. To alleviate the ongoing pressure from short-term financing choices, the government may guarantee that development initiatives have the required funds to go forward by issuing bonds with that purpose in mind.

4. Improved Government Accountability and Transparency: Openness in government borrowing and fiscal management is crucial for building a robust domestic bond market. Governments are held to higher standards of governance and accountability as a result of the stringent reporting and regulatory obligations that are imposed on them as bond issuing institutions. Further investment, both at home and abroad, may be encouraged by fostering investor trust via this openness.

2.9 Overcoming Barriers To A Robust Domestic Bond Market

1. Improving regulatory frameworks: The development of Nigeria's domestic bond market is impeded by regulatory obstacles. Reducing bureaucratic delays, improving investor safety, streamlining bond issuing procedures, and creating institutional and legal frameworks that support bond market development are all responsibilities of the government and regulatory agencies.

2. Raising awareness and educating investors: The advantages of bond market participation are still unknown to many prospective investors. Expanding the investor base beyond institutional players may be achieved via public awareness campaigns and investor education activities that highlight the benefits of bond investing.

3. Cutting-edge Financial Tools: Various types of investors may be courted via the creation of novel financial products including infrastructure bonds, social bonds, and green bonds. These tools might be attractive to local and foreign investors that prioritise ESG (environmental, social, and governance) factors, and they can fit in with the rising worldwide trend towards sustainable investment.

4. Bolstering the function of financial intermediaries: When it comes to the evolution of bond markets, financial intermediaries are vital. Bond market operations, including underwriting and marketing, may be improved with the help of financial advisers, asset managers, and investment banks, allowing for more thorough market participation.

2.10 Enhancing International Financing Through A Strong Domestic Bond Market

1. Access to international financial markets: If Nigeria's local bond market is strong, the country would have better access to international financial markets. Emerging economies with well-established domestic bond markets attract more international investment because these markets already have the necessary structures and standards in place, making them seem more trustworthy. An uptick in investment capital from outside sources may result from this assurance.

2. Reducing Currency Risk: The currency risk associated with foreign finance may be reduced with the support of a domestic Dond Market that is well-established and controlled by investors from the area. By relying heavily on local bonds for government funding, Nigeria may create a more stable finance environment by reducing its exposure to changes in foreign currency.

3. Better Ratings for Sovereign Credit: The sovereign credit ratings of Nigeria may be improved by bolstering the local bond market. Higher ratings, cheaper borrowing costs, and more access to international finance are all possible outcomes of a more diversified funding base, less reliance on external debt, and better governance.

4. Recruiting Investors from Other Countries (FDI): Foreign Direct Investment (FDI) may flourish in an economy with a robust bond market. A robust local bond market may offer the varied portfolios and stable investing environments that international investors are looking for.

3.0 Conclusion

To achieve its development objectives, Nigeria relies on its domestic bond market, which provides capital for social services, infrastructure, and other vital projects to both the government and corporations. But the market can't reach its full potential because of problems including insufficient liquidity, few investors, and the need for more regulation and transparency. International finance also gives Nigeria the chance to diversify its financial sources, increase capital flows, and entice international investors. However, risks related to currency volatility and global economic movements must be carefully managed when relying on foreign funding. Nigeria has to make strategic changes to boost market efficiency, investor trust, and long-term economic development if it wants to get the most out of its domestic bond market and its international funding. The interconnection of the Nigerian domestic bond market with foreign funding is, thus, crucial to the country's economic development and progress. She hopes to entice foreign investors by offering funding via domestic bonds. The Nigerian financial system may be strengthened and diversified. To make the most of these funding possibilities, Nigeria must be laser-focussed on overcoming the associated problems and establishing strong financial regulations.

4.0 Recommendations

Investors would be well-informed about the market because of the diverse funding sources that would be made possible by a robust domestic bond market and improved international financing, all of which are the result of a robust regulatory framework that aims to increase market liquidity and cross-border investment opportunities. If the government keeps these priorities in mind, Nigeria should be able to strengthen its local bond market and attract more foreign investment, both of which would help the country's economy thrive and ensure its long-term viability.

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