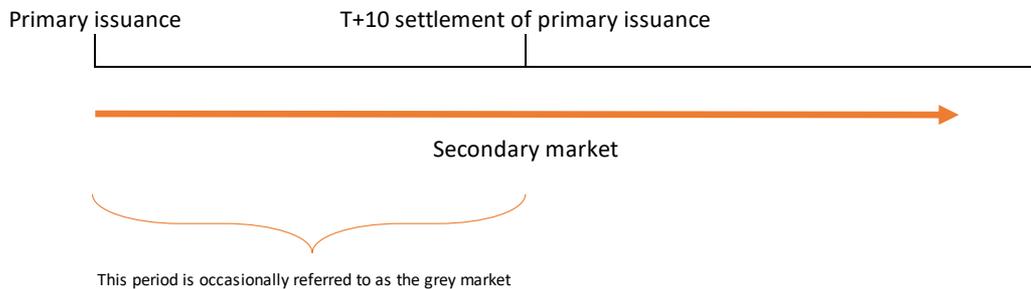


## The not so Secondary Market

Although commonly referred to as the secondary market, it is by no means secondary in terms of importance for portfolio managers when it comes to investing in the securitized investments universe. The secondary market now accounts for over 50% of volume traded within the U.K. DFM domain, so it's worth dedicating an FNL piece to explaining exactly what it is, where Fortem Capital supports the process and ultimately how we can help managers to extract value from the market. It is also worth emphasizing that the trading and settlement of these instruments is no different to when trading bonds (which these are!) or stocks.

### It's just a matter of timing

In many respects the primary and secondary market are the same thing. It really comes down to timings. A primary trade is generally made through a series of leads orders collated on day one. These initial trades settle after a set period of time (typically T+10) after trade date. The secondary market theoretically starts to exist as soon as the initial orders are executed. What this means is that any manager who chose not to participate in the lead order is still able to access the product at any point afterwards. The product will of course be subject to price changes, the major factor being how the relevant markets have moved.



Once these products are launched, they are as discussed above, subject to price moves. An excellent tool for monitoring these is our website portal to which you can register access. Here it shows all available products that we currently can offer.

Some factors to note are that like many securities out there, a bid/offer spread is applied. This has traditionally been maintained at 1% which demonstrates how tight these can trade and hence the value that can be extracted (more on this later). Furthermore, this also ratifies the idea that these products are liquid from a buyback perspective i.e. one is not forced to hold until maturity but can take full advantage of the tight bid level shown.

From a practical perspective we have over 30+ years experience in physically executing the secondary trades. We have built systems around them, built relationships with your dealers and are aware of all the idiosyncrasies that each firm has around settlements, nomenclature and such like. The point being that Fortem Capital assists in the execution of secondary market to the level at which you can consider these as no different to the ease at which you might trade a stock or fund.

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## 18<sup>th</sup> November 2016

Rates (bps)		
	Current	Week Chge
GBP 1yr	58.80	-0.20
GBP 3yr	79.50	+3.60
GBP 5yr	101.80	+7.20

Equity Indices (%)		
FTSE 100	6763.99	+0.50%
S&P 500	2151.13	-0.62%
Nikkei 225	17967.41	+3.41%
Eurostoxx 50	3025.24	-0.16%

Currencies (%)		
GBPUSD	1.2422	-1.38%

5yr Credit Spreads (bps)		
Citigroup	72.90	+0.02
Credit Suisse	149.06	+7.39
Deutsche	225.13	+4.99
GS	86.45	+0.87
HSBC	77.76	+10.97
JPM	56.21	-1.70
MS	82.38	+0.49

Commodities (%)		
Gold	1206.10	-1.75%
Oil	45.14	+3.99%

3m Implied (vol pts)		
FTSE 100	14.37%	-0.83%
S&P 500	12.57%	-0.67%
Nikkei 225	19.36%	+0.21%
Eurostoxx 50	19.33%	-0.02%

5yr Implied (vol pts)		
FTSE 100	19.98%	-0.03%
S&P 500	20.88%	+0.40%
Nikkei 225	20.00%	+0.83%
Eurostoxx 50	20.23%	+0.12%

Source Bloomberg / Partner Banks  
 Data as at 18<sup>th</sup> November, 10.30am

Upcoming events	
23 <sup>rd</sup> Nov	Eurozone PMIs
25 <sup>th</sup> Nov	UK GDP estimates



## FRIDAY NIGHT 'LIGHTS

### Common concerns

#### **Inventory**

Banks are always under pressure to reduce their balance sheet costs. Holding inventory on their books will inevitably attract some kind of working capital charge. Prior experience has taught us that banks have the tendency to indiscriminately retire inventory without consideration of end clients. Where we come in is to ensure we manage this aggressively to enable our clients access to these products for as long as possible. The way we do this is by understanding our clients demands and flow requirements and articulate this back to our partnering banks so that the correct amount of inventory is held for the right period of time.

#### **Secondary market as a profit backup to the primary market**

A common perception is that the secondary market is used as a tool to support the profitability of the primary issuance. One particular scenario is where an issuer may hook investors in by offering a product that squeezes any profitability out on day one and then widen offer levels out in the secondary market to compensate for this. Or indeed show very aggressive terms in a primary auction process and then point to deteriorating market conditions when the trade is actually launched with inferior terms. This type of play is quite damaging for the issuer as it builds a level of distrust within investors.

Conversely there is sometimes a concern that banks take profit on the bids, when clients come to sell back their holdings prior to maturity. The job of Fortem is to monitor and manage the bid – offer spread on these instruments by utilizing our models and experience to ensure that the prices do move in line with underlying market moves.

#### **Conclusion**

Foremost the perception, perhaps tainted by the retail market, that these instruments are illiquid is wrong. They are as liquid as bonds and stocks. Fortem's job for our clients is to utilize our models and experience to ensure clients are serviced fairly in terms of secondary pricing and equally the operational settlement of these instruments is as smooth and trouble free as the bonds and stocks we have referred to throughout this document.

## **Disclaimer**

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