

Establishment of Investors' and Exporters' FX Window: A Floating of the Naira?

This is a further update on the recent developments in the foreign exchange ("FX") market in Nigeria.

The Central Bank of Nigeria ("CBN"), in June 2016, introduced a single flexible Nigeria interbank foreign exchange market ("FX Market"). The CBN stated then that it will only participate in the FX Market through periodic interventions to regulate prices. This will be by either buying or selling FX spots based on valid two-way quotes on the standard amount or by placing orders for non-standard amounts in the FMDQ OTC ("FMDQ") Order Book System (i.e. one-way quote). End users were required to approach the FX market to obtain FX to fund eligible transactions.

Notwithstanding the above, the FX Market continued to experience serious liquidity challenges. Thus, the CBN took several steps to enhance liquidity and ensure timely settlement of eligible transactions. As part of such steps, the CBN issued a circular dated 21st April, 2017 titled "Establishment of Investors' and Exporters' FX Window" (the "Circular") to introduce a special Investors' and Exporters' FX Window ("Window") with effect from 24th April, 2017.

Some of the major highlights of the Circular which you need to know include the following:

- ◆ Transactions for which parties are permitted to access the Window include (i) invisible transactions such as loan repayments and interest payments, dividends/income remittances, capital repatriation, management services fees, consultancy fees, software subscription fees, technology transfer fees, personal home remittances for expatriates, and any other eligible invisible transactions (excluding international airlines tickets sales remittances); (ii) bills for collection transactions; and (iii) any other trade-related payment obligations (at the instance of the customer).
- ◆ All the documentation requirements (including, where applicable, certificates of capital importation or approval of the National Office for Technology Acquisition and Promotion) for eligible transactions for the purchase of FX in the FX Market will continue to apply to transactions carried out in the Window.
- ◆ International airlines and tickets sale remittances are excluded from the Window. These are only eligible to access the CBN FX window (i.e. Secondary Market Intervention Sales – retail and wholesale, spot and forward) ("SMIS").
- ◆ The supply of FX to the Window will be through portfolio investors, exporters (which we believe will include oil companies), Authorised Dealers (i.e. Nigerian banks) and other parties with foreign currency to exchange to Naira (including domiciliary accounts holders). The CBN will also participate in the Window from

time to time (as a buyer or seller) to promote liquidity and professional market conduct.

- ◆ Participants in the Window will trade via documented telephone conversations until appreciable progress is made by corporates in the on-boarding process to the FMDQ Thomas Reuters FX Trading & Auction Systems (“FMDQ Trading System”).
- ◆ The exchange rates for transactions in the Window will be as agreed between Authorised Dealers and their counterparties i.e. on a willing buyer and willing seller basis. In other words, the CBN has not set a band or pegged a rate for the Window.
- ◆ To provide price discovery for participants in the Window, FMDQ will be responsible for polling buying and selling rates and other relevant information from the major participants in the market while the CBN will provide depth until the market moves to the FMDQ Trading System. That means FMDQ will be asking banks and other major participants the rate they purchased or sold FX daily and, thereafter, use that information to determine the average rates and depth of transactions in the Window.
- ◆ FMDQ shall publish the market rates and other relevant information on its website (www.fmdqotc.com) twice daily. The opening rates will be published at 9.00am and closing rates at 4.00pm daily.
- ◆ To provide support for appropriate benchmarking and facilitate derivatives activities in the Window, FMDQ has developed and published a new fixing - the Nigerian Autonomous Foreign Exchange Fixing (“NAFEX”).
- ◆ The NAFEX methodology can be accessed through this link <https://www.fmdqotc.com/wp-content/uploads/2017/04/NAFEX-Methodology-April-21-2017.pdf>.
- ◆ Authorised Dealers are permitted to hold positions subject to their respective foreign currency trading position limits, but may exceed the position with the approval of the CBN.
- ◆ Participants are permitted to hedge their FX exposures. Authorised Dealers are required to provide the market with required FX hedges including forwards, swaps, futures and options.
- ◆ The CBN will continue to provide liquidity in the derivatives market with the Naira-settled OTC FX Futures which will, going forward, settle on NAFEX.
- ◆ The CBN shall offer holders of the Naira-settled OTC FX Futures Contracts (i.e. contracts with April 2017 to March 2018 maturities as at 18th April, 2017) (“Legacy Contracts”) options to settle their contracts on the Nigerian Interbank Foreign Exchange Fixing (“NIFEX”) or NAFEX at their maturity dates.

- ◆ The CBN will offer to holders of Legacy Contracts a choice between settlement of the contracts at the respective (i) NIFEX rates or (ii) NAFEX rates at the maturity dates of such contracts.
- ◆ Where a Legacy Contract holder selects NIFEX, such holder will be eligible to source for FX from the CBN FX Window (i.e. SMIS, the Window or the FX Market) to settle the underlying eligible transaction. Where the holder selects NAFEX, the Legacy Contract holder will only be eligible to source or purchase FX from the Window or the FX Market to settle the underlying eligible transaction.
- ◆ Holders of Legacy Contracts have 40 days from the date of the Circular – i.e. 21st April, 2017 – to inform FMDQ of their preferred settlement option for such contracts. A Legacy Contract holder that has not adopted a settlement option after the 40-day period will be settled at either NIFEX or NAFEX, depending on the type of the hedged eligible transaction(s).
- ◆ Holders of multiple Legacy Contracts are only entitled to choose one settlement option for all their contracts.
- ◆ All Naira Settled OTC FX Futures contracts offered by the CBN after 21st April, 2017 will be settled at the NAFEX rate.

From the above, it appears that the CBN has partially deregulated the FX Market and 'floated' the Naira. This is, however, not yet a full 'float' for the participants in the Window as the CBN will still occasionally intervene in the Window.

This update does not constitute legal advice and should you have any questions regarding these or any other developments, please contact: Aniekan Ukpanah (aniekan.ukpanah@uubo.org), Yinka Edu (yinka.edu@uubo.org), Joseph Eimunjeze (joseph.eimunjeze@uubo.org) and Dolapo Adesina (dolapo.adesina@uubo.org) or your regular UUBO contact.

