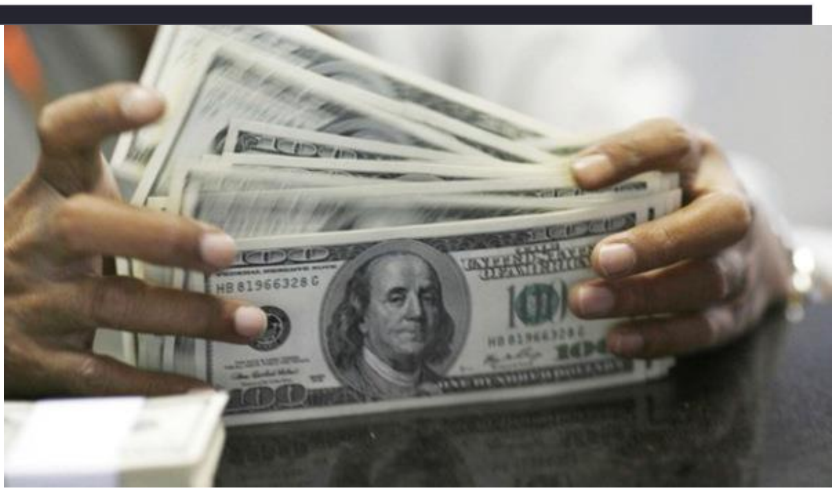
TEMPLARS
www.templars-law.com June 2016 NEWSLETTER

# An Era of Change in the Nigerian Foreign Exchange Market



After weeks and weeks of waiting and speculation, the Governor of the Central Bank of Nigeria ("**CBN**") on June 15, 2016 finally announced certain far-reaching changes to the foreign exchange regime in Nigeria. The announcement was quickly followed by the release of a new set of guidelines for the implementation of the changes. (The new guidelines comprising the (a) Revised Guidelines for the Operation of the Nigerian Inter-bank Foreign Exchange Market; and (b) Guidelines for Primary Market Dealership in Foreign Exchange Products, are together referred to in this client alert as the "**New FX Guidelines**").

Although some details about the practicalities of the proposed changes are still being worked out among the CBN and such stakeholders as bank treasurers and the Nigerian Financial Market Dealers Association, there is no doubt that the changes represent the most ambitious and extensive reordering of the foreign exchange market in Nigeria since the repeal in the 1990s of the Exchange Control Act of 1962.

As market participants and the advisory community continue studying the changes to determine their exact ramifications and impact on both foreign investors and Nigerian businesses, this client alert is intended to highlight some of the headline changes introduced by the new regime.

Below is a summary of some of the key changes introduced by the New FX Guidelines:

### *A single market with "uncapped" and flexible prices*

Among other things, the New FX Guidelines discarded the much-criticised artificial peg on the Naira to U.S. dollar rate of exchange. In addition, the New FX Guidelines have abolished what used to be a dual FX market comprising the CBN window and the inter-bank market, and established in its place a single market structure for foreign exchange which shall be the restructured inter-bank/autonomous market window (the "**New FX Market**").

As a consequence of the above, exchange rates in the New FX Market will no longer be dependent on or be determined by the CBN but will instead be driven by market forces on a daily basis using metrics from FMDQ Thomson-Reuters Order Matching System and the Conversational Dealing Book.

The sale and purchase of FX in the New FX Market shall be on a two-way quote basis between the authorised dealers *via* the FMDQ Thomson Reuters FX Trading Systems (or any other platform approved by the CBN).

### *Participants in the New FX Market*

Under the New FX Guidelines, the following are all entitled to participate in the New FX Market: authorised dealers (*i.e.* CBN licensed banks); authorised buyers (*i.e.* hotels and other corporate bodies appointed by the CBN); oil companies; oil services companies; exporters; end-users (*i.e.* businesses and members of the public requiring FX for CBN designated "eligible transactions"); and any other entity designated as a market participant by the CBN from time to time.

## *Interventions and "Quantitative Easing" by the CBN*

The New FX Guidelines empower the CBN to participate in the New FX Market through periodic interventions to either buy or sell FX as the need arises. Presumably, this would enable the CBN to ensure continuous liquidity in the New FX Market and keep the exchange rate within check from time to time (without necessarily stipulating the rates in the ordinary course of business).

The CBN could exercise the above power by either purchasing or selling FX directly into the New FX Market using the two-way quote system or by selling FX on a wholesale basis to authorised dealers or on a retail basis to end-users through the authorised dealers (provided that such end-users require the FX for "eligible transactions" and submit appropriate documentation).

For the purpose of such interventions and other purposes relating to the New FX Market, the CBN will trade only with a limited number of banks to be registered as Primary Market Dealers in FX upon such banks satisfying certain criteria stipulated under the Guidelines for Primary Market Dealership in Foreign Exchange Products.

## *Derivatives Products in the New FX Market*

Authorised dealers may provide hedging products such as over-the-counter ("**OTC**") Naira-settled FX futures to end-users. Such OTC FX futures must be backed by trade transactions or evidenced investments. The benchmark for the valuation and settlement of the OTC FX futures and other derivatives in the New FX Market shall be provided by FMDQ and the settlement amounts paid by the authorised dealers on OTC FX futures transaction may be repatriated by foreign investors upon presenting the certificates of capital importation ("**CCI**") issued to them at the time of their making the underlying investment into Nigeria.

In the same vein, in order to enhance liquidity in the New FX market, the CBN may also intervene to offer long-tenored FX forwards to the registered primary FX dealers who may purchase such OTC FX futures for their own account or sell to other authorised dealers or end-users. The CBN may also offer such products to end-users (through authorised dealers) for trade-backed transactions.

The introduction of the OTC FX futures transactions in the New FX Market is expected to reduce the demand for FX on the spot market by moving non-urgent FX demands from the spot market to the futures market offered by both the CBN and the authorised dealers.

## *The Notorious 41*

Under the New FX Guidelines, the notorious 41 goods and services (including toothpicks!) which were declared "*Not Valid for Foreign Exchange*" and hence disallowed access to the old official FX market by the CBN in its June 23, 2015 circular (TED/FEM/FPC/GEN/01/010) remain ineligible for the purchase of FX from the New FX Market.

## *More Naira for Foreign Investors*

Foreign investors importing capital into Nigeria and persons receiving money in Nigeria through any of the international money transfer systems may now have more Naira upon conversion of the foreign currency to Naira (whether for the purpose of obtaining CCIs or for any other purpose). This is because the New FX Guidelines allow the proceeds of foreign investment inflows and international money transfers to be purchased by authorised dealers at the market-driven rate in the New FX Market (rather than the fixed rate which existed under the old regime).

## *Still no hope for the BDCs*

The New FX Guidelines do not provide any reprieve for bureaux de change operators, a segment of the FX market which the CBN discontinued the direct sale of FX to in January 2016. This segment of the market continues to be barred from direct access to the New FX Market.

## *Conclusion*

We conclude this newsletter by informing our clients that there has been no change to the modalities for importing investment capital into Nigeria or repatriating investment proceeds from Nigeria. This is because investment capital is still required to be imported into Nigeria through an authorised dealer who then issues a CCI upon conversion of such foreign capital into Naira. Similarly, foreign investors will still be required to present their CCIs when seeking to purchase foreign currency from the New FX Market for the purpose of repatriating their investment proceeds. Going forward, the key impacts of the New FX Guidelines on foreign investors are that (i) the rate of conversion of their foreign capital into Naira is no longer a pre-determined rate and they may now have more Naira for their FX; and (ii) the derivatives products in the New FX Market seems to provide some assurance of liquidity on the settlement dates for repatriation of imported capital.



**Key Contacts:** Chike Obianwu - (Partner) chike.obianwu@templars-law.com; Desmond Ogba (Managing Counsel) desmond.ogba@templars-law.com; and Ayokanmi Aderibigbe (Associate) Ayokanmi.aderibigbe@templars-law.com.