

RECENT CBN REFORMS IN THE NIGERIAN FOREIGN EXCHANGE MARKET

Introduction

Previously, navigating the Nigerian foreign exchange market could be a challenge for foreign businesses and investors. Fluctuations in the Naira exchange rate meant investors received less when converting profits back to their home currency. Repatriating funds could be hindered by a shortage of foreign currency, rendering Certificates of Capital Importation (CCIs) less useful due to limited liquidity. Backlogs in accessing FX further complicated matters. However, recent reforms by the Central Bank of Nigeria (CBN) paint a brighter picture. The Naira has strengthened vis-a-vis the US dollar by approximately 22.42% over the past 3 months (February to April 2024).

The Central Bank of Nigeria in line with its objectives to promote a market-based price discovery system in Nigeria's Foreign Exchange market, has recently implemented a series of reforms aimed at improving the value of the Nigerian Naira, stabilizing the Nigerian foreign exchange (FX) market and fostering a more transparent business environment. These reforms hold significant implications for foreign investors and business owners operating in Nigeria.

For ease of reference, we have collated in this newsletter recent FX policies issued by the CBN.

1. Prohibition of Dollar-Denominated Collateral for Naira Loans

The Central Bank of Nigeria, through a directive issued on April 8, 2024, now prohibits the use of foreign-currency denominated collaterals such as US Dollars or non-export domiciliary accounts for loans issued in Nigerian Naira, with exceptions for specific types of foreign currency collateral such as federal government issued eurobonds or guarantees of foreign banks, including standby letters of credit.

All loans secured by prohibited dollar-denominated collaterals are to be wound down within the next 90 days. Failure to comply with this directive poses significant implications. Defaulting loans would be regarded as being high risk (risk-weighted 150% for capital adequacy ratio computation).

This CBN's directive aims to curb further dependence on US Dollars and boost the Naira's role in the Nigerian economy. By encouraging Naira-denominated collateral for loans, it will further strengthen the Naira.

- 2. Sale of FX to Bureau De Change Operators (BDCs) at the Rate of N1101 per \$1**
The CBN has made available \$10,000 which may be bought by eligible BDCs at N1101 per \$1 (sale price) and must be resold to the retail market at no more than 1.5% of the sale price. All eligible BDCs can now make purchases and pay into designated CBN accounts.

CBN's injection of FX into the system through BDCs, will increase the availability of foreign currency for retail transactions. This will be helpful for individuals and businesses that need dollars for travel, education, or small-scale imports.

- 3. Discontinuation of Limits on Interbank FX Transactions and Removal of Restrictions on Interbank Proceeds**

The CBN by a circular issued on February 8, 2024 removed the $\pm 2.5\%$ cap spread on interbank FX transactions it had imposed in the previous year. The circular also removed the restrictions placed on sale of interbank proceeds to BDCs.

The implication of this is that authorised dealers (financial institutions licensed by the CBN to trade FX) in the interbank FX market would be able to sell the proceeds from the market to BDC operators and a wider range of buyers outside the market. Also, with more buyers and sellers able to participate, FX transactions can happen faster and with less friction.

- 4. Removal of Exchange Rate Limits for International Money Transfer Operators (IMTOs)**

The CBN on January 31, 2024 removed the $\pm 2.5\%$ exchange rate cap for IMTOs and also enabled IMTOs to quote exchange rates for naira payout to beneficiaries based on prevailing market rates. IMTOs were previously required to quote rates within an allowable limit of -2.5% to $+2.5\%$ around the previous day's closing rate of the Nigerian Foreign Exchange Market. CBN's removal of the exchange rate cap for IMTOs is in line with its continued efforts to liberalize the Nigerian FX market.

The removal will allow IMTOs to offer market-driven rates, increasing transparency and potentially leading to more competition and innovation in the money transfer market. By allowing IMTOs to set market-driven rates, the CBN is improving the efficiency of the Nigerian FX market for money transfers.

IMTOs can now offer more competitive rates, which can benefit both senders and receivers of money, internationally. Also, IMTOs may be incentivized to develop new products and services to better serve their customers. This could include faster transfer times or lower fees.

5. Reintroduction of the “Willing Buyer, Willing Seller” FX Market Based Pricing Model at the Investors & Exporters (I & E) FX Window

The CBN in a press release last year abolished all other foreign exchange windows, collapsing all FX market segments into the I & E window and mandated authorized dealers to conduct their foreign exchange transactions on a “Willing Buyer and Willing Seller” basis. Market participants were previously required to sell foreign currency at the CBN rate. This implies that exchange rates would now be determined by market forces of demand and supply.

What are the possible implications of these policies for you and your businesses?

1. A stronger and more stable Naira value minimizes the risk of losses due to currency fluctuations when converting profits into your home currency.
2. Increased FX liquidity should allow for easier repatriation of your capital and profits thereby allowing you to put your CCIs to good use again. This is possible because CBN in a bid to restore credibility and confidence in the Nigerian economy, recently concluded the payment of \$1.5 billion to clear and settle outstanding FX obligations/backlog.
3. The CBN's reforms promote a more transparent FX market, allowing you to make informed decisions with greater confidence.

Conclusion

Nigeria boasts a vast and growing market, offering foreign investors a chance to tap into its immense potential. The recent reforms introduced by the CBN are all concerted efforts to stabilize, strengthen and enhance transparency in the Nigerian foreign exchange market. These initiatives represent a positive step towards aligning Nigeria's foreign exchange market with global best practices, offering a positive outlook for foreign investors seeking to enter the Nigerian market, and we expect that it would ultimately support sustainable economic development.

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