FMDQ SPOTLIGHT

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FMDQ
OTC Securities Exchange
...empowering the Nigerian debt capital & FX markets

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NEW STORIES

CBN Set to Support the Economy with a Liberalised FX Market…Launches Investors’ & Exporters’ FX Window

In a bid to further improve liquidity in the Nigerian Foreign Exchange (FX) Market, the Central Bank of Nigeria (CBN) announced the establishment of a special FX window for Investors, Exporters and End-users via a circular dated April 21, 2017. The special FX window, called the “Investors’ & Exporters’ FX Window” (the I&E FX Window), which sets out a single and autonomous FX market structure, clearly outlines the CBN’s desire to enhance efficiency and facilitate a liquid and transparent Nigerian FX market.

The I&E FX Window shall cater mainly for Invisible transactions (excluding International Airline Ticket Sales’ Remittances), Bills for Collection and any other trade-related payment obligations (at the instance of the customer) and will have Exporters, Foreign Portfolio Investors (FPIs), Foreign Direct Investors (FDIs), Authorised Dealers (Banks) and any other party with autonomous sources of foreign currency, sell US Dollars to willing buyers at mutually agreed rates. The CBN may also participate in this Window from time to time as the apex Bank sees fit.

The introduction of the I&E FX Window by the CBN is an audacious and welcome move towards the resuscitation of the Nigerian FX market which will serve to restore confidence, as improved transparency is a major precursor for further inflows into the market, invariably improving the liquidity of the market. This will help reduce devaluation risk, provide necessary price formation and discovery, encourage efficient allocation of resources, bolster investments and promote hedging opportunities, thereby bringing integrity to the Nigerian FX market, restoring confidence and ultimately supporting economic development.

Consequently, with the establishment of the I&E FX Window, the CBN sets a strong FX Reform agenda and clearly demonstrates its alignment with the Federal Government’s Economic Recovery & Growth Plan (ERGP) by introducing measures to promote the increase in supply and liquidity to the FX market which will in turn reduce exchange rate volatility and inflation in the near-term. Furthermore, with the introduction of this enhanced market-driven structure, Investors’, Exporters’ and End-users’ confidence is enhanced, as liquidity continues to recover in the market.

The CBN also reaffirmed its commitment to continue to bolster liquidity in the derivatives market by continuing to offer Naira-settled OTC FX Futures contracts of non-standardised amounts for different tenors from one (1) month through to twelve (12) months which will settle on bespoke maturity dates, providing liquidity in the product and enabling corporate treasurers effectively and efficiently manage their FX risk. This is also a much-welcomed development as the OTC FX Futures market continues to serve to, *inter alia*, minimise the disequilibrium in the Spot FX market and cause the rate to moderate; attract significant capital flows to the FMDQ-fixed income and equity markets; and achieve exchange rate stability.

Also, in keeping with the progressive nature of the introduction of the I&E FX Window, the CBN announced that it will, going forward, settle its OTC FX Futures contracts on the new Fixing (NAFEX) developed by FMDQ OTC Securities Exchange ("FMDQ" or the "OTC Exchange"), which will be reflective of the activities in the new FX Window. This clearly demonstrates the CBN's total commitment to the establishment of an independent and well-functioning FX market.

In a statement given by Mr. Bola Onadele. Koko, MD/CEO of FMDQ, he affirmed as follows, "the CBN has again demonstrated its unrelenting resolve to resuscitate and support the Nigerian FX market, back to its erstwhile vibrancy and possibly even better. This globally-monitored market is one that unarguably is deeply complex and kudos must be given to the CBN for continuously striving to ensure that the market operates for the ultimate benefit of the Nigerian economy. The introduction of this new FX Window, amidst the other policy actions the CBN is executing in the FX market, is yet another expression of the CBN's commitment to maintain FX market stability whilst striving to attract and retain foreign capital into the economy. FMDQ, on its part, will continue to support the CBN in the achievement of the common objective and other market stakeholders are encouraged to do the same. The Nigerian FX market is indeed on a certain path to recovery. Once the new market is firmly established, focus should be on convergence of the multiple exchange rates and resuscitation of the two-way quote-driven inter-bank market complemented with optimal transparency, which made Nigeria an ideal destination of capital."

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Autonomous FX Fixing Goes Live on FMDQ

As part of its market development initiative, FMDQ, following the recent establishment of the I&E FX Window by the CBN, has proactively developed a new FX Fixing – the **NAFEX**, to support appropriate benchmarking and facilitate derivatives activities in the I&E FX Window.

NAFEX - the Nigerian Autonomous Foreign Exchange Rate Fixing - is essentially the FMDQ reference rate for foreign exchange activities in the I&E FX Window, and is designed to represent the Spot FX market rates in this Window. Having diligently developed an overarching methodology, for the independent and objective generation of this rate, FMDQ, in line with its commitment to support the CBN's activities toward resuscitating the vibrancy of the Nigerian FX market, launched and published the maiden NAFEX on Monday, April 24, 2017. The NAFEX, which is a polled rate derived from FX rates submissions by a selection of Authorised Dealers participating in the I&E FX Widow, was calculated as **$/₦375.33** on the day of its launch.

The Fixing, which, serves as the fixing for the settlement of the Naira-settled OTC FX Futures and other FX derivatives, promotes transparency and awareness of the market-driven USD/NGN rates, thereby enabling foreign and local investors benefit from the independent reference rate. It also provides growth and income potentials for market players through the trading of hedging products, whilst serving as a benchmark for portfolio valuations, conversions, performance measurement and audits for derivatives products.

The real-time NAFEX is published on the FMDQ information - FMDQ e-Markets, at 12:00 noon every business day. For more information, contact bog@fmdqotc.com.

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FMDQ Holds 5th Annual General Meeting

The Board and Management of FMDQ hosted its shareholders to its 5th Annual General Meeting (AGM) at the Intercontinental Hotel, Lagos, on Friday, April 28, 2017.

As part of the ordinary business of this AGM, the shareholders received the Financial Statements of the OTC Exchange for the year ended December 31, 2016, together with the Reports of the Directors and Auditors to the Shareholders. During the AGM, the Shareholders reappointed the Auditors, Messrs. KPMG Professional Services, to serve as the Company's External Auditors for another year, authorised the Directors to fix the External Auditors' remuneration, re-elected the members of the Audit Committee and ratified the appointment of two (2) Directors, Mr. Kennedy Uzoka and Mr. Dapo Akisanya.

Presiding over the AGM, the Chairman of FMDQ, Dr. (Mrs.) Sarah O. Alade, OON, stated that "the OTC Exchange is in a strong position despite the fact that 2016 was a tough year for all Nigerian businesses, FMDQ included. Furthermore, FMDQ was able to sustain its growth by continuing to explore new opportunities to expand and enhance its activities, markets and reach. This expansion was clearly noticeable in the listings and quotations business which saw a total of twenty-seven (27) debt securities, amounting to N233.98bn, listed and quoted on the OTC Exchange, and in the number of FMDQ's members which grew from seventy-five (75), as at December 31, 2015, to one hundred and fifty-seven (157), as at December 31, 2016.

Speaking to the financial performance of the OTC Exchange, the MD/CEO of FMDQ, Mr. Bola Onadele. Koko noted that in 2016, the challenges in the Nigerian financial markets, particularly, the foreign exchange market, resulted in a 1.71% decrease in FMDQ's total revenue to N2.04bn from N2.07bn in 2015. He, however, noted that FMDQ was able to diversify its revenue sources resulting in an increase in the contribution of non-transaction fees to total revenue from 20.56% in 2015 to 32.29% in 2016, in line with its strategic objectives. He further stated that in 2017 the OTC Exchange will focus on, amongst others, the diversification of products offerings to include consolidation of OTC FX futures, the introduction of new derivative products such as fixed income, interest rate and currency derivatives, the establishment of a central clearing house to enhance the credit risk management standards and introduction of post trade services to the OTC cash markets.

At the close of the AGM, Dr. Alade announced her retirement from the Board of FMDQ, effective May 1, 2017, following her retirement from Central Bank of Nigeria which she represented on the Board of FMDQ. She thanked the shareholders for according her the pleasure of serving them and her fellow Board members, FMDQ staff members and Management team for their individual and collective efforts during her tenure.

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Mixta Real Estate PLC Lists ₦4.50bn on the OTC Exchange

On the heels of the approval granted to the Lagos State Government by the Board Listings, Markets and Technology Committee of FMDQ for the listing of the Lagos State ₦47.00bn Bond on the OTC Exchange, in an unrivalled time to market, comes the approval for the listing of the Mixta Real Estate PLC ₦4.50bn Series 1 5-Year 17.00% Fixed Rate Senior Guaranteed Bond (the Mixta Bond) under a ₦30.00bn Medium Term Note Programme on FMDQ. In streamlining the efficiency of its processes and delivering value to both corporate and commercial businesses desirous of accessing the debt capital markets (DCM), FMDQ has continued to avail its credible platform, as well as tailor its Listings and Quotations service to suit the needs of the issuers. Mixta Real Estate PLC, a real estate developer, providing advisory services, and taking on special medium to large scale development projects, therefore, becomes the first real estate bond to be listed on FMDQ's platform in 2017.

By listing on FMDQ, the Mixta Bond enjoys exceptional benefits which include, but are not limited to, enhanced investor confidence in the Mixta Bond, transparent information disclosure, effective price formation and global visibility from the FMDQ-Bloomberg E-Bond Trading and Surveillance System, the FMDQ website and FMDQ e-Markets Portal. A unique listing ceremony is being planned to formally welcome the Mixta Bond onto the platform in the coming weeks, in honour of the issuer, Mixta Real Estate PLC.

Having signed a memorandum of understanding with the Nigeria Mortgage Refinance Company (NMRC) PLC, towards bridging the housing gap in Nigeria through the DCM, the listing of the Mixta Bond on FMDQ, is therefore a welcome development, paving the way for other issuers in the real estate sector, with a view to fully maximising the potential of the DCM in supporting economic growth and development. As the Nigerian DCM-focused OTC Exchange, FMDQ has and shall continue to enable even more issuers key into the offerings of the Nigerian DCM to boost their businesses and there from, build their corporate profiles, and at the same time, establish the necessary governance structures that will instill investor confidence and in turn participation in the DCM.

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UPDC PLC & Nigerian Breweries PLC Quote ₦10.00bn Worth of Commercial Papers on the FMDQ Platform

As market participants continue to align their activities in the wake of the policy reforms shaping the Nigerian financial markets landscape, FMDQ is pleased to welcome the quotations of the UACN Property Development Company PLC ₦7,284,198,000.00 Series 4 - 11 Commercial Paper (CP) Notes under its ₦24.00bn CP Programme; and the Nigerian Breweries PLC ₦2,223,708,000.00 Series 10 CP Notes under its ₦100.00bn CP Programme, to its platform.

In support of the growth of the Nigerian economy, FMDQ championed the resuscitation of the CP market to provide corporate and commercial businesses with the opportunity to meet their short-term funding requirements, whilst building their profiles in the Nigerian DCM space. The time to market for these securities lays credence to the efficiency of the FMDQ quotation process and brings the count of CPs admitted onto the FMDQ platform for Q1 2017 to a total of fifteen (15). As with securities quoted on FMDQ, these CPs will be availed global visibility and governance by the promotion of credibility and transparency of information, as part of the value-add provided by the FMDQ Listings and Quotations service.

FMDQ remains positive about the possibilities of the Nigerian debt capital markets and will continue to articulate and implement, with the support of its key stakeholders, ways to improve and make the Nigerian DCM globally competitive, operationally excellent, liquid and diverse.

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The FMDQ OTC Market Turnover Report shows the turnover on all products traded on the FMDQ secondary market – FX, Treasury Bills (T.bills), Bonds (FGN Bonds, other Bonds (Agency, Sub-national, Corporate & Supranational) & Eurobonds)) and Money Market (Repos/Buy-Backs and Unsecured Placements/Takings). These figures exclude primary market auctions in T.bills and Bonds.

The data, collated from the weekly trade data submissions by FMDQ Dealing Member (Banks), represents trades executed amongst the Dealing Member (Banks), Dealing Member (Banks) & Clients, and Dealing Member (Banks) & the CBN.

FMDQ OTC Market Turnover (January - March 2017)

Product Category	(₦'mm)	($'mm)
Foreign Exchange	2,189,854	7,043
Foreign Exchange Derivatives	4,514,654	14,521
Treasury Bills	18,269,287	58,762
FGN Bonds	3,438,310	11,059
Other Bonds*	1,630	5
Eurobonds	43,651	140
Repurchase Agreements/Buy-Backs	7,705,855	24,785
Unsecured Placements/Takings	285,827	919
Money Market Derivatives	8,820	28
Commercial Papers	-	-
Total	**36,457,888**	**117,264**

No. of Business Days	65	65
Average Daily Turnover	**560,891**	**1,804**

Average $/₦ @ 310.90
mm - million
*Other Bonds include Agency, Sub-national, Corporate & Supranational Bonds
Note: Figures may be subject to change due to potential adjustments from Dealing Member (Banks)
Source: FMDQ Data Portal as @ April 7, 2017; Figures reported by Dealing Member (Banks) on a week-ending basis

The total turnover for January to March 2017 period amounted to ₦36.46trn. Trading activities in T.bills contributed the largest to overall turnover, accounting for 50.11% of the market. Secured market transactions (Repos/Buy-backs) accounted for 21.14%, whilst FX market transactions accounted for 18.39%, Bonds, 9.56%, with Unsecured Placement & Takings, Money Market Derivatives and Commercial Papers representing less that 1%, of overall market turnover.

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Top Ten (10) Dealing Member (Banks) in FMDQ Markets (January - March 2017)

The FMDQ League Table shows the rankings of its top ten (10) Dealing Member (Banks).

RANK	DEALING MEMBER (BANKS)
1	ACCESS BANK PLC
2	ECOBANK NIGERIA LIMITED
3	UNITED BANK FOR AFRICA PLC
4	STANBIC IBTC BANK PLC
5	FIRST BANK OF NIGERIA LIMITED
6	STANDARD CHARTERED BANK NIGERIA LIMITED
7	FBN MERCHANT BANK LIMITED
8	DIAMOND BANK PLC
9	GUARANTY TRUST BANK PLC
10	UNION BANK OF NIGERIA PLC

The top ten (10) Dealing Member (Banks) accounted for 70.84% (₦25.83trn) of the overall turnover in the market, with the top three (3) accounting for 30.38% (₦11.07trn) of this sub-section of the market. Access Bank PLC, Ecobank Nigeria Ltd. and United Bank for Africa PLC topped the League Table for the third month running, ranking 1st, 2nd and 3rd respectively, in the value traded for the overall over-the-counter (OTC) market.

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Fundamentals of Derivatives – Part 1

Derivatives instruments are a strategic asset class and a useful risk management tool required for surviving uncertainties in the financial markets. Over the next three (3) editions of FMDQ Spotlight, this section will focus on this important asset class. Part 1 of the series will provide an overview of derivative products, including the features and types. The second part will discuss the various uses of derivatives and the relevant market stakeholders/players; while the final part will review and provide valuable insights into the Nigerian derivatives market.

What are Derivatives?

Derivatives are financial market products whose values are derived from one or more underlying assets or sets of assets, which can be bonds, stocks, commodities, precious metals, market indices, interest rates, etc. Though the market price of a derivative product is based on and determined by the underlying asset, its ownership is distinct and exclusive. Derivatives can be traded OTC or on organised securities exchanges such as FMDQ OTC Securities Exchange. The basic features of most derivatives products are discussed below:

- **Future settlement date:** A derivatives contract essentially specifies that the underlying asset(s) may be exchanged at a later date, and at a price fixed today. Indeed, it is this time difference between the contract date and settlement date that creates the value traded in a derivatives contract, given that the market price of the underlying asset may be different by the settlement date
- **Symmetrical vs. asymmetrical contracts:** A derivatives contract can be symmetrical – in this case, the parties (buyer and seller) are both bound by an obligation to execute the contract by the settlement date. A derivatives contract can also be asymmetrical, a situation whereby one party has the right, but not the obligation, to follow through with the contract
- **Settlement procedures:** A derivatives contract can be settled in cash (here, the difference in the price of the underlying asset on settlement date and the agreed contract price is computed and paid) or by physical delivery of the underlying asset. However, derivatives contracts are mostly settled in cash
- **Zero-Sum game:** Derivatives contracts are theoretically zero-sum games (excluding the associated transaction costs). By implication, the parties (buyer and seller) are competing, such that when one party wins, the other party loses

Types of Derivatives Products

Broadly speaking, there are three (3) major types of derivatives: Futures/Forward contracts, Options and Swaps.

Futures/Forward contract: In a futures/forward contract, two (2) counterparties agree to exchange a specified quantity of an underlying asset (real or financial) at an agreed-upon price (the strike price) on a specified date (settlement date). Futures/forward contracts are usually written in reference to the spot or today's price and typically used to hedge risk as well as speculate on future prices. Examples of such contracts are foreign currency futures/forwards, interest rate futures/forwards, treasury-bills futures/forwards, etc. The key differences between futures and forwards contracts are summarised in the table below:

Characteristics	Futures Contract	Forward Contract
Definition	A standardised contract, traded on an exchange, to buy or sell an underlying asset at a certain date in future, at specified price	An agreement between two (2) parties to buy or sell an underlying asset at a specified date, at an agreed rate in future.
Structure	Standardised contract	Customised contract
Counterparty Risk	Low	High
Contract size	Standardised/Fixed	Customised/depends on the contract terms
Regulation	Securities exchange	Self-regulated/OTC
Collateral	Initial margin required	Not required
Settlement	On a daily basis	On the maturity date

Source: 5paisa.com

Options Contract: In an option contract, the buyer of an option contract pays a premium to the writer of the option. In return, the buyer acquires the right but not the obligation to buy (call option) or sell (put option) a specified underlying item (real or financial) at an agreed-upon contract price (the strike price) on or before a specified date. The major difference between forward and option contracts is that either party to a forward contract is a potential debtor, whereas the buyer of an option acquires an asset, and the option writer incurs a liability. Options are written on a wide variety of underlying items — such as equities, commodities, currencies, and interest rates. Options can be also written on futures, swaps (known as swaptions), and other instruments.

Swaps Contract: A swap is a derivative contract made between two (2) parties to exchange cash flows in the future in line with a pre-arranged formula. The three (3) most popular swap contracts, which are traded OTC between derivatives market players, are interest rate swaps, currency swaps and commodity swaps. Interest rate swaps typically entail the swapping of interest related cash flows between parties in the same currency, whereas currency swaps are contracts between two (2) institutions to exchange the principal and/or interest payments on loans for equivalent amounts in a different currency. Similarly, a commodity swap is an OTC contract to exchange cash flows, which are dependent on the price of an underlying commodity.

In exploring the fundamentals of the derivatives market, the following terminologies, among others, are key to note:

- **Market Maker**: A market maker is a player who provides both buy and sell quotes to other market participants/traders. The market maker essentially provides liquidity to the derivatives market
- **Bid - Ask Spread:** This is the difference between the bid price (the price the buyer is willing to pay) and the ask price (the price a seller is willing to accept) in a derivatives contract. Market makers always give two (2) sets of prices (buy and sell) in the derivatives market.

- **Strike price**: The price at which the holder of a derivatives contract exercises his/her/its right if it is economic to do so, at the appropriate point in time
- **Call/Put Option:** A **Call Option** conveys to the option buyer the right (but not the obligation) to purchase the underlying asset at a fixed strike price per unit at any time during the life of the option. A **Put Option**, on the other hand, conveys to the option buyer the right (but not the obligation) to sell a predefined quantity of the underlying asset at the pre-determined strike price
- **Margin:** This refers to funds that a derivatives investor/trader must maintain on deposit with his/her/its broker to guarantee his/her/its ability to fulfil his/her/its financial obligation to make or take delivery of the underlying asset
- **Clearing House:** A clearing house is an intermediary between buyers and sellers in the derivatives market, responsible for settling trading accounts, clearing trades, collecting and maintaining margin monies, regulating delivery, and reporting trading data. It guarantees the performance and settlement of exchange traded contracts to its members. Essentially, clearing houses act as third parties to all Futures and Options contracts
- **Exercise Price:** This is the fixed price per unit at which a call option conveys the right to purchase the underlying asset and at which a put option conveys the right to sell the underlying asset
- **Long/Short Position:** Purchasing a derivatives contract puts a trader (buyer) on the long side of the contract, simply referred to as 'going long'. A **short position** is the opposite of going long, and refers to the selling side of a derivatives contract
- **Spot Contract**: A spot contract is a contract for immediate delivery. Since derivatives, by definition, include delivery at a future date, spot contracts usually do not form part of the derivatives market. However, they do provide the reference price/rate for the pricing of Futures, Forwards and Options
- **Expiration Date:** Derivatives are time bound financial instruments. An expiration date is when the contract is finally settled, signifying the end of the agreement. Expiration dates are commonly used with Options contracts
- **Settlement Date:** Settlement date is the day on which a trade or a derivatives contract (particularly Forwards, Swaps or Futures transactions) must be settled either in cash, or via the transfer of the underlying asset

In the second part of the series, we will explore the various uses of derivatives products in the financial markets, as well as the relevant players/stakeholders in derivatives market.

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