FMDQ

Introduction to FMDQ Naira-Settled Exchange-Traded FX Futures

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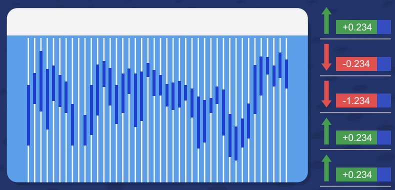
Introducing the FMDQ Naira-Settled Exchange-Traded FX Futures

In line with its mandate to advance economic progress by championing laudable market development initiatives in the Nigerian financial markets and its vision to be the most attractive Exchange in Africa by 2025, FMDQ Securities Exchange Limited ("**FMDQ Exchange**" or the "**Exchange**") seeks to launch the FMDQ Naira-Settled Exchange-Traded FX Futures ("**NSEFF**") to boost the depth and diversity of product offerings in the Nigerian financial markets.

What are FMDQ Naira-Settled Exchange-Traded FX Futures?



FMDQ Naira-Settled Exchange-Traded FX Futures are financial derivatives that create an obligation for the contract holders to exchange cashflows on a specified date based on the predetermined rate of the United States Dollar (USD) relative to the Nigerian Naira (NGN). FMDQ Naira-Settled Exchange-Traded FX Futures are standardised derivatives contracts created by FMDQ Exchange which have the exchange rate of one (1) USD to NGN ($/₦) as the underlying reference. They are a type of exchange-traded derivatives which are used in managing foreign exchange risk, enhancing portfolio performance, and gaining foreign currency exposure for investment purposes.

FMDQ Naira-Settled Exchange-Traded FX Futures Contract Specification

Underlying	Exchange rate of one (1) US Dollar to the Nigerian Naira (i.e. $/₦ exchange rate)
Contract Codes	[MMMYY] NGN - USD
Central Counterparty	FMDQ Clear Limited ("**FMDQ Clear**")
Trading, Clearing, and Surveillance System	FMDQ Proprietary Market ("**Q-ex**") System
Trading Hour	9:00 AM – 3:00 PM
Last Trading Date	Two (2) business days before the Expiry Date of each respective contract (*subject to business day convention rules of FMDQ Exchange*)
Settlement Method	Cash-Settled in Nigerian Naira
Contract Size ($)	100,000.00
Listing Date	As communicated by the Exchange
Expiry Date	Last Wednesday of each Contract Month
Contract Expiration Months	Monthly contracts for thirteen (13) consecutive months and quarterly contracts (March, June, September and December)[1]
Mark-to-Market Methodology	Mark-to-market ("**MTM**") is carried out daily by comparing the initial contract price (on trade day) or previous MTM price (for open positions) with the daily settlement price
Daily Settlement Price	Volume Weighted Average Futures Price for available transactions or Theoretical Futures Price computed from the relevant FMDQ Exchange Spot Fixing and relevant Interest Rate Differential as detailed in the FMDQ Exchange Futures Settlement Price Methodology
Final Settlement Price	FMDQ Exchange Spot Fixing on Expiry Date
Quote Convention	Futures Price; in Nigerian Naira per US Dollars to two (2) decimal points
Eligible Margin Collateral	Initial Margin - Cash and eligible securities[3]; Variation Margin - Cash only

[1]For market launch, only monthly contracts for twelve (12) consecutive months will be introdcued
[3]List of eligible securities will be advised by FMDQ Clear

How FMDQ Naira-Settled Exchange-Traded FX Futures Works?

FMDQ Naira-Settled Exchange-Traded FX Futures contracts approved by the Securities and Exchange Commission (SEC) will be listed for trading and clearing on the FMDQ Q-ex System or any other system designated by the Exchange. The FMDQ Q-ex System, which will facilitate transparency, competitive pricing and seamless execution of trades in FMDQ Naira-Settled Exchange-Traded FX Futures, will be accessible to Derivatives Trading Members of the Exchange for the initiation, execution and management of trades for all users of the FMDQ Naira-Settled Exchange-Traded FX Futures.

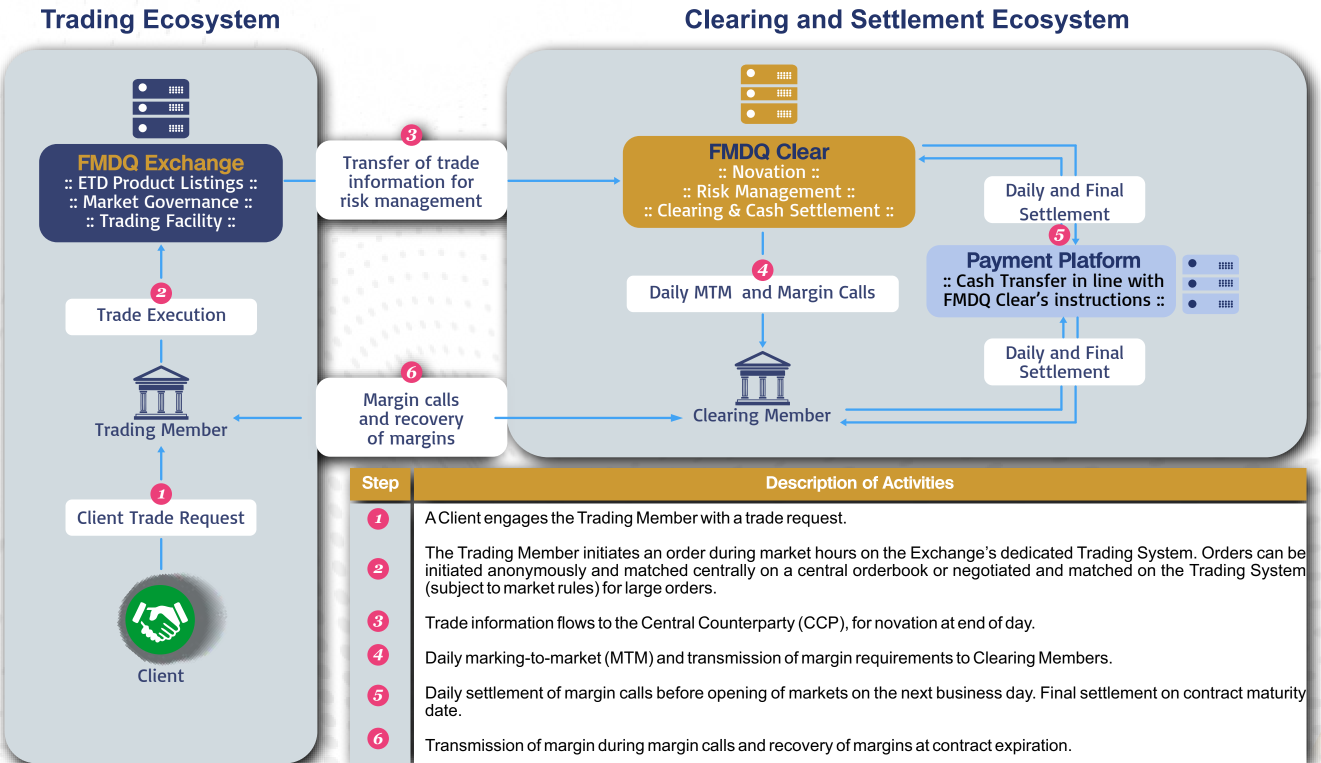
To further promote transparency and price discovery, FMDQ Exchange shall also publish relevant price information for the FMDQ Naira-Settled Exchange-Traded FX Futures via channels accessible to market participants. Derivatives Trading Members of FMDQ Exchange will initiate and execute trades in FMDQ Naira-Settled Exchange-Traded FX Futures for themselves and their clients on the FMDQ Q-ex System. Upon execution of trades in the FMDQ Naira-Settled Exchange-Traded FX Futures, transactions will be centrally cleared by FMDQ Clear via novation *(i.e., becoming the buyer to every seller and the seller to every buyer)*.

Hence, to protect against counterparty risk associated with derivatives transactions, users of FMDQ Naira-Settled Exchange-Traded FX Futures will be required to provide "*good-faith-deposit*" or **Initial Margin** to FMDQ Clear for trades executed in FMDQ Naira-Settled Exchange-Traded FX Futures. The required amount of Initial Margin for each FMDQ Naira-Settled Exchange-Traded FX Futures contract will be determined by FMDQ Clear and displayed as a percentage of the notional value of the contract on its contract specification published on the FMDQ Exchange website.

In addition to the Initial Margin, to further minimise the risk of default in the market, all open positions in FMDQ Naira-Settled Exchange-Traded FX Futures contracts will be valued (marked-to-market) daily by FMDQ Clear, and the resultant daily gains/losses from such valuation will be received/paid as Variation Margins by the holders of such open positions from/to FMDQ Clear through their designated Clearing Members.

The settlement of all Variation Margin obligations must occur before the opening of the market on the next business day. Valuation of open positions to determine Variation Margins will be calculated based on the mark-to-market approach stipulated on the contract specification.

Life Cycle of an FMDQ Naira-Settled Exchange-Traded FX Futures Transaction



Step	Description of Activities
1	A Client engages the Trading Member with a trade request.
2	The Trading Member initiates an order during market hours on the Exchange's dedicated Trading System. Orders can be initiated anonymously and matched centrally on a central orderbook or negotiated and matched on the Trading System (subject to market rules) for large orders.
3	Trade information flows to the Central Counterparty (CCP), for novation at end of day.
4	Daily marking-to-market (MTM) and transmission of margin requirements to Clearing Members.
5	Daily settlement of margin calls before opening of markets on the next business day. Final settlement on contract maturity date.
6	Transmission of margin during margin calls and recovery of margins at contract expiration.

Difference Between FMDQ Naira-Settled Exchange-Traded FX Futures and Extant Naira-Settled OTC FX Futures

	Naira-Settled Exchange-Traded FX Futures	Naira-Settled OTC FX Futures
Listed and Traded on an Exchange	✓	✓
Bilaterally Negotiated and Executed	✗	✓
Standardised Quantity	✓	✗
Standardised Tenor	✓	✓
Margining and Daily Mark-to-Market	✓	✓
Novated by FMDQ Clear	✓	✗
Bilateral Counterparty Risk	✗	✓
Request for Eligible Underlying Transaction	✗	✓

Target Users & Uses of the FMDQ Naira-Settled Exchange-Traded FX Futures

The target users of FMDQ Naira-Settled Exchange-Traded FX Futures includes banks, non-bank financial institutions, government & government-related entities, corporates and other financial market participants with FX risk exposure inherent in their day-to-day economic activities.

BANKS

- **Banks** are exposed to FX risk from their currency trading activities (buying and selling of foreign currencies) and their lending activities (provision of loans denominated in foreign currency, as well as Naira-denominated loans with collaterals/underlying assets denominated in foreign currency), as part of their banking activities. Hence, they bear financial losses arising from the fluctuations in exchange rates of the US Dollar to the Nigerian Naira. Consequently, banks need the FMDQ Naira-Settled Exchange-Traded FX Futures to hedge their FX risk, as well as enhance the return on their trading activities

- **Non-Bank Financial Institutions (NBFIs)** such as Pension Funds Administrators (PFAs), Insurance Companies, Asset Managers, etc., also face FX risk and potential financial losses due to their investment, operating and financing activities (holdings in asset and financial obligations denominated in foreign currency). As a result, they can also use the FMDQ Naira-Settled Exchange-Traded FX Futures contracts to manage their risks and possibly guarantee/enhance return levels on their portfolios

NON-BANK FINANCIAL INSTITUTIONS

GOVERNMENT &
GOVERNMENT-RELATED ENTITIES

- **Government & Government-Related Entities** also face FX risk on revenue (e.g, export proceeds, fees/levies/royalties denominated in foreign currency, etc.), and expenditure (cost of imports and other resources denominated in foreign currency related to capital expenditures, financing obligations on loans denominated in foreign currency, etc.). As a result, they also need the FMDQ Naira-Settled Exchange-Traded FX Futures to hedge the FX risk exposure and ensure efficient planning and budgeting

- **Corporates and Other Financial Market Participants** may utilise the FMDQ Naira-Settled Exchange-Traded FX Futures for the following purposes:
  - Hedge FX risk on their imports and other purchases denominated in foreign currency
  - Hedge FX risk on their asset and other investment denominated in foreign currency
  - Hedge FX risk on their financial obligations (interest, dividend, and principal) from loans and other capital instruments denominated in foreign currency
  - Investment to preserve capital by gaining exposure to FX returns

CORPORATES

Practical Examples of the Uses of FMDQ Naira-Settled Exchange-Traded FX Futures

The tables below analyse, per practical example, the break-even point in the Futures transaction, i.e., estimation of the pay-off in the Futures position and how it offsets the gains/losses in the Spot market, and the estimated Cost of Hedge expected to be incurred entering the hedge

a. Hedging Net Open FX Position in US Dollars by a Bank

A Nigerian bank operating in multiple countries which trades various currencies as part of its day-to-day treasury activities bought $100.00mm and sold $90.00mm on the same day, leaving it with a net open FX position of $10.00mm (i.e., the bank has $10.00mm which it plans to sell within 1 month) at an exchange rate of $/₦750.00. The bank is wary of a depreciation in the value of the US Dollar against the Naira (i.e., a decrease in the exchange rate to $/₦745.00) over the next month which will result in an FX loss to the bank (because it would have to sell its $10.00mm cheaper than it bought it today), as such, the bank is looking to lock-in a price for the future sale of its $10.00mm, at the current price of $/₦750.00 or more.

To hedge against this anticipated FX risk, the bank can hedge its net open FX position by selling 100 units [That is $100,000.00 (Contract Size) * 100 units = $10.00mm] of the 1-month FMDQ Naira-Settled Exchange-Traded FX Futures contract at $/₦750.00 to hedge against the anticipated fall in exchange rate.

Through this trade, the gains/losses on the position in the 1-month FMDQ Naira-Settled Exchange-Traded FX Futures contract will offset the gains/losses in the Spot FX market in a month.

Break- Even Analysis

Sale of 1M FMDQ Naira-Settled Exchange-Traded FX Futures	
Parameter	Value
Amount to be Hedged ($'mm)	10.00
Futures Price at Trade Date ($/₦)	750.00
Number of Sold Contracts	100
Futures Settlement Price at Maturity ($/₦)	745.00
Futures Position Profit/(Loss) (₦'mm)	**50.00**
Cost of bank's $10.00mm net long Spot FX position at $/₦750.00 (Futures Contract Trade Date) (₦'bn)	7.50
Sale of bank's $10.00mm net long Spot FX position at $/₦745.00 (Futures Maturity Date) (₦'bn)	7.45
Mark-to-Market Profit/(Loss) in Spot Market Position (₦'mm)	**(50.00)**

Cost of Hedge

Applicable Cost for Selling a 1M FMDQ Naira-Settled FMDQ Exchange-Traded FX Futures Contract	
Parameter	Value
Futures Price ($/₦)	750.00
Number of Contract(s)	100
Amount Hedged ($)	10,000,000.00
Contract Notional Amount (₦)	7,500,000,000.00
Cost of Hedge Simulation	
Fee Type	Amount (₦)
Transaction	112,500.00
Clearing	7,500,000.00
Maintenance	1,137,500.00
Total Cost of Hedge	**8,750,000.00**

b. *Hedging Potential Insurance Claims Payout in US Dollars by an Insurance Company*

A non-life insurance company (ABC Ensure) operating in Nigeria which insures oil & gas assets and installations against fire and theft has insured the assets of an Upstream Energy – an oil & gas firm, valued at $5.00mm. Under the insurance contract, ABC Ensure would be required to pay Upstream Energy $5.00mm as claims payout if the insured assets are damaged by fire. ABC Ensure has assessed the risk in Upstream Energy's operations and estimated that the probability of a fire accident affecting Upstream Energy's insured assets is ***very high***. Thus, ABC Ensure has made a decision to set aside funds in Naira to be able to meet any claim payout obligation in three (3) months, with respect to Upstream Energy's insured assets. However, ABC Ensure is wary of exchange rate fluctuations and the cost of purchasing USD in 3 months' time to be able to settle the potential $5.00mm claim payout obligation on Upstream Energy's insured assets.

To safeguard against FX risk, ABC Ensure would need to buy 50 units of the 3-month FMDQ Naira-Settled Exchange-Traded FX Futures [That is $100,000.00 (Contract Size) * 50 units = $5.00mm] to hedge against the anticipated rise in the exchange rate.

Through this trade in the 3-month FMDQ Naira-Settled Exchange-Traded FX Futures contracts, the gains/losses in the Spot FX market will offset the losses/gains on the FMDQ Naira-Settled Exchange-Traded FX Futures, thereby ensuring ABC Ensure is able to purchase the USD at the exchange rate it hedged itself.

Purchase of 3M FMDQ Naira-Settled Exchange-Traded FX Futures	
Parameter	Value
Amount to be Hedged ($'mm)	5.00
Futures Price at Trade Date ($/₦)	745.00
Number of Purchased Contracts	50
Futures Settlement Price at Maturity ($/₦)	750.00
Futures Position Profit/(Loss) (₦'mm)	**25.00**
ABC Ensure Potential Claims Payout Obligation at $/₦750.00 (Futures Contract Trade Date) (₦'bn)	3.75
ABC Ensure Actual Claims Payout Obligation at $/₦755.00 (Futures Maturity Date) (₦'bn)	3.78
Mark-to-Market Profit/(Loss) in Spot Market Position (₦'mm)	**(25.00)**

Applicable Cost for Buying a 3M FMDQ Naira-Settled FMDQ Exchange-Traded FX Futures Contract	
Parameter	Value
Futures Price ($/₦)	745.00
Number of Contract(s)	50
Amount Hedged ($)	5,000,000.00
Contract Notional Amount (₦)	3,725,000,000.00
Cost of Hedge Simulation	
Fee Type	**Amount (₦)**
Transaction	55,875.00
Clearing	3,725,000.00
Maintenance	1,694,875.00
Total Cost of Hedge	**5,475,750.00**

c. Hedging Of Revenue in Foreign Currency by a Government Agency

Naira Corportation is a Nigerian Government agency which earns its revenue from receiving fees & royalties paid in USD, has to finance its operations (staff salaries and other operating expenses) in Nigeria primarily by selling its USD revenue receipts. Any shortfall between the Naira proceeds from the sale of its USD revenue receipts, and its total operating expense is fulfilled by the Federal Government.

In recent times, the Naira has appreciated against the USD (with exchange rates dropping from $/₦750.00 to $/₦730.00 in the last 1 month). The Management of Naira Corporation is concerned about the further appreciation of the Naira and its impact on their ability to meet their financial obligations with respect to staff salaries and benefits, especially as the Federal Government recently announced that it would stop providing budgetary support to revenue-generating government agencies such as Naira Corporation.

Consequently, Naira Corporation is looking to hedge its estimated monthly revenue of $10.00mm for each of the next three (3) months against further appreciation of the Naira. To hedge against this unwanted impact of further appreciation of the Naira against the USD, Naira Corporation would need to sell 100 units each [That is $100,000.00 (Contract Size) * 100 units = $10.00mm] of the 1-month, 2-month and 3-month FMDQ Naira-Settled Exchange-Traded FX Futures contracts today at $/₦730.00, $/₦725.00 and $/₦720.00, respectively to hedge against the anticipated decrease in exchange rate.

It is expected that the gains/losses from the future sale of USD (from revenue receipts) by Naira Corporation will offset the losses/gains on its FMDQ Naira-Settled Exchange-Traded FX Futures contracts.

Sale of 1M, 2M and 3M FMDQ Naira-Settled Exchange-Traded FX Futures

Parameter	Value		
Amount to be Hedged ($'mm)	10.00	5.00	5.00
Futures Price at Trade Date ($/₦)	730.00	725.00	720.00
Number of Purchased Contracts	100	100	100
Futures Settlement Price at Maturity ($/₦)	725.00	720.00	715.00
Futures Position Profit/(Loss) (₦'mm)	**50.00**	**50.00**	**50.00**
Naira Corporation Estimated Monthly Revenue at applicable monthly $/₦ rates (Futures Contract Trade Date) (₦'bn)	7.29	7.24	7.19
Naira Corporation Actual Monthly Revenue at applicable monthly $/₦ rates (Futures Maturity Date) (₦'bn)	7.24	7.19	7.14
Mark-to-Market Profit/(Loss) in Spot Market Position (₦'mm)	**(50.00)**	**(50.00)**	**(50.00)**

Summary of Applicable Cost for Selling 1M, 2M and 3M FMDQ Naira-Settled Exchange-Traded FX Futures Contracts

Parameter	Value		
	1-month	2-month	3-month
Futures Price ($/₦)	730.00	725.00	720.00
Number of Contract(s)	100	100	100
Amount Hedged ($)	10,000,000.00	10,000,000.00	10,000,000.00
Contract Notional Amount (₦)	7,300,000,000.00	7,250,000,000.00	7,200,000,000.00
Cost of Hedge Simulation			
Fee Type	**Amount (₦)**		
Transaction	109,500.00	108,750.00	108,000.00
Clearing	7,300,000.00	7,250,000.00	7,200,000.00
Maintenance	1,107,166.67	2,199,166.67	3,276,000.00
Total Cost of Hedge	**8,516,666.67**	**9,557,916.67**	**10,584,000.00**

a. *Hedging of Assets Denominated in Foreign Currency*

A Fund Manager in Nigeria currently holds $1.00mm worth of 2-Year US Sovereign Bond in one of its portfolios. Due to inherent volatility in the FX market and exchange rate fluctuation, the Fund Manager faces the risk of potential losses in the portfolio due to the decrease in the Naira value of its US Sovereign Bond assets as a result of a potential appreciation of the Nigerian Naira against the US Dollar.

In recent times, the Naira has appreciated against the USD (with exchange rates reducing from $/₦750.00 to $/₦730.00 in the last 1 month). The Fund Manager is concerned about the further appreciation of the Naira and its impact on the valuation of its holdings in the 2-Year US Sovereign Bond.

To hedge against this anticipated FX risk of Naira appreciating against the US Dollar over the next nine (9) months until its next financial reporting date, the Fund Manager would need to sell 10 units [$100,000.00 (Contract Size) *10 units = $1.00mm] of the 9-month FMDQ Naira-Settled Exchange-Traded FX Futures at $/₦730.00 today.

As is customary, the resulting gains/losses on the Fund Manager's position in the 9-month FMDQ Naira-Settled Exchange-Traded FX Futures contract will offset the valuation losses/gains on the 2Y US Sovereign Bond.

Sale of 9M FMDQ Naira-Settled Exchange-Traded FX Futures	
Parameter	Value
Amount to be Hedged ($'mm)	1.00
Futures Price at Trade Date ($/₦)	730.00
Number of Purchased Contracts	10
Futures Settlement Price at Maturity ($/₦)	725.00
Futures Position Profit/(Loss) (₦'mm)	**5.00**
Value of Fund Manager's Bond Position at $/₦729.00 (Futures Contract Trade Date) (₦'mm)	729.00
Value of Fund Manager's Bond Position at $/₦724.00 (Futures Maturity Date) (₦'mm)	724.00
Mark-to-Market Profit/(Loss) in Spot Market Position (₦'mm)	**(5.00)**

Summary of Applicable Cost for Selling a 9M FMDQ Naira-Settled FMDQ Exchange-Traded FX Futures Contract	
Parameter	Value
Futures Price ($/₦)	730.00
Number of Contract(s)	10
Amount Hedged ($)	1,000,000.00
Contract Notional Amount (₦)	730,000,000.00
Cost of Hedge Simulation	
Fee Type	Amount (₦)
Transaction	10,950.00
Clearing	730,000.00
Maintenance	996, 450.00
Total Cost of Hedge	**1,737,400.00**

Getting started and using FMDQ Naira-Settled Exchange-Traded FX Futures

Step 1

Engage an FMDQ Derivatives Trading Member to discuss hedging and investment needs using FMDQ Naira-Settled Exchange-Traded FX Futures towards opening a client account

Step 2

Send the trade request for the relevant FMDQ Naira-Settled Exchange-Traded FX Futures contract to the FMDQ Derivatives Trading Member

Step 3

Deposit relevant Initial Margin requested by the FMDQ Derivatives Trading Member to enter the position in the relevant FMDQ Naira-Settled Exchange-Traded FX Futures contract

About FMDQ Group

FMDQ Group PLC ("FMDQ Group") is Africa's first vertically integrated financial market infrastructure group, strategically positioned to provide registration, listing, quotation and noting services; integrated trading, clearing & central counterparty, settlement, and risk management for financial market transactions; depository of securities, as well as data and information services, across the debt capital, foreign exchange, derivatives and equity markets, through its wholly owned subsidiaries – FMDQ Exchange (Nigeria's Largest Exchange by Market Turnover), FMDQ Clear Limited (Nigeria's Foremost Central Counterparty), FMDQ Depository Limited (Nigeria's Integrated Securities Depository) and FMDQ Private Markets Limited (Nigeria's Private Capital Information Repository).

About FMDQ Exchange

FMDQ Exchange is a wholly owned subsidiary of FMDQ Group, registered by the Securities and Exchange Commission (SEC), Nigeria, as an over-the-counter Market (2012) and subsequently as a Securities Exchange (2019), to focus on organising the markets within its purview and creating an efficient platform for the registration, listing, quotation, trading and reporting of financial securities.

To know more about the FMDQ Naira-Settled Exchange-Traded FX Futures and other hedging opportunities provided by FMDQ Exchange, contact Derivatives Business Group via:

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