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CBN CIRCULAR ON "NET OPEN POSITION" TO ALL BANKS

INTRODUCTION

The Central Bank of Nigeria has highlighted concerns over the trend of banks holding large foreign currency position with the hope of making profit from exchange rate fluctuations. The CBN by a circular titled "Harmonisation of Reporting Requirements of Foreign Currency Exposures of Banks", and dated January 31, 2024 issued guidelines to reduce the risks associated with holding large foreign currency position.

HIGHLIGHTS OF THE CIRCULAR

- The Circular amongst other things mandates Banks to adhere to and maintain a Net Open Position (NOP) limit not exceeding 20% short and 0% long of shareholders' fund unimpaired by losses, using the Gross Aggregate Method. The CBN has directed that Banks with current NOPs exceeding the prescribed limits should adjust their positions to comply with the Circular by February 1, 2024.

- In simple terms, Net Open Position is the difference between a bank's foreign currency assets and liabilities, including the assets and liabilities itemized on and off the bank's balance sheet.

- The Circular also mandates banks to calculate their daily and monthly NOP and Foreign Currency Trading Position using specific templates provided by the CBN.

- The Circular emphasized employing strategic financial practices in order to mitigate foreign currency risks effectively. The strategic financial practices include borrowing and lending in the same currency, aligning the interest rate for borrowing with the interest rate for lending and eliminating discrepancies in floating and fixed interest rates.

- The Circular further provides that where a bank fails to comply with NOP limits, such non-compliance may result in immediate sanctions and possible suspension from participating in the foreign exchange market.

CONCLUSION

The implementation of the Circular may lead to the immediate reprieve for the foreign exchange market as banks will be required to liquidate their net long positions by selling forex into the market and effectively increasing the supply of forex.