THE PRIVATISATION OF THE COMMODITIES EXCHANGE AND PROSPECTS FOR THE DIVERSIFICATION OF THE NIGERIAN ECONOMY

Nigeria is a resource-rich country, but the focus has been on the production and exportation of crude oil and oil products. With the prolonged downturn in oil prices, more than ever, it is imperative for Nigeria to move from being a mono-product economy to one with a more diverse revenue base. Agriculture has been touted as the new oil.

Although approximately 78% of Nigeria’s land area is agricultural land, of which roughly half is arable, with the discovery of oil, Nigeria permitted its agricultural sector to stagnate and eventually the country became a net importer of food. According to the Central Bank of Nigeria (CBN) report, a sum of $949 million was spent on the importation of sundry food items within the first five months of 2015. Between January and May 2015, the CBN had spent at different times; $575 million on importation of wheat and $374 million on importation of fish.\(^1\) It is expected that this new administration will reverse this trend and strengthen Nigeria’s underdeveloped commodities market.

The Nigeria Commodities Exchange (NCX), formerly referred to as the Abuja Stock Exchange, is the Government body responsible for facilitating commodities trading in Nigeria, and has been in existence since 1998. The NCX was introduced as a means of diversifying the economy and expanding the scope of export commodities, with particular emphasis on the agro-economy. However, due to poor funding, among other reasons, this purpose has not been achieved. Following the trend of privatization of neglected Government assets, the Government has decided to cede ownership and control of the NCX to the private sector, in the hope this will jumpstart commodities trading in Nigeria.

This article will assess the potential impact of the privatization of the NCX and its role in ensuring the expansion of commodities trading in Nigeria.

**Current Structure of Commodities Trading**

Commodities include agricultural produce, livestock and its derivative products, extractive minerals and all other goods and articles, except all services, rights and interests in which contracts for future delivery are presently or in the future dealt in\(^2\).

Trading on the NCX is governed by its Trading Rules and Regulations which provide that the NCX will, for the time being, operate the spot market and forward market segments. The spot market is designed for trading arrangements in commodities for immediate payment and delivery. Trading in the spot market segment takes place either on the floor or through remote

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2. Rule 256 of the Securities and Exchange Commission Rules 2013
negotiated trading platforms. The forward markets, on the other hand, are for trading arrangements in commodities not meant for immediate payment and delivery.

Before trading can be permitted to take place, the seller must have deposited the commodities in any NCX accredited warehouse or in any warehouse of his choice in different parts of the country where they would be issued electronic receipts stating details such as the commodity type, quality, quantity, owner and other relevant information that may be useful to intended buyers and investors. After the trade is executed, the record is submitted to the clearing agency, which matches the buyer and seller records and confirms that the parties agree to the terms. The clearing, registration and settling of contracts transacted in the NCX is carried out by the Clearing and Settlement Department.

Following the clearing process, the delivery requirements of the subject of trade are fulfilled through the settlement process. The seller tenders a delivery notice along with the certified warehouse receipt of stocks held at the warehouse. The buyer then makes payment upon assignment of the delivery order by the Clearing House, followed by assignment of certified warehouse receipt(s) in its favor by the Clearing and Settlement Department.

**Privatization of the Exchange is Overdue**

The success of a commodity exchange is dependent on the availability of both physical and complementary infrastructure. The NCX is currently operating below potential as a result of poor funding, which has led to both infrastructural and logistics gaps. Inadequate market and trading facilities such as warehouses, storage facilities, laboratories, communication networks and modern IT infrastructure, integral to the day to day functionalities of the NCX has led to inefficient operations and very low trading volumes.

Privatization of the NCX would provide the opportunity for investors to utilize both existing and additional resources to close the existent infrastructural gap and in turn improve trading volumes. In jurisdictions where commodity trading is conducted via privately established commodities exchanges, trading volumes are impressive. For example in South Africa, the South African Futures Exchange (SAFEX) trades well over a hundred thousand contracts a month since 2001. This has placed the exchange as the continent’s largest commodity exchange. From all indications, it is clear that the privatization of the NCX is overdue if trading capacity in commodities is to improve in Nigeria.

**The Privatization Process – Work in Progress**

The Public Enterprises (Privatization and Commercialization) Act (the Act) provides the legal framework for privatization of a number of public enterprises, including the NCX, which is

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4 The Exchange was bought out by the Johannesburg Stock Exchange in 2001
5 Guidebook on African Commodity and Derivatives Exchanges
slated for full privatization. Therefore, the Federal Government will divest its entire shareholding in the NCX.

The privatization of NCX commenced in June 2014 when the Bureau of Public Enterprise (BPE) advertised for Expressions of Interest (EOI) from prospective advisers that will recommend the appropriate transaction structure for the privatization process. The BPE is the body charged under the Act with the responsibility of implementing the National Council on Privatization’s (NCP) policy on privatization and commercialization. The BPE then directed that Requests for Proposal (RFP) be sent to six consortia of transaction advisers shortlisted at the EOI stage. After submission and evaluation of RFPs, in April 2015, the NCP requested the BPE to invite Banca Leonardo Consortium (Germany), United Capital Consortium (Nigeria), CPCS Transcom Consortium (Barbados) and BGL Consortium (Nigeria) to participate in the Financial Bid Opening stage to enable the appointment of advisers that will recommend the appropriate transaction structure for the privatization process. The company with the best offer on quality and cost would be made transaction advisers to the NCX privatization process. Once the final structure of the process is in place, the BPE will oversee the privatization of the NCX. The actual privatization process of the NCX will commence when adverts are placed to invite bidders and investors to express interest.

Steps are currently being taken to ramp up the value of the NCX prior to its sale. For example, the Nigeria Sovereign Investment Authority, as part of its statutory mandate to receive, manage and invest government revenue for the development of critical infrastructure, has expressed interest in making a pre-privatization equity investment in the NCX of about $20 million.

The Great Expectations for Privatization of the Exchange
By privatizing the NCX, the Government aims overall to overhaul the NCX’s operations so that it begins to function at an optimal level, and thereby expand the commodities market and ultimately the economy. At a micro level, privatization of the NCX is intended to inject much needed funding into the Exchange, which consequently would improve the Exchange’s infrastructure, increase market participants’ access to finance, diversify commodities traded on the Exchange and create more jobs. At a macro level, it is expected that the privatization process would primarily impact on the agro economy as it would improve trade volumes and encourage large scale farming.

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6 Sections 13-16 Public Enterprises (Privatization and Commercialization) Act
a. **Improvement of Infrastructure and Commodities Trading**

Private sector participation and investment in the NCX is expected to bridge the infrastructural gap that currently exists and improve commodities trading in Nigeria. In 2014, the NCX launched a pilot e-warehouse receipt system whereby farmers may store their agricultural produce in one of the NCX’s four accredited warehouses where it will be preserved for sale. It is anticipated that privatization of the Exchange would increase investment in more storage facilities and warehouses which would further mitigate the risks of spoilage and waste of commodities and insecurity of available commodity output, amongst others. This would increase farmers’ bargaining power, since they can choose not to sell their produce at harvest time where supply exceeds demand and prices are low.

Once privatized, the NCX also intends to upgrade its trading platform, key to improving trading volumes and the scale of commodities transactions. In all, a rise in participation in the sector is expected, which in turn will increase income for all stakeholders.

b. **Increased Access to Finance**

Market commentators indicate that private sector investment in NCX core infrastructure would decrease price volatility and uncertainty of available production and supply quantity which are associated with the underlying commodities market. Consequently, this would attract market participants much needed funding and investment from financial institutions that are currently hesitant to provide capital.

c. **Commodity Diversification**

At inception, the NCX was created to help farmers manage production and marketing risks, while improving commercialization and growth of their agricultural produce. The NCX has placed emphasis on agricultural produce to the detriment of other commodities like extractive minerals. Private investors are primarily profit-oriented and do not have a social responsibility to focus strictly on developing the agro-economy. As such, it is likely that privatization will usher in diversification of the types of commodities traded on the NCX so that private investors can maximize their profit.

d. **Job Opportunities**

With the diversification of commodities traded on the Exchange, the expectation is that this would lead to the creation of more jobs which cut across different sectors of the economy including transport, packaging, and logistics.

**The Need for a Holistic Approach**

The SEC Rules on Commodity Exchanges would be useful for the NCX post privatization as it prescribes general corporate governance guidelines for the NCX and capital market operators of the NCX. The Trading Rules and Regulations of the NCX would also provide for the...
procedural requirements of trading in the NCX which would prove useful to trading members and market participants post privatization.

However, it is important to note that the anticipated impacts of the privatization process highlighted above would never be fully realized without an enabling environment that would foster commodities trading in Nigeria. This can occur through the implementation of policies tailored to improving trading volumes in the NCX. Following the example of Ethiopia, the Government may implement policies that make it mandatory for large industries and processors that use raw materials and feedstock in their various manufacturing businesses, to purchase certain commodities via the NCX. In Ethiopia, it became compulsory for traders and exporters of coffee to go through the Ethiopian Commodities Exchange.

Furthermore, it is necessary for the NCX to develop a Basis Grade system for traded commodities. This means that the NCX would develop a minimum accepted standard that a commodity must meet before it can be traded on the NCX. This is necessary to ensure uniformity of traded commodities since a given commodity (e.g. rice) may vary drastically in quality. Standards would also ensure that market participants produce what the market requires to avoid wastage. Pre-approved criteria for owners of infrastructure such as warehouses and silos are also integral. These may include criteria relating to technical expertise, ownership of necessary equipment for bulk handling of commodities and insurance.

**Conclusion**

Privatization of the NCX has become necessary due to inadequate funding that has resulted in a dearth in operational and complementary infrastructure of the NCX. It is expected that the privatization process would improve infrastructure and commodity trading volumes, increase access to finance, enable diversification of the commodities currently traded on the NCX and increase job opportunities available to the labor market. It is however important to note that a more holistic approach would be required in fully attaining the desired impact of the privatization process. As such, it is important that the government but also enables the environment where the Nigerian commodities market can foster. This can only be achieved through the enactment and implementation of appropriate government policies and directives.

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