UNDERSTANDING NOFR AND ITS POTENTIAL MARKET IMPACT

The introduction of the Nigerian Overnight Financing Rate represents a significant step towards modernising Nigeria's financial benchmarks and aligning its money market with global best practices.

INTRODUCTION

Over the years, the Nigerian financial market has operated without a single reliable benchmark rate that accurately reflects prevailing day-to-day market transactions and funding conditions. On 17 April 2026, the Central Bank of Nigeria (CBN), in collaboration with the Financial Markets Dealers Association (FMDA), announced its introduction of the Nigerian Overnight Financing Rate (NOFR) as the standardised benchmark of the Nigerian money market.

Previously, and unlike more developed financial markets, pricing in the Nigerian financial market was anchored on a range of disparate rates, including the Monetary Policy Rate (MPR), the Nigerian Interbank Offered Rate (NIBOR), the Open Buy Back (OBB) Rate, the interbank call rate, and treasury bill yields. Rather than a single, transaction-based, secured overnight rate, the market effectively relied on a mix of indicators serving different purposes, ranging from a policy signalling rate, to quote-based benchmarks, sovereign borrowing rate, and distinct overnight lending rates under varying collateral framework – all of which collectively functioned as pricing references for financial transactions.

However, these indicators do not always reflect the actual market activity, due to factors such as limited trading activities or inconsistent transaction reporting. As a result, the

indicators often fail to accurately capture the true cost of short-term funding in the Nigerian financial system.

The effect of this gap was fragmented pricing across banks, driven by differences in internal liquidity positions. As a result, similar transactions within the market were often executed at significantly different rates, with no single benchmark serving as a standard basis for comparison. The lack of a single benchmark also heightened perceived risks for foreign investors, contributing to higher borrowing costs across the economy.

More importantly, without a single benchmark rate, the monetary policy signals of CBN were transmitted into the market gradually and inconsistently when considered alongside other prevailing rates. This widened the gap between the CBN's policy intentions and actual market conditions, thereby reducing the Central Bank's ability to manage inflation and regulate market liquidity. The introduction of the NOFR, therefore, aligns Nigeria with the global transition toward risk-free reference rates and modern benchmark structures.

The CBN stated that the major objectives of the reform include improving the credibility of benchmark rates, strengthening monetary policy transmission, enhancing transparency within financial markets, reducing the risk of manipulation of reference rates, and aligning Nigeria with global reforms in short-term interest rate benchmarks. In addition, the NOFR is expected to enhance the effectiveness of the monetary policy transmission and deepen the Nigerian money market.

This article examines the meaning of the NOFR, its key characteristics, implications for the banking sector and financial contracts, as well as the potential implementation challenges, market readiness, and future outlook.

OVERNIGHT FINANCING RATE

The NOFR is a standardised overnight interest/reference rate that reflects the cost of secured overnight lending between banks in the Nigerian financial system based on real market transactions. A reference rate in a money market serves as the standard on which transaction pricing is based. Where it is widely adopted for most transactions in a financial market, it represents the true reflection of the overall health of a country's financial market.

The NOFR is published daily by the CBN at 10:00am Lagos time based on transactions completed the previous day. Its consistent publication schedule gives market participants a reliable and predictable benchmark for pricing and valuation purposes.

In instances where transaction data is insufficient, the previous day's rate is carried forward and expressly disclosed at publication, ensuring transparency in the computation and publication.

The rate is calculated by assessing larger transactions, excluding transactions with unusually high or low rates, such that the resulting rate truly reflects market conditions and provides an accurate picture of how banks actually price short-term funding. As history shows, a new reference rate has the capacity of reshaping the entire financial ecosystem. Like its counterparts in other financial markets, the NOFR could enable new derivative markets, attract global investors, strengthen financial stability, increase local currency bond participation and improve risk management.

KEY FEATURES

Transaction-based methodology: The NOFR represents a key transition from the interbank offered rates (IBORs), previously adopted by most financial systems around the globe. The NOFR aligns the Nigerian financial market with the global transition, using eligible, completed naira-denominated transactions of a minimum value of N5 billion.

Broad applicability: As money market practices evolve around the rate over time, the NOFR is expected to improve pricing consistency across money market instruments. These include corporate and structured loans, commercial papers, treasury bills, and repurchase agreements.

Transparent governance: The CBN serves as the key administrator of the NOFR. It is responsible, as a public duty, for publishing the daily rates in alignment with its key role of maintaining monetary and price stability. While it may review the methodology for composing the data as often as necessary, corrections to already published rates are only allowed in instances of material error of 5 basis points (0.05%) or more, with full disclosure to the public.

KEY IMPLICATIONS

The introduction of NOFR presents a significant opportunity to transform transaction pricing, particularly in the lending market. Nigerian financial institutions have traditionally relied on the MPR as their benchmark pricing rate to which lending margins are applied. These margins typically reflect factors such as the bank's cost of funds, the tenor of the facility, and the borrower's credit risk, amongst others. However, the MPR remains unchanged in the periods between Monetary Policy Committee meetings, even where there are material shifts in the money market conditions. As a result, loan pricing may fail to reflect prevailing market conditions, remaining tied to a policy benchmark that may no longer align with current market dynamics.

The NOFR is designed to address this gap by providing money market participants with a reference rate that reflects actual overnight transactions and can serve as a credible benchmark for loan pricing. Its impact, however, is unlikely to be immediate. Rather, it is expected to cascade through the various financial market segments. The transition is likely to begin with the pricing of overnight lending within the banking sector, before extending to broader loan structuring, risk management practices, and pricing of government securities, and ultimately the drafting and pricing mechanisms applicable to a wide range of financial contracts.

The banking sector: Banks are expected to remain both primary contributors to, and principal users of, the NOFR framework. Consequently, the introduction of NOFR is likely to materially influence the manner in which banks price funds, manage liquidity, and structure their balance sheets. In particular, banks may progressively transition away from reliance on internal cost-of-funds models and bilateral pricing negotiations towards the use of NOFR.

In the course of their operations, banks routinely manage key risks, such as liquidity risk, interest rate risk, and funding mismatches. The availability of a transparent overnight benchmark rate would support more effective management of financing risks, providing a common reference point for funding costs. In turn, this would ensure the consistency of internal transfer pricing frameworks and strengthen the reliability of stress testing models by anchoring assumptions on observable market conditions.

Financial contracts: A key implication of the NOFR in loans and financial contracts is the gradual alignment of Nigeria's money market with global benchmark-based pricing systems, particularly in relation to floating-rate instruments. In more developed financial markets, lending and other financial products are typically anchored on standardised benchmark rates. However, the transition to such frameworks, including

the adoption of the SOFR in the United States and SONIA in the United Kingdom, was neither immediate nor automatic. Rather, it required coordinated regulatory intervention, sustained industry collaboration, and, in certain instances, binding transition timelines.

Accordingly, beyond the daily publication of the NOFR by the CBN, the active participation by market players will be essential to its effective adoption and institutionalisation. With adequate coordination among financial institutions and regulators, the Nigerian money market is expected to follow a similar trajectory towards benchmark-driven pricing. In practical terms, the NOFR is likely to become progressively embedded in floating-rate lending across key sectors such as infrastructure finance, project finance, and corporate lending, where interest rates are predominantly benchmark-linked.

Furthermore, the introduction of the NOFR promotes a stronger framework for fairness and transparency in financial contracting by ensuring the reference rates reflect prevailing market conditions at the time parties enter into a transaction. By anchoring pricing on observable and contemporaneous market data, NOFR reduces information asymmetry between counterparties, enhances pricing transparency, and strengthens the overall equity of loan pricing and financial contracts.

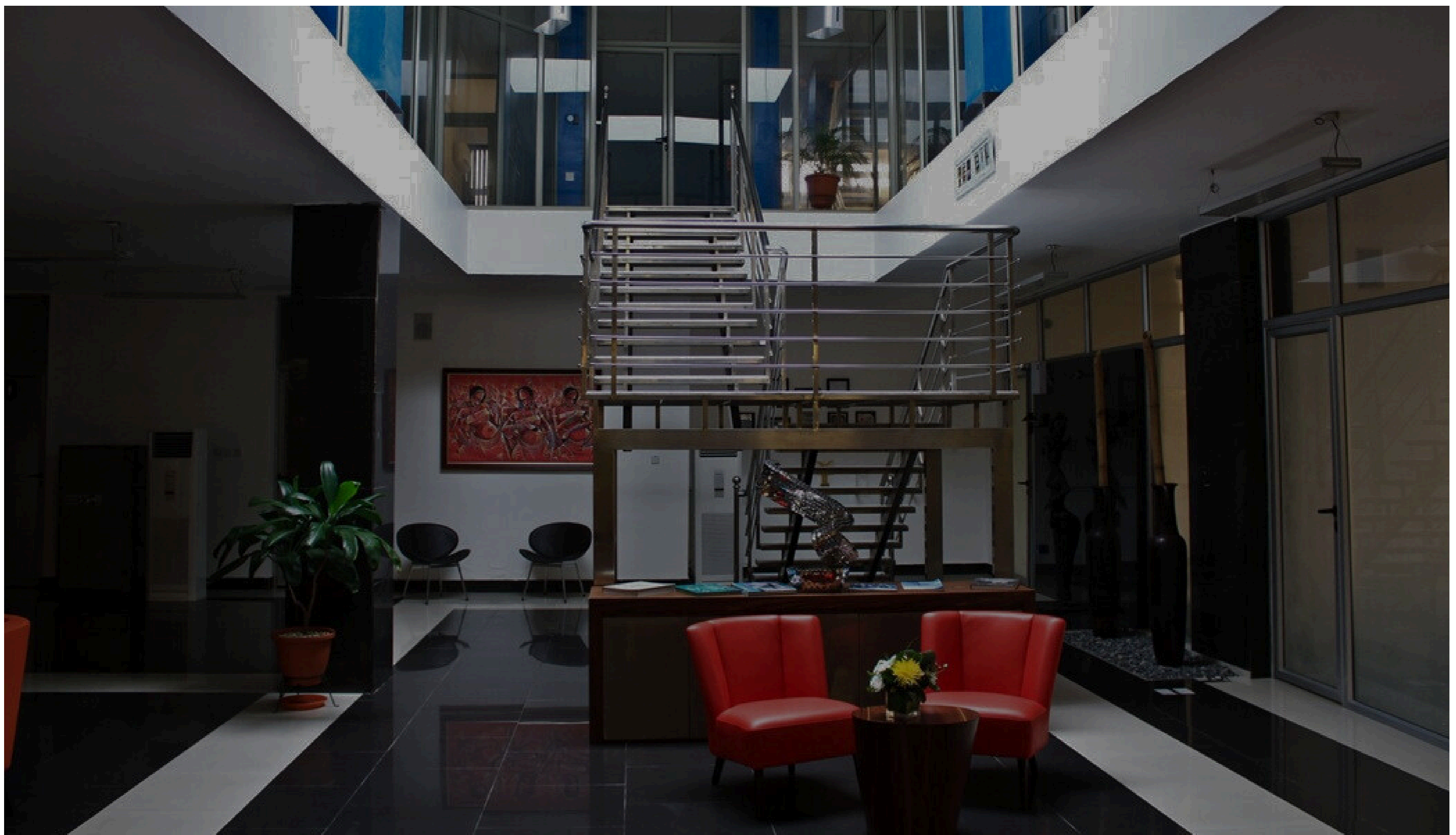
OUTLOOK

The introduction and implementation of the NOFR represent two distinct phases, each requiring coordinated action among regulators, financial institutions, and other market participants. While the CBN's introduction of the benchmark rate is a significant and commendable development, its successful implementation extends beyond its regulatory mandate alone. Effective adoption will depend on the willingness and preparedness of market participants to incorporate the rate into interbank transactions, financial contracts, risk management frameworks, valuation methodologies, and pricing structures.

A potential challenge that may arise during the transition period is the coexistence of dual benchmark rates resulting from the gradual, rather than immediate, adoption of the NOFR, a common feature of reference rate reforms across global financial markets, which may initially create inconsistencies in pricing practices and market conventions. In addition, the adoption of the NOFR requires significant internal transformation across financial institutions and other market participants. Treasury management systems, risk engines, valuation models, pricing tools, and operational infrastructure will need to be recalibrated to accommodate the daily publication and application of the NOFR. Institutions will also need to invest in capacity building and stakeholder training to ensure that relevant professionals possess the technical and operational knowledge required to effectively utilise the benchmark rate within transactions and risk management processes.

CONCLUSION

The introduction of the NOFR represents a significant step towards modernising Nigeria's financial benchmarks and aligning its money market with global best practices. However, the full benefits of the NOFR will only be realised where market participants proactively adapt their systems, contractual frameworks, and pricing models to accommodate the transition. Early adoption is likely to reduce legal, operational, and financial risk exposure, enhance investor confidence, encourage greater participation by international lenders in the Nigerian money market, and strengthen the ability of the CBN in promoting financial stability and maintaining orderly market conditions.



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