EXCHANGE TRADED FUNDS IN NIGERIA – BRIEF OVERVIEW

It has long been recognised that there is a lack of product diversity in the Nigerian capital market. The need for a diversity of products in the Nigerian capital market has led to the introduction of products such as Exchange Traded Funds (‘ETF’) into the market.

An ETF is a marketable security that tracks a stock index, commodity or basket of assets. According to the Securities and Exchange Commission (SEC), an ETF is:

“an undertaking which could be a unit trust scheme; an open-ended investment company; or any other such structure as may be approved by the Commission, that issues unleveraged securities or units listed on a securities exchange recognized by the Commission that tracks the performance of a specified security or other assets which includes but is not limited to stocks, basket of assets, indices, commodity prices, foreign currency rates, or any other appropriate benchmark approved by the Commission from time to time.”

The Nigerian Stock Exchange (NSE) on the other hand defines an ETF as

“an undertaking which is a unit trust; or mutual fund; or collective investment scheme; or company with fixed capital; or company with variable capital whose articles provide that: (a) the amount of the paid up share capital of the company shall at all times be equal to the net asset value of the company, and (b) the shares of the company shall have no par value or (c) other structure satisfactory to The Exchange and the Commission which issues an unleveraged security listed on The Exchange or an Approved Exchange and tracks the performance of a specified security or other asset which includes but is not limited to stocks,

1 Rule 543 SEC Rules & Regulations
2 Chapter 7, Rule 7.1, NSE Rule Book.
basket of assets, indices, commodity prices, and/or foreign currency rates or any other appropriate benchmark approved by The Exchange from time to time”.

While ETFs are similar to mutual funds in that they offer investors a proportionate share in a pool of stocks, bonds, and other assets and is most commonly structured as an open-ended investment, they are however different because they are listed on an exchange and traded like stocks.

ETFs’ in Nigeria

The first ETF listed in Nigeria is the New Gold Exchange Traded Fund which was listed on the NSE on 19th December 2011. The New Gold ETF is a commodity based ETF which offers investors in Nigeria the opportunity to invest in gold bullion as it tracks the South African Rand price of Gold.

The Vetiva Griffin 30 Exchange Traded Fund (VG 30 ETF) is the first equity based ETF in Nigeria. It was listed on the NSE on 14th March 2014 and it tracks the NSE 30 Index, which is an index of the most capitalised and liquid stocks listed on the NSE, including banks, insurance, brewery, construction companies amongst others.

The Lotus Halal Equity Exchange Traded Fund (LHETF) is the third ETF listed on the NSE. It was listed on 14th November 2014 and tracks the NSE-Lotus Islamic Index i.e. a market index currently comprising 15 Sharia compliant equities listed on the NSE.

Other listed ETFs on the NSE include:

(i) The Stanbic IBTC ETF 30 which also tracks the NSE 30 Index;
(ii) The Vetiva Banking ETF which tracks the NSE Banking ETF;
(iii) The Vetiva Consumer Goods ETF which is set to track the NSE Consumer Goods Index; The Vetiva Industrial ETF which tracks the NSE Industrial Index;
(iv) The SIAML Pension ETF 40 which tracks the NSE Pension Index; and,
(v) The Vetiva S&P Nigerian Sovereign Bond ETF which is an optimized Bond ETF that tracks the S&P Nigerian Sovereign Bond Index. The Vetiva S&P Nigerian Sovereign Bond ETF is also listed on the FMDQ OTC Securities Exchange (‘FMDQ’) which is an exchange that
provides a platform for registration, listing, quotation and trading of fixed income securities such as bonds, treasury bills and Commercial papers

The listings of these ETFs in Nigeria has made the NSE the leading ETFs market in the West African region in terms of number of listing, turnover value and capitalization\(^3\).

Whilst there are several benefits in investing in the ETFs such as offering liquidity to investors, diversified exposure to the constituents of the stocks being indexed; mitigating the risks of the volatility of the Nigerian capital market amongst others, there are still some inherent risks related to investing in the ETFs. For instance, 7 out of the 9 listed ETFs are equity based ETFs. Their performances therefore depends on the performance of the Nigerian stock market. Other risks include economic and political risks i.e. change in economic and market conditions as well as changes in government policies and composition risk i.e. the composition of the ETF being different from that of its underlying asset.

**ETFs Listing Requirements in Nigeria**

An ETF company seeking to be listed in Nigeria must comply with the listing requirements of the SEC and NSE. Where the ETFs are also to be listed on the FMDQ, the listing requirements of the FMDQ must also be complied with. The requirements for listing an ETF in Nigeria include the following:

- The ETF shall be fully backed at all times; either by an acquisition of the underlying securities, assets or instruments it represents, and proxy securities acceptable to the NSE and/or FMDQ which should be listed, freely tradable and have adequate liquidity;
- The ETF must appoint a liquidity provider i.e. a third party who shall be an authorized financial institution and who shall undertake to use its reasonable endeavours to maintain a secondary market in the ETF;
- The application for listing must be sponsored by a registered dealing member of the NSE and/or FMDQ as the case may be;
- The ETF must hold assets which shall be held by a trust or in custody with a third party (unrelated to the sponsor or originator of the ETF) and a trustee or custodian shall be

appointed, subject to approval by the NSE and/or FMDQ as the case may be to protect the interests of the investors in the ETF;

- the ETF's Fund Manager shall satisfy the NSE and/ or FMDQ that a secondary market in the securities of the ETF will be effectively established and maintained.

Listing Requirements for Foreign ETFs in Nigeria

There are additional requirements for foreign ETFs wishing to list in Nigeria. These additional requirements include:

- the foreign ETF must be registered and approved by the relevant regulatory authority in its country of origin;
- Copy of the prospectus/offer documents of the foreign ETF approved/cleared by the relevant authority.
- the foreign Issuer applying for the listing of the ETF shall ensure that the constitution of the foreign ETF provides for rights of investors which are at least equivalent to the rights provided for under the SEC rules.
- the foreign Issuer shall on an annual basis provide the Commission with all regulatory and audit filings submitted to its home regulator and primary exchange.
- confirmation of the name of the ETF's primary exchange which must be a member of the World Federation of Exchanges;
- the foreign ETF must appoint a Sponsoring Broker in good standing with the SEC, NSE and/or the FMDQ as its authorized representative in Nigeria.

The ETFs market in Nigeria has grown tremendously since being introduced. Indeed between 2011 when the first ETF was introduced in Nigeria and September 2016, the ETFs listed on the NSE grew by 1900%. In 2017, the ETFs listed on the NSE recorded an average gain of 20.2% and between June 2017 and June 2018, the net asset value of the listed ETFs increased by 23.17%.

The listing of ETFs in Nigeria has clearly deepened the Nigerian capital market. It has inspired investor participation and confidence in the market and its performance to date should be a source of encouragement for the introduction of other products into the Nigerian capital market.

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4 Disclosed by the CEO of the NSE at the NSE ETF workshop 2016.
5 Market Intelligence Report by The Nation Newspaper.
ABOUT – AKINDELANO LEGAL PRACTITIONERS

Akindelano Legal Practitioners’ (ALP) primary area of specialization is commercial and corporate practice. The Firm prides itself on a reputation of quality legal services, integrity and a close effective Client-Lawyer relationship. ALP has advised on several complex and rather interesting transactions involving corporate and project finance, mergers and acquisitions, capital markets transaction amongst others. It has the distinct privilege of providing legal advice on the registration and listing of all the local ETFs in Nigeria.

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