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Matric number: 17/sms01/043

Course tittle: International Economics

Date: 12th march 2020

**Question 1**

What Is Foreign Exchange (Forex)?

Foreign Exchange (forex or FX) is the trading of one currency for another. For example, one can swap the U.S. dollar for the euro. Foreign exchange transactions can take place on the foreign exchange market, also known as the Forex Market.

The forex market is the largest, most liquid market in the world, with trillions of dollars changing hands every day. There is no centralized location, rather the forex market is an electronic network of banks, brokers, institutions, and individual traders (mostly trading through brokers or banks).

How Does Foreign Exchange Work?

The market determines the value, also known as an exchange rate, of the majority of currencies. Foreign exchange can be as simple as changing one currency for another at a local bank. It can also involve trading currency on the foreign exchange market. For example, a trader is betting a central bank will ease or tighten monetary policy and that one currency will strengthen versus the other.

THE CBN

This is the regulator of the foreign exchange market as well as the representative of the Federal Government providing the required enabling environment for the market. The major functions of the CBN in the market include, but not limited to, the following:

* Establishing the ground rules of the market.
* Enforcing the rules governing the allocation of foreign exchange.
* Determining the auction system
* Enforcing exchange control regulations
* Providing the foreign exchange for each bidding and ensuring allocation of successful participants
* Advising the Government on the developments in the market ϖ Enforcing discipline among erring foreign exchange market participants.

THE FOREIGN EXCHANGE MARKET

This is just the medium of interaction between the buyers and sellers of Foreign Currencies by way of payment for transactions or by physical exchange of currencies. It is not limited to any particular location. It can take place anywhere and in any form.

PARTICIPANTS IN THE MARKET

The participants are numerous. These include anybody that has an interest in foreign trade either directly or indirectly. Therefore the Central Bank or Ministry of Finance is an interested party as they regulate the market. They are also participants as they are on the supply side. The banks are the Authorized Dealers. The Bureau de Change (BDC) is also a participant.

**Question 2**

LIMITATIONS OF FOREX MARKET MANAGEMENT IN NIGERIA

The Management of the Forex market in Nigeria has had a lot of challenges and limiting factors over the years. Some of these limitations include, but not limited to the followings.

i. Imbalance in demand and supply of foreign exchange currencies. This is a major challenge in almost all developing countries. However, our peculiar situation in Nigeria is more acute because we rely heavily on imported goods. This is closely related to the issue of adverse balance of trade and payment with our trading partners.

ii. Another limitation to our Forex management is due to our monolithic economic base. We rely heavily on oil as our major source of foreign exchange earnings. Before the advent of oil in Nigeria, our economy was doing quite well with Agricultural product such as Cocoa, Rubber, Cotton, Groundnut etc. driving our Forex earnings. This has changed drastically since the discovery of oil, the Agric sector has been neglected and Forex earnings from that sector lost.

iii. Again, Nigeria has become an import-dependent nation because of our new found sudden wealth in oil. We now import virtually everything, including consumer goods and luxury goods that we can easily do without.

iv. Another limitation is the inconsistencies in government policies that have hampered progress in industrialization. Most of our industries have collapsed over the years, thereby contributing/compounding our import-dependency.

v. Corruption is another challenge or limitation in our Forex management. Most of our leaders prefer to

question 3

For most developing countries that need to import raw materials and spare parts for the · purpose of economic development, foreign exchange reserves, fore build-up is required to ensure that panic measures are not resorted to when foreign exchange receipts are dwindling. When there is a disequilibrium in the foreign exchange market caused by inadequate supply of foreign exchange reserves, pressure may be exerted on foreign exchange reserves. If the reserves are not adequate, this may deteriorate into balance of payments problems. There is, therefore, need to manage a nation's foreign exchange resources.so as to reduce the adverse effects of foreign exchange volatility. The management of foreign exchange resources is further· informed by the need to set an appropriate clearing price in the foreign exchange market that would guarantee adequacy of supply in relation to the demand for foreign exchange. Therefore, the art of foreign exchange management is a conscious attempt to harness foreign exchange resources, deploy them to ·service the economy and to meet other international commitments while saving some to raise the level of the country's international reserves so as to prevent the economy from experiencing shocks due to foreign exchange volatility.

Exchange Rate Management The framework for foreign exchange management under the dispensation, tire Foreign Exchange Market (FEM), was conceived as a mechanism for the determination of an appropriate exchange rate for the naira in order to reduce the pressure on foreign exchange resources and stabilize the balance of payments. In effect, the exchange rate mechanism was expected to result in a more rational allocation and utilization of foreign exchange resources and reduce foreign exchange volatility, thus m~ foreign exchange management. less difficult. The major source of foreign exchange to the market is the Central Bank of Nigeria