An Investigation of African Securities Markets Competitiveness, (Concise Final Report)

23 July 2022

Conduct of the African Capital Markets Competitiveness Study
The African Capital Markets Competitiveness Study is sponsored by the Capital Markets Development Trust Fund (CMDTF) whose aim is to promote the development and integration of African capital markets through the provision of technical assistance. CMDTF’s operations complement the African Development Bank’s efforts to mobilize resources through domestic capital and financial markets to fund the real sector and advance the Bank’s High 5 priorities.

CMDTF interventions are financed by the Ministry for Foreign Trade and Development Cooperation of the Netherlands and the Ministry of Finance of Luxembourg.
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<thead>
<tr>
<th>Acronym</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>AELP</td>
<td>African Exchanges Linkage Project</td>
</tr>
<tr>
<td>ADB</td>
<td>Asian Development Bank</td>
</tr>
<tr>
<td>AfDB</td>
<td>African Development Bank</td>
</tr>
<tr>
<td>ASEF</td>
<td>Asian and Oceanian Stock Exchanges Federation</td>
</tr>
<tr>
<td>ASEA</td>
<td>African Securities Exchanges Association</td>
</tr>
<tr>
<td>ASEAN</td>
<td>The Association of Southeast Asian Nations</td>
</tr>
<tr>
<td>BDD</td>
<td>Business Development Drive</td>
</tr>
<tr>
<td>BRVM</td>
<td>Bourse Régionale des Valeurs Mobilières</td>
</tr>
<tr>
<td>BVMAC</td>
<td>Bourse des Valeurs Mobilières de l'Afrique Centrale</td>
</tr>
<tr>
<td>CCP</td>
<td>Central Counter Party</td>
</tr>
<tr>
<td>CEO</td>
<td>Chief Executive Officer</td>
</tr>
<tr>
<td>CFA</td>
<td>West African Franc (XOF)</td>
</tr>
<tr>
<td>CG</td>
<td>Corporate Governance</td>
</tr>
<tr>
<td>CIS</td>
<td>Collective Investment Schemes</td>
</tr>
<tr>
<td>CMDTF</td>
<td>Capital Markets Development Trust Fund</td>
</tr>
<tr>
<td>CREPMF</td>
<td>Conseil Régional de l’Epargne Publique et des Marchés Financiers</td>
</tr>
<tr>
<td>CSCS</td>
<td>Central Securities Clearing System (Nigeria)</td>
</tr>
<tr>
<td>DC/BR</td>
<td>Central Depository/Settlement Bank (BRVM)</td>
</tr>
<tr>
<td>DvP</td>
<td>Delivery versus payment</td>
</tr>
<tr>
<td>EBRD</td>
<td>European Bank for Reconstruction and Development</td>
</tr>
<tr>
<td>ETF</td>
<td>Exchange Traded Fund</td>
</tr>
<tr>
<td>EU</td>
<td>European Union</td>
</tr>
<tr>
<td>FCFA</td>
<td>Central African Franc (XAF)</td>
</tr>
<tr>
<td>FEAS</td>
<td>Federation of EuroAsian Stock Exchanges</td>
</tr>
<tr>
<td>FESE</td>
<td>Federation of European Stock Exchanges</td>
</tr>
<tr>
<td>FIABNET</td>
<td>Federación Iberoamericana de Bolsas (The Ibero-American Federation of Stock Exchanges)</td>
</tr>
<tr>
<td>GAX</td>
<td>Ghana Alternative Exchange</td>
</tr>
<tr>
<td>GDP</td>
<td>Gross Domestic Product</td>
</tr>
<tr>
<td>GEMS</td>
<td>Growth Enterprise Market Segment (Kenya)</td>
</tr>
<tr>
<td>GFIM</td>
<td>Ghana Fixed Income Market</td>
</tr>
<tr>
<td>GHS</td>
<td>Ghanaian Cedi</td>
</tr>
<tr>
<td>GSE</td>
<td>Ghana Stock Exchange</td>
</tr>
<tr>
<td>IFC</td>
<td>International Finance Corporation</td>
</tr>
<tr>
<td>IFRS</td>
<td>International Financial Reporting Standards</td>
</tr>
<tr>
<td>IOSCO</td>
<td>International Organization of Securities Commissions</td>
</tr>
<tr>
<td>IPO</td>
<td>Initial Public Offer</td>
</tr>
<tr>
<td>ISC</td>
<td>International Securities Consultancy</td>
</tr>
<tr>
<td>JSE</td>
<td>Johannesburg Stock Exchange</td>
</tr>
<tr>
<td>NASD</td>
<td>National Association of Securities Dealers</td>
</tr>
<tr>
<td>NASDAQ</td>
<td>National Association of Securities Dealer Automated Quotation (System)</td>
</tr>
<tr>
<td>NGX</td>
<td>Nigerian Exchange Group</td>
</tr>
<tr>
<td>NGXG</td>
<td>Nigerian Exchange Group</td>
</tr>
<tr>
<td>NGX</td>
<td>Nigerian Exchange</td>
</tr>
<tr>
<td>OECD</td>
<td>Organisation for Economic Co-operation and Development</td>
</tr>
<tr>
<td>OTC</td>
<td>Over The Counter</td>
</tr>
<tr>
<td>Abbreviation</td>
<td>Full Form</td>
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<tr>
<td>--------------</td>
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<tr>
<td>PE</td>
<td>Private Equity</td>
</tr>
<tr>
<td>REIT</td>
<td>Real Estate Investment Trust</td>
</tr>
<tr>
<td>SEC</td>
<td>Securities Exchange Commission</td>
</tr>
<tr>
<td>SET</td>
<td>Stock Exchange of Thailand</td>
</tr>
<tr>
<td>SLA</td>
<td>Service Level Agreement</td>
</tr>
<tr>
<td>SME</td>
<td>Small/Medium Enterprise</td>
</tr>
<tr>
<td>SRO</td>
<td>Self-Regulatory Organisation</td>
</tr>
<tr>
<td>TOR</td>
<td>Terms of Reference</td>
</tr>
<tr>
<td>UCITS</td>
<td>Undertakings for the Collective Investment in Transferable Securities.</td>
</tr>
<tr>
<td>USD</td>
<td>US Dollar</td>
</tr>
<tr>
<td>VC</td>
<td>Venture Capital</td>
</tr>
<tr>
<td>WAEMU</td>
<td>West African Economic and Monetary Union</td>
</tr>
<tr>
<td>WFE</td>
<td>World Federation of Exchanges</td>
</tr>
<tr>
<td>$</td>
<td>In this report refers to US dollar unless otherwise stated</td>
</tr>
</tbody>
</table>
FOREWARD

1. This publication results from a consultancy study carried out by ISC (the International Securities Consultancy) for the African Development Bank and funded by the Capital Markets Development Trust Fund which is administered by the Bank and funded by the Ministry for Foreign Trade and Development Cooperation of the Netherlands and the Ministry of Finance of Luxembourg.

2. One of the Bank’s mandates is to develop competitive capital markets in Africa that are able to attract a wide range of securities issuers and investors and compete effectively for international capital and cross-listings.

3. Most African financial markets are small and fragmented, resulting in the overall financial sector being dominated by banks. Importantly, the state of Africa’s capital markets is impeding the mobilization of local currency savings.

4. Capital market development is limited by the absence of a critical mass of listed and tradeable securities, too few issuers, investors, intermediaries, lack of product diversity, weak regulatory structures, inadequate financial infrastructure, poor risk and price identification methods and low activity in the secondary markets, among other constraints.

5. These challenges have resulted in ineffective capital markets, limiting their ability to address the financing needs of Africa’s development agenda.

6. The study was designed to assist the Bank in identifying key competitive variables driving or hindering the success of African capital market ecosystems, especially competitive factors that influence issuers’ and investors’ decisions. The method proposed was to use published data, which in the event was somewhat scarce, as well as surveys to specified markets. The focus was to be on West Africa but the survey was extended to other markets and the results have been included in the report.

7. It was initially believed that it might be possible to arrive at a single statistical measure for competitiveness. The Bank requested the determination of a universally agreed, accepted competitiveness variable or standard as a constant against which to measure the significance of the analyzed qualitative and quantitative variables. However, after examining all competitive aspects of the markets this was not a feasible objective. It emerged that the areas where there do appear to be competitive advantage are size of the market and an amalgam of features which the consultants termed Business Development Drive. The amalgam is less precise than size, but it can be represented by a combination of exchange ownership model, diversity of tradeable assets and the number of IPOs.

8. The consultants therefore provided a rating framework for the markets under review which indicates the degree to which they are currently successful and the ways in which their markets might progress. Recommendations and areas for intervention are suggested and these largely reflect the existing areas in which the Bank is very active for some time.

9. The work was carried out in 2020 and 2021 and there has been progress since then which is not reflected here.

ACKNOWLEDGEMENT

10. The Publication Team would like to acknowledge the efforts of the African Development Bank Financial Sector Development Department / Capital Markets Development Division and the African Securities Exchange Association in the publication of this report. The principal AfDB team included Mr. Stefan Nalletamby, Mr Ahmed Attout, Mr. Emmanuel Diarra, Mr. Akin Adigun, Mr. Albin Kakou and Mr. Victor Chando.

11. We thank Dr Edoh Kossi AMENOUNVE, President of the African Securities Exchanges Association (ASEA) and all members of the ASEA Executive Committee for their support. We also thank Ms. Furaha Karba, Head of Secretariat the ASEA for assisting greatly with the distribution of surveys the ASEA members and for providing other suggestions.
12. The International Securities Consultancy (ISC) Team comprised Mr. Stephen Wells, Mrs Susan Selwyn-Khan, Mr. Bi Balicléoui Emmanuel Zamble, Mr. Mathewos Shamo Humbamo and Mr. Ayokunle Ilesanmi.

13. We also wish to express our gratitude to all the stakeholders and industry experts who were consulted as part of this report. They contributed valuable insights, comments and time. Officers of the following organisations were particularly helpful:

- BODIVA (Bolsa de Dívida e Valores de Angola) (The Angola Debt and Stock Exchange)
- Botswana Stock Exchange
- Ghana Stock Exchange
- Khartoum Stock Exchange
- Malawi Stock Exchange
- Nairobi Securities Exchange
- Nairobi Securities Exchange
- Rwanda Stock Exchange
- Rwanda Stock Exchange
- Securities and Exchange Commission, Ghana
- Stock Exchange of Cape Verde
- Stock Exchange of Mauritius
- The Egyptian Exchange
- The Nigerian Exchange Limited
- Uganda Securities Exchange

14. Special thanks are due to colleagues Mr. Akin Adigun and Mr. Albin Kakou from the African Development Bank without whose inputs or support this report could not have been realized.
EXECUTIVE SUMMARY

The project

1. This publication results from a consultancy study carried out by ISC (the International Securities Consultancy) for the African Development Bank and funded by the Capital Markets Development Trust Fund which is administered by the Bank and funded by the Ministry for Foreign Trade and Development Cooperation of the Netherlands and the Ministry of Finance of Luxembourg.

2. The Terms of Reference (TOR) provided by the AfDB described the work as “a study of the competitiveness of African Capital Markets” which would “assist the Bank in identifying key competitive variables driving or hindering the success of selected African capital market ecosystems, especially competitive factors that influence issuers’ and investors’ decisions when selecting a market platform to raise capital or access investment products”.

3. The TOR required examination of 12 countries but, because more data became available, this was extended to 17 countries. Of these, four countries in West Africa including Ethiopia were selected for a deep dive analysis. This report presents the findings of research conducted into those capital markets. It draws conclusions about the competitive factors that differentiate the various markets, including recommendations that could be addressed in future support for national capital markets.

4. The analysis provides a visual model showing Business Development Drive (BDD) indicating the competitive ranking of the surveyed exchanges. The ranking is based on the features identified as important by users and from the consultant’s experience as detailed below.

Competition in capital markets

5. In capital markets there is competition between banks and formal markets for business in raising capital and managing savings. There is also competition between exchanges for that business. This is discussed in the following section. The factors which affect the competitive position of a capital market (equity, debt and derivative platforms etc.) were examined through a survey (questionnaire) and wide-ranging research.

6. The key competitive factors which at the outset the consultants assessed are likely to be important were investigated in the questionnaires and are summarised below:

<table>
<thead>
<tr>
<th>Issuer</th>
<th>Investor</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Domestic</strong></td>
<td></td>
</tr>
<tr>
<td>Listing process timescale</td>
<td>Market abuse regulation</td>
</tr>
<tr>
<td>Listing costs</td>
<td>Secure payments and settlement</td>
</tr>
<tr>
<td>Disclosure requirements</td>
<td>Compensation scheme</td>
</tr>
<tr>
<td>Competent intermediaries</td>
<td>Disclosure rules</td>
</tr>
<tr>
<td>Liquidity</td>
<td>Financial literacy</td>
</tr>
<tr>
<td>Taxation</td>
<td>Regulated intermediaries</td>
</tr>
<tr>
<td></td>
<td>Trading costs</td>
</tr>
<tr>
<td></td>
<td>Taxation</td>
</tr>
<tr>
<td><strong>Foreign</strong></td>
<td></td>
</tr>
<tr>
<td>Exchange control</td>
<td>Exchange control</td>
</tr>
<tr>
<td>Accounting standards</td>
<td>Accounting standards</td>
</tr>
<tr>
<td>Listing process timescale</td>
<td>Liquidity</td>
</tr>
<tr>
<td>Listing costs</td>
<td>Market abuse regulation</td>
</tr>
<tr>
<td>Disclosure requirements</td>
<td>Robust settlement – DvP/CCP</td>
</tr>
<tr>
<td>Competent intermediaries</td>
<td>Accounting standards</td>
</tr>
<tr>
<td>Liquidity</td>
<td>Custodians</td>
</tr>
</tbody>
</table>

Summary of key competitive factors and relevance to different user groups
Fundamental results from the research

7. African exchanges, while achieving many development goals, have not managed to achieve the level of importance in their economies as has been the case in other regions such as Asia. Some key findings are:

- Almost all the exchanges studied are small. Even the larger ones such as Egypt and Nigeria are small in global terms.
- Except for Egypt, none of the exchanges has a total market value which exceeds 20% of their GDP, an indication that the public capital market is relatively insignificant in the economy.
- The total number of new companies across all the 17 exchanges assessed in the five years to December 2020 is 72, slightly more than one per month across all those exchanges.
- All the 17 markets except Egypt are extremely illiquid.

Universal infrastructure models and standards

8. The infrastructure required by global investors and issuers is largely present in the surveyed African exchanges.

International standard regulatory models

9. All the surveyed markets have the attributes that users would expect of modern markets: a statutory regulator, International Organization of Securities Commissions (IOSCO) membership, licensing standards, prospectus standards, laws on market abuse etc. Most also have basic corporate governance requirements for listed companies, standard accounting requirements for reporting, computer-based systems for detecting market abuse and requirements for brokers to have relevant qualifications.

Easier access for foreign investors and to foreign markets

10. Most of the studied markets have removed capital controls or, at least, made them rule-based and so predictable. Similarly, most markets have few if any restrictions on foreign ownership.

Diverse business development levels

11. While the similarities are a strength for African capital markets, there are some features which are not positive for market development and competitiveness.

   i) Investors. African markets have sought to develop a broader range of investor participants, but all remain illiquid in their secondary markets. Foreign investors have become important in many markets and the legal infrastructure for collective investment schemes (CIS) and pension plans has been developed. However institutional investors, while they exist and command significant funds, have not been actively investing in the stock market, preferring bank deposits, money market instruments and government bonds.

   ii) Issuers. Issuers are scarce in African markets, even the largest exchanges have relatively few listings and the ratio of total market capitalisation to GDP is small. This is contrasted with Asian exchanges where IPO activity has been high, even in the least successful exchanges. (This is discussed and data is presented in Section 5) In developed markets, intermediaries take responsibility to seek out potential listed companies. In mid-level developed markets such as Thailand, the exchange plays a bigger role in recruiting new companies. But neither the intermediaries nor the exchanges in African markets seem to be sufficiently aggressive in attracting new business. While the lack of liquidity is a contributory factor deterring new companies/issuers, if there were assets to trade then more investors would be attracted and liquidity would improve. As with investors, the regulatory and other costs of listing are not a significant deterrent. Companies will inevitably state that charges are too high, but the regulatory
costs are not large in comparison to the implicit costs of preparing a business for listing and pricing it in a way that is attractive to investors while not disadvantaging the issuer.

iii) **Commercial approach.** This covers the enthusiasm and commitment of the exchange to generate new business. It is difficult to measure but three indicators can be used — ownership of the exchange, diversity of assets traded and the number of IPOs. These indicators can be considered in assessing the approach of exchanges to business development and expansion.

I. **Ownership.** Exchanges are now often organised as private or even listed companies rather than as member owned cooperatives or as government companies. An exchange with a focus on profitability is more likely to develop new products, techniques etc. in the face of opposition from vested interests. Currently five of the 17 exchanges are listed, five are private companies and seven are member or government owned.

II. **Diversity of assets traded.** The more innovative exchanges will try to introduce new products either in response to user requests or their own wish to develop the business. Only one exchange, Nairobi, among the 17 surveyed offers derivatives but several offer Exchange Traded Funds (ETFs) and Real Estate Investment Trusts (REITs). Nigeria offers the most asset types with nine.

III. **Number of IPOs.** This is covered above.

### Diverse market and economy sizes

12. The size of the market is a measure of success, but it is also a major contributor to continued success. A larger economy assists greatly in market development. More rapid market development supported by a large customer base leads to a more successful exchange. The size of the economy brings diversity and an abundance of investment, high quality and dynamic issuers, economies of scale and liquidity and an abundance of skilled practitioners. By contrast small countries struggle to compete.

### Improve business focus of stock exchanges

13. Evidence of the past two decades in Africa and in other regions suggests that a stronger business focus of stock exchanges has a positive impact on market development.

14. In Africa several exchanges are listed (including four of the surveyed exchanges) or operate as private companies (five of the surveyed exchanges). But the survey data showed also that two of the surveyed exchanges remain mutually owned and five are government owned. The Ethiopian exchange, when it commences operation, is planned to be majority privately owned.

15. The development of local capital markets would be enhanced if the exchanges of Africa moved towards private ownership and, ultimately, listing.

16. The AfDB could support the process by encouraging private ownership of exchanges, supporting regional grouping initiatives and also less formal resource-sharing arrangements, and set guidelines for exchange governance.

### Visual model

17. Using GDP data and combining this with a rating for commercial approach (based on diversity of assets, exchange ownership model and success in attracting IPOs) gives the table below showing the assessment of the surveyed exchanges according to their BDD.

18. The three exchanges in dark red boxes are in danger of being unsustainable. Their potential markets are small and have limited BDD.

19. The five exchanges in paler red boxes are still in a challenging situation. They still have small potential markets and show limited BDD. They are state/member owned, have had few IPOs and have a limited product range.
20. The four exchanges in yellow boxes are still in small markets but display better levels of BDD, suggesting that they may be able to overcome the size disadvantage and develop their businesses.

21. The five exchanges in green boxes are in larger economies or regional groupings of economies (except for Mauritius) and they have exhibited the drive to expand their business. Egypt will remain constrained by its government ownership but, nonetheless, it has successfully developed its business. It should be noted that notwithstanding its ranking, Bourse des Valeurs Mobilières de l’Afrique Centrale (BVMAC) is operationally successful.

<table>
<thead>
<tr>
<th>Market size</th>
<th>Ranking</th>
<th>0</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
</tr>
</thead>
<tbody>
<tr>
<td>Small</td>
<td>Malawi</td>
<td>Cape Verde</td>
<td>Rwanda</td>
<td>Botswana</td>
<td>Mauritius</td>
<td></td>
<td></td>
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</tr>
<tr>
<td></td>
<td>Sudan</td>
<td>Zambia</td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Medium</td>
<td>Tunisia</td>
<td>Angola</td>
<td>Uganda</td>
<td>Ghana</td>
<td>Tanzania</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td></td>
<td></td>
<td>BVMAC</td>
<td></td>
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<td></td>
<td></td>
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<tr>
<td>Large</td>
<td></td>
<td>BRVM</td>
<td>Nigeria</td>
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<tr>
<td></td>
<td></td>
<td>Egypt</td>
<td>Kenya</td>
<td></td>
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</tr>
</tbody>
</table>

Recommendations for interventions

Support diversification of asset types

22. Many African markets have only a limited number of products – asset types – which they trade. Adding new assets is challenging in developing markets but is valuable in that it generates activity and improves the business models of the participants in infrastructure providers.

23. AfDB could benefit the capital markets by assisting in this development by:

- Conducting feasibility studies in countries with a narrow asset range. The studies would include assessing supply, demand and infrastructure requirements.

- Depending on the results of the feasibility study, assisting in drafting rules or regulations leading to a time-bound action plan for implementation.

- Assisting the regulator and exchange in the introduction of the new products.

Explore potential for more regional groupings

24. Africa has two successful regional groupings of capital markets – Bourse Régionale des Valeurs Mobilières (BRVM) and Bourse des Valeurs Mobilières de l’Afrique Centrale (BVMAC) – based on currency areas. Africa also has many smaller countries where the viability of a separate capital market is doubtful. AfDB is supporting several regional projects covering those countries that do not have a common currency.

25. One way of addressing this is through exchange linkages and the AfDB is supporting the African Exchanges Linkage Project (AELP) project for cross-border links between intermediaries. It could supplement this by conducting or supporting research on the best way of helping smaller countries to develop viable and sustainable capital markets which allow them to have the benefits of a capital market without handing over to a larger market and losing the local benefits of an active financial sector.

Build market abuse monitoring capacity

26. Detection and prosecution of market abuse is a key factor in raising investor confidence and encouraging investor participation. African markets have basic prohibitions however, as markets develop, they will need more effective monitoring and enforcement to maintain investors’ confidence.
27. The AfDB could benefit African capital markets by:

- Assisting in the acquisition of IT infrastructure by providing funding and assisting with procurement plans.
- Arranging for capacity building for surveillance staff.
- Assisting in the drafting of agreements between capital market agencies.
- Supporting external assessment of legal/regulatory arrangements.
- Supporting drafting of MOUs or similar between the regulator and the judicial authorities.
- Supporting training for legal professionals including prosecutors and judges.

**Improve Corporate Governance standards**

28. The survey results suggested that most of the surveyed markets had some regulations regarding Corporate Governance (CG) requirements. However, the experience of other developing markets suggests that improvements in CG standards are required to bring conformity with international norms and meet the needs of domestic and international institutional investors.

29. In the near term, the AfDB could usefully sponsor a CG assessment of a group of African countries. This would involve assessments of existing codes compared with international standards. It would also be appropriate for the AfDB to support CG league tables to raise the profile of CG perhaps by following the model of the ASEAN Corporate Governance Scorecard.

**Improve environment for listing**

30. African exchanges need to attract more companies to list on their markets. Currently the numbers are low with few Initial Public Offers (IPOs) each year.

31. The barrier to attracting new companies seems to lie in issues relating to areas of process and marketing:

- **Process.** Listing processes appear to be relatively slow, burdensome and unpredictable. AfDB, in cooperation with the African Securities Exchanges Association (ASEA), could assist by:
  - Drafting a model Service Level Agreement (SLA) for prospectus approval at the regulator.
  - Setting guidelines for automating the application process using electronic submissions, scrutiny and storage.
  - Standardising prospectus content by providing model templates.

- **Marketing and support.** Just improving processes or even introducing Small/Medium Enterprise (SME) markets with more relaxed requirements, while important, will not bring potential listed companies to the exchanges. To improve the flow of companies the exchanges need to:
  - Study the range and types of potential listed companies in their markets.
  - Study the requirements of investors.
  - Identify potential companies for listing.
  - Support and coach identified companies.

32. The AfDB could usefully survey a sample of African exchanges to gather data on how exchanges approach these challenges – and follow up by arranging studies or similar explorations to see how listing marketing works in other exchanges.

**Develop institutional investors**

33. Domestic institutional investors are beginning to develop in Africa but are still small and, so far, have tended not to invest in stock market assets. In time, local initiatives will support the development of savings and pension schemes, but this may not be reflected in domestic stock market investment. Mutual funds are not well developed and where they exist, as with other funds, they mainly invest in bonds and deposits.
34. The AfDB could assist African capital market development by supporting in-depth analyses of the institutional investor landscape.

Support greater availability of regular, reliable and consistent data

35. There is currently a shortage of good information on African capital markets. This deficiency covers a range of data types including basic statistical data, structural data on how the markets are organised and regulated, and data on market users.

36. AfDB could benefit the capital markets by assisting in this development by:
   - Working with ASEA to collect, produce and disseminate basic information.
   - Working with ASEA to support inter-exchange working groups to agree definitions and conduct surveys.
   - Sponsoring basic research projects to build further information beyond basic statistics into the structural data (systems, investors etc.).

Ethiopia

37. Ethiopia is on the cusp of starting a capital market and has been well supported. The plans for developing a regulator and exchange are well crafted and follow best practices. However, like other African markets, it may well face a shortage of tradeable assets. The AfDB could support an examination of the companies traded on the Over The Counter (OTC) market and extend this to assess corporate finance demand in Ethiopia. This would assist the new exchange in developing the number of listings.

Current AfDB interventions

38. It should be noted that the AfDB is already very active in the capital markets space and has a number of current and past projects especially in the field of regional integration which are already addressing many of the issues identified in this report.

THE PROJECT AND METHODOLOGY

Project structure

39. The Terms of Reference (TOR) provided by the AfDB described the work as “a study of the competitiveness of African Capital Markets” which would “assist the Bank in identifying key competitive variables driving or hindering the success of selected African capital market ecosystems, especially competitive factors that influence issuers’ and investors’ decisions when selecting a market platform to raise capital or access investment products”.

40. The statistical research was confined to publicly available data and in the expectation that this would not be easy to gather for all the capital markets on the continent, the TOR required examination of the capital markets of only 12 countries.

41. However during the project, the consultants were able to gather fundamental data on a wider range of exchanges, increasing the sample size to 17. Data on all of these is presented in the report.

42. Of these, four countries in West Africa including Ethiopia were selected for a deep dive analysis involving interviews where possible and eight were covered at a less detailed level. The markets are shown in Table 1.
Table 1: Capital markets covered by the research

<table>
<thead>
<tr>
<th>Deep Dive</th>
<th>Other Selected for Data Collection</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nigeria, West African Economic and Monetary Union (WAEMU)/BRVM, Ghana, Ethiopia</td>
<td>Angola, Central Africa (BVMAC), Kenya, Rwanda Tanzania, Tunisia, Uganda, Zambia</td>
</tr>
</tbody>
</table>

43. This report presents the findings of research conducted into selected national capital markets and draws conclusions about the competitive factors that differentiate the various markets and includes recommendations which could be addressed in future support for national capital markets.

44. This section, Section 2, describes the fundamentals of the project, the selection of countries to be studied and the methodology used.

45. Section 3 presents a discussion of competitive factors in capital markets, with a focus on stock exchanges, drawn from the consultant’s experience of developing markets in Africa, Asia and Europe.

46. This is further developed in Section 4 with a discussion of the detailed competitive factors that are covered in the study.

47. The study was conducted using consultant analyses, a quantitative survey of 17 exchanges and a qualitative survey supported by interviews with market participants for the deep dive markets. The overall statistical findings of the research which illustrate the level of success of exchanges in generating exchange business are presented in Section 5.

48. The overall findings of the surveys – based on non-statistical, factual data from the quantitative survey summary and results from the qualitative survey and interviews – are presented in Section 6. This section also draws conclusions describing the assessment of the competitive situation of the individual surveyed exchanges.

49. Section 7 draws on the competitive situation assessments to suggest potential future interventions for development partners and describes interventions which the AfDB has supported.

Methodology

50. The TOR for the study required the design and administration of a questionnaire about published information relating to key competitive features of the markets in the study. Extensive desk research was conducted before the questionnaire work began. There is relatively little published data on African exchanges. Since this report was drafted, the African Securities Exchanges Association (ASEA) has again started publishing some statistics but the information was not available at the time.

51. Two questionnaires\(^1\) were used for data collection, including basic data and qualitative information on the capital markets examined:

- A quantitative questionnaire to collect factual data from the exchanges. This was designed to collect essential quantitative metrics. A summary is attached as Appendix A. This was sent out to exchanges and, in some cases, capital market regulators. ASEA assisted with distribution to their members. The questionnaire yielded a total of 17 capital markets useable results.

- A qualitative questionnaire was designed for market participants to comment on the quality of the capital market offered in the country. The questionnaire was drafted and discussed with AfDB who suggested additions. A summary is attached as Appendix B. This survey had separate sections for corporate finance advisers and for investors.

52. The detailed findings of the surveys as well as a fuller description of the methodology are presented in Appendices C and D.

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\(^1\) In both English and French.
53. In the event the responses to the qualitative questionnaire were unsuccessful. Therefore contacts in
the deep dive markets were approached and the questionnaire completed by interview.

54. In Ethiopia, which currently has no formal capital market infrastructures or organisations but where work
on the setting up of a regulator is progressing, the national consultant conducted interviews with the
National Bank of Ethiopia and the staff working on the Project Team implementing the Proclamation
and the establishment of the regulator.

**WHAT DOES COMPETITIVENESS MEAN IN THE CONTEXT OF CAPITAL
MARKETS?**

**Bank markets v. securities markets**

55. In economic theory, competition is between providers of goods which are close substitutes. In the
extreme, all goods are substitutes as they compete for the consumer’s attention but the stronger the
possibilities for substitution, the more intense will be the competition. Capital markets support the
issuance and trading of risky assets. These assets are themselves bundled products since each is
comprised of several attributes such as return, risk, and cost of acquisition/disposal (liquidity).

56. Capital markets are generally contrasted with bank markets. In a bank market the business of the bank
participants is the gathering of deposits and the provisions of loans through a process of
disintermediation by those banks. The depositors and the borrowers have no knowledge of or interest
in each other. Banks manage the credit risk of borrowers so that they can pay back depositors who
expect to be paid in full in all circumstances and especially irrespective of the success of the bank’s
lending. This will also involve an element of time shifting since, in most cases, the deposits are short
term, and the loans are longer term – a “maturity mismatch” which banks strive to manage. The security
depositors will be ensured by prudential regulation of banks and supported by some form of deposit
protection scheme.

57. In a capital market the lenders (equivalent to bank depositors) have a direct relationship with the
borrowers. The relationship may be a loan relationship (a bond market) or an ownership/profit-sharing
relationship (an equity market). The directness of the relationship means that the lenders need to be
continuously well informed of, and interested in, the commercial state of the borrowers. The maturity
mismatch also exists but in a capital market it is resolved by allowing lenders to transfer the assets
provided by the borrowers (bonds or shares) to other borrowers. The key difference to the banking
market is risk. There is no guarantee that the lenders (investors) will get their money back. In a bond
market they hope to get their money back with interest, so the upside is limited. Risk is also limited by
giving bondholders a higher priority claim on assets in the event of a failure. Equity investors stand to
make an unspecified amount through dividend payments and a larger amount through capital gains.
However, as they have lowest priority in a failure, they stand a chance of losing all their investment.

58. Capital market activities may be carried out on informal trading structures, Over The Counter (OTC) or
on formal markets. The characteristics of the alternatives are set out below.

59. Informal market:

- Issuance is limited to a small group of investors and conducted through direct negotiations, generally
  known as a private placement market. There is no issue on a formal market such as a stock
  exchange and so no compliance with stock exchange rules for issuers.

- Trading is carried out by direct negotiation between investors with only a limited display of offered
  prices.

- Settlement of trades is directly between counterparts on negotiated, ad hoc terms.

- There is limited regulation of activities, conformity with national laws but no specific laws for
  securities. There is no regulatory agency.
• There are no structured channels for information sharing, participants must discover information about issuers and trade at their own expense and manage the residual risk that their information search has not been complete.

• Participation is limited by commercial pressures to a small number of professional participants who may have more than one role. There are no licenses or similar qualifications for participation.

60. Formal market:

• Issuance is by public offer to a wide group of investors at a fixed price, by an auction or by a book-building process or a combination. This will involve admission to an organised market where certain standards are required.

• Trading is carried out through an open and public system for establishing trading interest and prices either by exposing orders or by displaying quotes at which dealers will trade. This is usually operated by a stock exchange or an entity that is similar to a stock exchange.

• Settlement of trades is through an organised system involving transfer of securities to a fixed timetable and with processes to manage risk and guarantee delivery.

• Extensive capital market specific laws and regulations are monitored and enforced by a government regulatory authority which makes regulations, licenses participants, monitors the market and enforces the regulations.

• Part of the regulatory structure will be designed to ensure that information is widely available to all participants. This applies to information relating to the issuers and to trading.

• Participation involves a wide range including specialised intermediaries and retail investors.

61. Informal markets are generally restricted to a small group of participants. Private placement markets for bonds are an example where a small number of issuers sell securities to a small number of investors. The amount of information offered with each issue is relatively small as investors are expected to do their own due diligence to discover the financial state of the issuer. As issuers grow in size, they will wish to tap a larger market and reach a wider group of participants and so will be more likely to issue on formal markets and be willing to share the necessary information with investors. This transition is most apparent in equity markets where private placements are mainly confined to private equity/venture capital (PE/VC) investors and where the specialist nature, short history and general riskiness of the issuer is not attractive to most investors. PE/VC investors often take an active role in the day-to-day management of the company which is not something that most investors can do or wish to do. Private placements, even those of a considerable size, remain common for bond issues, though the largest issues are on formal markets. Even when bonds are issued on formal markets secondary trading remains mainly OTC.

62. The two types of markets will often exist side by side. PE/VC investors have limited time horizons and so will want to sell their holdings and a formal market is the best place for them to do this. Without formal markets PE/VC activity will remain low. Even in bond markets, where many investors hold to maturity, secondary market trading is generally low. Newly issued bonds may be actively traded but after the initial period trading is mainly limited to a small number of benchmark bonds or to credit events where portfolio adjustments are required by investors.

63. Formal markets, meaning stock exchanges, are therefore essential for substantial capital raising efforts and for involving a wide range of investors. So they are the focus of this study. They are also, by their nature, the markets where a reasonable amount of non-anecdotal information is publicly available.

**Competitive environment for exchanges**

64. As providers of frameworks for companies and other entities to raise money, exchanges face competition within the country from other sources of finance. A corporate wishing to raise long-term external funds can choose between:
• **Bank borrowing.** This is usually a relatively easy and quick process since the bank will know the borrower as a customer. There will be fixed repayment terms and a limited loss of control as long as debt is serviced so overall there is a lower cost but higher risk for the borrower.

• **Private issues including private equity and venture capital.** This is a longer process involving disclosure to a limited group of investors and more external control. Minimal liquidity will mean investors demand higher returns.

• **Public issues of equity or bonds.** This is a longer and more expensive process as more public disclosure is required. Banks will offer better terms for loans because of the lower gearing, and they will also be willing to take shares as collateral. The company will also have a higher profile with the public and investors. There will be scope to use shares to grow by taking over other companies. Higher liquidity will mean investors are likely to not require such high returns.

65. The competition for stock exchanges amounts to the issuers’ evaluation of the higher cost and longer time for the listing process versus the advantages of listing – lower risk compared to fixed income borrowing, lower required return because of greater liquidity etc. In practice the competitive factors inside a country are ease of gaining a listing (while maintaining the standards that a listing implies) and liquidity of trading.

66. Within the country the stock exchange also competes for domestic investors who have alternatives such as bank savings accounts, government bonds and real estate. If the investors do not consider that the stock exchange is a fair or safe place, they will look elsewhere. This does not imply that an exchange is risk-free, but on an exchange, investors are protected from fraud, market abuse, theft of assets, payments failures etc.

67. Stock exchanges also compete with other exchanges both overseas and domestically (for example in the USA and India). An international investor, in particular, may be prepared to sacrifice a fundamentally good investment if the investor has little confidence in the disclosure standards of the market. A foreign investor will have similar concerns to those of domestic investors – liquidity, disclosure quality etc. It may also have additional concerns relating to cross-border transactions particularly exchange controls, perhaps concerns about legal restrictions on foreign ownership, availability of custodian banks, security of settlement infrastructure and conformity with international standards. Issuers, if they are permitted to list in foreign markets, will apply the same analysis as to their domestic market to determine whether the benefits of listing outweigh the potentially higher cost of listing in the foreign market.

68. Table 2 summarises the key competitive factors based on knowledge and experience of competitive features for the type of user. The features are incorporated into the competitive drivers of the questionnaire.

### Table 2: Summary of key competitive factors and relevance to different user groups

<table>
<thead>
<tr>
<th>Issuer</th>
<th>Investor</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Domestic</strong></td>
<td></td>
</tr>
<tr>
<td>Listing process timescale</td>
<td>Market abuse regulation</td>
</tr>
<tr>
<td>Listing costs</td>
<td>Secure payments and settlement</td>
</tr>
<tr>
<td>Disclosure requirements</td>
<td>Compensation scheme</td>
</tr>
<tr>
<td>Competent intermediaries</td>
<td>Disclosure rules</td>
</tr>
<tr>
<td>Liquidity</td>
<td>Financial literacy</td>
</tr>
<tr>
<td>Taxation</td>
<td>Regulated intermediaries</td>
</tr>
</tbody>
</table>

| **Foreign** | | |
| Exchange control | Exchange control |
| Accounting standards | Accounting standards |
| Listing process timescale | Liquidity |
| Listing costs | Market abuse regulation |
| Disclosure requirements | Robust settlement – DvP/CCP |
| Competent intermediaries | Accounting standards |
| Liquidity | Custodians |

69. The questionnaires and interviews used in this study were designed to gather comparative information on these market attributes.
COMPETITIVE FACTORS

70. In the previous section some key competitive drivers are indicated. In this section a more detailed analysis is provided. These factors formed the basis of the questionnaires sent via the African Securities Exchanges Association (ASEA) to selected and other exchanges. Overriding the detailed points are two major factors which drive the competitiveness of exchanges – financial development level and size of economy. These affect both in-country and inter-country competitiveness.

Development level

71. The capital markets of Africa cover a wide spectrum of development levels. The spectrum is covered and reflected in the markets selected for this study ranging from the nascent, embryonic capital market in Ethiopia which does not yet have the basic infrastructure of formal markets, though first steps are now coming into place, to the most sophisticated and diverse markets of Kenya and Nigeria.

72. In a note dated January 2020\(^2\) the IFC reported on a study, based on structured interviews of 38 international market users, which aimed to construct a framework and some key features on development levels. The note describes an “early phase” and a “late phase”. In summary:

- **Early development phase:**
  - Government is the predominant issuer to finance its fiscal deficit.
  - Domestic investor base is dominated by banks which buy (and may be obliged to buy) government debt as part of their reserve requirement. No other significant domestic investors.
  - There is little, if any, secondary trading and, if there is an organised exchange, its reach is very limited.
  - Foreign investors may be present but mainly speculative, short-term investors.

- **Late development phase:**
  - Corporate issuers begin to access the capital market. The preference for equity or debt issuance varies from country to country. Corporate debt markets are an obvious step from government debt markets, but equity has more attraction for many investors because of its greater upside and because many countries already have long-standing, basic equity markets.
  - Domestic institutional investors, insurance companies and pension funds start to emerge. Retail investors participate both directly and through mutual funds.
  - A fairly sophisticated legal and regulatory framework exists. This will include basic legal provisions guaranteeing property rights and enforceability of contracts for capital market assets. Alongside this there will be a regulatory framework for licensing capital market participants, rules governing the issuance of securities and rules on treatment of investors by intermediaries and issuers and rules on trading/settlement of capital market trades.
  - A functioning market infrastructure exists to support trading of assets including exposure of interest, negotiation of terms, distributing trading information – and settlement of those trades including methods of recording ownership, a firm timetable for settlement to take place, management of settlement risks and arrangements to compensate for settlement failures. The infrastructure is represented by a system of processes usually supported by an IT infrastructure.

73. The late development stage market lacks many of the features of a fully developed market. However, it is a crucial interim step, with the basics of a capital market in place, and usually marks a point beyond which it is hard to revert to a system of purely bank-based or government-sourced finance.

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\(^2\)Creating Domestic Capital Markets in Developing Countries: Perspectives from Market Participants, IFC, Note 77, January 2020.
74. Countries do not advance at the same speed on all fronts. Typically, the legal and regulatory infrastructure lags behind the IT infrastructure. Most of the markets studied here have high quality IT infrastructure. Development of a culture and a capacity to support a functioning capital market comes some way even behind the legal/regulatory infrastructure. There are no short cuts; development of culture and capacity is a long process which requires diligence and willingness to take steps which are often politically challenging.

75. Inevitably, early stage markets will be far less competitive with domestic and foreign alternatives for finance and investment.

**Market size**

76. It is a truism that a larger economy will support a larger capital market, but the correlation is not linear. A larger economy will, other things being equal, have an exponentially bigger capital market than a smaller one. The corollary of this is that some economies may be too small to support a viable capital market. This is a consequence of several factors. The list below is indicative rather than exhaustive:

- High costs of regulation and supervision
- High cost of compliance for participants
- High costs of research etc. in a smaller market
- Costs of infrastructure to meet global standards
- Costs of global standard accountancy firms
- Lower liquidity as fewer participants
- Smaller pool of capital
- Fewer potential issuers
- Limited range of assets
- Limited capital of intermediaries
- Limited competition leading to high costs.

77. There are no hard and fast rules so it is not possible to predict that once an economy reaches a specific size it will be able to sustain a capital market, but an approach can be suggested. The IFC paper (mentioned above) cites a study which indicates that economies whose GDP is less than $20 billion may struggle to support a capital market. The study was published in 2007, so an adjustment is required. The total GDP of Africa has, using World Bank data for GDP (in $ at current prices), increased by 51% between 2007 and 2020. Therefore, on that basis, the level becomes $30 billion.

78. How many African countries have a GDP that exceeds $30 billion? This is not a point about Africa though Africa has a disproportionate number of countries which are small and not affluent. The $30 billion is only a guide. Outside Africa there are countries that have struggled to support viable capital markets to a large extent because of the small size of their economy (examples would include Cambodia, Laos, Georgia and the Bahamas) but Africa has more of this type of country. Some economies with GDPs exceeding $30 billion have not yet developed viable capital markets (examples would include Azerbaijan, Bolivia and Nepal). But taking $30 billion as a guide, of the 54 African countries reported by the World Bank (in $, current prices), and only 15 exceed $30 billion, as listed in Table 3.

<table>
<thead>
<tr>
<th>African Countries with GDP over $30 billion</th>
<th>GDP 2020 $ bn</th>
</tr>
</thead>
<tbody>
<tr>
<td>Algeria</td>
<td>145</td>
</tr>
<tr>
<td>Angola</td>
<td>58</td>
</tr>
<tr>
<td>Cameroon</td>
<td>41</td>
</tr>
<tr>
<td>Congo, Dem. Rep.</td>
<td>49</td>
</tr>
<tr>
<td>Côte d’Ivoire</td>
<td>61</td>
</tr>
<tr>
<td>Egypt, Arab Rep.</td>
<td>365</td>
</tr>
<tr>
<td>Ethiopia</td>
<td>108</td>
</tr>
<tr>
<td>Ghana</td>
<td>69</td>
</tr>
</tbody>
</table>
79. Solutions to the size question are simple to see but have proved difficult to implement in practice. Small capital markets can outsource their operations, but this does not address the difficulties with such markets unless the markets merge. Mergers have proved difficult in other continents with all but one of the attempts to link markets (by linking existing stock exchanges) being abandoned as failures. However, Africa has created some multinational capital markets based on common currency areas – Bourse Régionale des Valeurs Mobilières (BRVM) and Bourse des Valeurs Mobilières de l’Afrique Centrale (BVMAC). These have avoided the legacy competitive issues which have been barriers to successful cross-border exchanges elsewhere. Both groupings have combined a number of countries with relatively small GDPs (only Côte d’Ivoire, part of BRVM and Cameroon in BVMAC have GDPs over $30 billion) to create groupings covering much larger GDPs – $160 billion in the case of BRVM (making it the fourth largest market in Africa in GDP terms) and $90 billion in the case of BVMAC (making it the ninth largest GDP in Africa).

80. The flagship project supported by the African Development Bank (AfDB), the African Exchanges Linkages Project (AELP), is intended to permit cross-exchange linkages between intermediaries to facilitate cross-border trading. The initial phase of AELP will include seven larger exchanges.

**Competitive drivers**

81. Given the remarks about development level and size, there are a number of areas which mark out markets as being more or less competitive. These are described here under seven headings:

   i) Regulatory quality
   ii) Settlement infrastructure
   iii) Trading system
   iv) Intermediary capacity
   v) Issuer regulation
   vi) Accessibility of market
   vii) Taxation.

82. For many of these areas there are de facto global standards – attributes which have become the norm and which a market will be expected to have, especially if it wishes to attract foreign capital. Globalisation has driven a standardisation of capital markets just as it has in, say, manufacturing cars where there is no scope for regional or national variations. A generation or so ago national capital markets had a wide variety of, for example, trading practices but now they all follow the same models.

   i) Regulatory quality

83. Regulation is crucial to the success of capital markets as it determines whether participants, especially those less sophisticated, feel they will be treated fairly when they invest and trade. There must be a credible regulator with appropriate statutory backing and adequate resources to detect and enforce against malpractice. Market abuse – insider trading and market manipulation – are activities that can seriously weaken a capital market and the regulator needs to have both the powers to take action and the means to detect abuse. The ability to act requires a surveillance system to identify suspicious trading and trained staff to manage cases and take them through to enforcement action. Surveillance systems

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3 In contrast, takeovers of exchanges have become more common as exchanges have become private, commercial entities which has led to substantial consolidation of the industry.
are available in a range of levels of sophistication and prices and relatively simple systems are adequate for early stage and smaller markets.

84. Membership of the International Organization of Securities Commissions (IOSCO) is a common way to demonstrate regulatory capacity as the assessment process thoroughly examines the legal framework, the capacity of the regulator and interactions with other regulators.

85. The regulator must be adequately staffed and funded. The regulator may be reliant on budget allocations or may have its own income stream from fees, fines etc. IOSCO principles express a preference for self-funding over budget funding as markets become more developed as that is more likely to produce sufficient funding levels.

ii) Settlement infrastructure

86. Settlement processes and infrastructure hold the market together. Without secure and timely settlement, participants cannot trade with confidence so the market will not function. The standard is to have:

- All stock held in dematerialised form in a central depository.
- Delivery versus payment processing meaning that the exchange of stock and cash takes place simultaneously, so in the event of a default no participant is left without either stock or cash.
- Settlement cycle of T+3 or similar (there are some variations in different markets but T+3 is the entry-level standard).
- Some form of guarantee fund to give redress in the event of a settlement failure or default.

87. The most sophisticated markets will have Central Counter Party (CCP) structures. These are essential for derivative markets and are increasingly adopted in cash markets. The CCP system requires margins to be paid by buyers and sellers, essentially marking to market, so that in the event of a default the counterparty will be protected against market risk during the settlement cycle as well as credit risk. However, CCP systems are expensive and complex for users so they are mainly confined to the largest markets (and derivative markets).

88. Some markets require pre-funding of buy orders where the buyers are required to pre-deposit cash with their broker and sellers are required to demonstrate a depository holding before an order is accepted. The alternative is to rely on the brokers to make good any shortfall.

iii) Trading system

89. At one time there was considerable diversity in trading systems and a debate about the merits of so-called quote-driven systems and order-driven systems. That is no longer a live discussion. Almost all equity markets have all orders displayed to the market and orders are executed by matching the displayed orders which are executed in price/time priority (order-driven). The results of trades are displayed to the market as soon as the orders are executed.

90. In practice, exposing a large order in this way is likely to cause the market price to move against the order, so many markets have special provisions for larger trades – block trades. In most markets large orders are pre-negotiated between counterparties before being exposed to the market. Some markets also delay publication of large trades though this achieves little unless market makers are actively taking positions. Many markets have experimented with market maker systems but generally they have not been found to be successful.

91. The dominance of order-driven systems applies only to equities. Bonds are most commonly traded Over The Counter (OTC) by direct negotiation. Efforts to encourage or attract bond trading to migrate to order-driven systems have largely proved unsuccessful.

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4 DvP also protects against credit risk.
92. Capacity of the stock exchange is important – including whether the exchange is adequately staffed. The ownership structure of the exchange is also a factor. Some exchanges are government owned which tends to impede competitiveness and development, some are owned by their members which is similarly a barrier to development. The most successful exchanges in development terms are owned by non-broker shareholders either as private companies or as listed companies.

iv) Intermediary capacity and scope

93. Markets require intermediaries to ensure settlement takes place. In practice, intermediaries – brokers – have taken on a wider range of activities including order execution, research/advice for investors, fund management and corporate finance. All these activities require compliance with regulations so the norm is to require intermediaries to obtain a license from the regulator and to prohibit unlicensed entities from conducting securities business. Licensing conditions include probity of principals (directors) and staff, skill and experience of principals and staff, capacity to operate and ensure regulatory compliance of the various business activities, and adequate financial and IT resources.

94. Some regulators issue general licenses allowing a broker to engage in all regulated activities; others require specific licenses for each activity. This is mainly a function of market complexity and size – in relatively small markets brokers tend to be generalists, taking on a wide range of roles, while in larger markets brokers tend to specialise and need to avoid incurring the costs of licensing for activities they do not intend to carry out.

95. Increasingly regulators require staff and principals of brokers to have capital market specific qualifications, particularly for customer-facing staff, but also for staff whose roles involve significant risk to the integrity of the broker and the market.

96. Brokers can be independent or can be subsidiaries of other financial entities, usually banks. Historically there has been a regulatory preference for independent brokers to guard against conflicts of interest. The superior financial strength, general capacity, and opportunities from offering an integrated financial entity have raised the attraction of allowing a mix of independent and bank owned brokers.

v) Issuer regulation

97. Issuer regulation describes the standards and processes necessary to list a corporate security and then the ongoing monitoring of the listed security to ensure continued compliance. The function is usually carried out by the regulator rather than the exchange though exchanges may add their own layers of regulatory or other qualification requirements.

98. It covers a wide and diverse range of regulatory areas including:

- Content of prospectuses and assessment of prospectuses
- Underwriting of issues
- Regulation of corporate officers
- Rules determining the pricing of IPOs
- Trading and settlement procedures
- Continuous disclosures by issuers – regular reporting and intermittent releases of price sensitive information
- Accounting standards to be used by issuers in reports
- Corporate governance code and monitoring
- Takeovers and other corporate actions.

99. A key measure is time taken for a new entrant company to complete the listing process from submission to final listing. The time taken in many developing markets started out at several months. This in part reflected an overly cautious approach – so-called “merit regulation” where the regulator takes a view on the suitability of a particular investment for domestic investors. It can also reflect lack of skill in the intermediaries preparing the document, leading to frequent referrals back and rejections, or it can be that the process is inefficient.
Accessibility of market

Accessibility concerns the level of openness of the market to foreign participants. Foreign participants can have beneficial effects on a market, particularly by introducing innovative ideas or raising standards. However, they can also lead to speculative outflows and possible replacement of local participants.

Exchange controls are intended to reduce the impact of hot-money flows but can also be a severe deterrent to foreign participants. The negative effects can be reduced by having a clear framework and rules so that foreign participants can plan for and adapt to the exchange controls.

Discriminatory regulations may also restrict the ability of foreign intermediaries to participate in the market through, for example, foreign ownership limits or obstacles to foreign companies issuing into the domestic capital market.

Taxation

Taxation has a major impact on investments and so is a key factor driving investment decisions. Indeed in many markets it is the dominant factor. Fairness requires that investors bear an equitable share of the burden alongside employed and self-employed workers so most capital markets impose some taxes on investment income and gains. The main variations are:

- Taxation of dividends and interest, if taxed at all, will be subject to normal income tax. Dividends may already have been subject to profits tax on the company and some offset may be allowed.
- Capital gains, if taxed at all, may be subject to income tax or a special capital gains tax.
- Transactions may be subject to a stamp duty or other transaction tax.
- Some types of investment or investor may be subject to differential tax rates, for example pension funds may be exempt from tax on interest, dividends and capital gains. Mutual funds may be subject to tax on their investment activities, or they may be treated as pass-through vehicles with payments to unit holders being tax free with the tax responsibility falling on the unit holders.

Taxation can have a distorting effect on capital markets and the more complex the system the more likely there are to be distortions.

FUNDAMENTAL DATA ILLUSTRATES A FAILURE TO THRIVE

The quantitative survey requested information on basic metrics such as the number of companies listed, the market value of listed companies, the turnover and the number of IPOs. Some of this data was also gathered from the exchanges’ websites. Table 4 shows the data for the 12 exchanges mentioned in the Terms of Reference (TOR) and the extra exchanges that responded to the survey.

Table 4: Fundamental data for selected African Stock Exchanges

<table>
<thead>
<tr>
<th>Exchange</th>
<th>Number of companies listed</th>
<th>Number of new companies in last 5 years</th>
<th>Market Value - equities USD million</th>
<th>Market Value - bonds USD million</th>
<th>Turnover equity USD million</th>
<th>Turnover bonds USD million</th>
</tr>
</thead>
<tbody>
<tr>
<td>Angola</td>
<td>n/a</td>
<td>n/a</td>
<td>-</td>
<td>2,065.0</td>
<td>-</td>
<td>181.4</td>
</tr>
<tr>
<td>Botswana</td>
<td>33</td>
<td>5</td>
<td>3,302.1</td>
<td>1,907.9</td>
<td>64.7</td>
<td>255.5</td>
</tr>
<tr>
<td>BRVM</td>
<td>45</td>
<td>8</td>
<td>8,100.3</td>
<td>11,222.9</td>
<td>191.0</td>
<td>0.2</td>
</tr>
<tr>
<td>BVMAC</td>
<td>5</td>
<td>1</td>
<td>67.1</td>
<td>1,205.7</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Cape Verde</td>
<td>4</td>
<td>0</td>
<td>896.8</td>
<td>822.2</td>
<td>0.1</td>
<td>0.6</td>
</tr>
<tr>
<td>Egypt</td>
<td>238</td>
<td>15</td>
<td>41,377.4</td>
<td>104,326.8</td>
<td>43,842.8</td>
<td>24,033.1</td>
</tr>
<tr>
<td>Ghana</td>
<td>42</td>
<td>6</td>
<td>9,279.0</td>
<td>24,055.3</td>
<td>62.9</td>
<td>n/a</td>
</tr>
<tr>
<td>Kenya</td>
<td>60</td>
<td>2</td>
<td>21,438.4</td>
<td>n/a</td>
<td>1,363.6</td>
<td>n/a</td>
</tr>
</tbody>
</table>
### Table 5: Key market ratios for selected African stock exchanges

<table>
<thead>
<tr>
<th>Country</th>
<th>GDP 2020 USD bn</th>
<th>Equity total market value/GDP %</th>
<th>Bond total market value/GDP %</th>
<th>Equity turnover/Total equity market value %</th>
<th>Bond turnover/Total bond market value %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Angola</td>
<td>58</td>
<td>-</td>
<td>4</td>
<td></td>
<td>9</td>
</tr>
<tr>
<td>Botswana</td>
<td>15</td>
<td>22</td>
<td>13</td>
<td>2</td>
<td>13</td>
</tr>
<tr>
<td>BRVM</td>
<td>160</td>
<td>5</td>
<td>7</td>
<td></td>
<td>0</td>
</tr>
<tr>
<td>BVMAC</td>
<td>90</td>
<td>0</td>
<td>1</td>
<td></td>
<td>-</td>
</tr>
<tr>
<td>Cape Verde</td>
<td>2</td>
<td>45</td>
<td>41</td>
<td></td>
<td>0</td>
</tr>
<tr>
<td>Egypt</td>
<td>365</td>
<td>11</td>
<td>29</td>
<td></td>
<td>23</td>
</tr>
<tr>
<td>Ghana</td>
<td>69</td>
<td>13</td>
<td>35</td>
<td></td>
<td>n/a</td>
</tr>
<tr>
<td>Kenya</td>
<td>101</td>
<td>21</td>
<td>-</td>
<td></td>
<td>n/a</td>
</tr>
<tr>
<td>Malawi</td>
<td>12</td>
<td>19</td>
<td>10</td>
<td></td>
<td>-</td>
</tr>
<tr>
<td>Mauritius</td>
<td>11</td>
<td>81</td>
<td>11</td>
<td>2</td>
<td></td>
</tr>
<tr>
<td>Nigeria</td>
<td>432</td>
<td>11</td>
<td>1</td>
<td></td>
<td>-</td>
</tr>
<tr>
<td>Rwanda</td>
<td>10</td>
<td>35</td>
<td>7</td>
<td></td>
<td>6</td>
</tr>
<tr>
<td>Sudan</td>
<td>21</td>
<td>7</td>
<td>3</td>
<td></td>
<td>-</td>
</tr>
<tr>
<td>Tanzania</td>
<td>62</td>
<td>11</td>
<td>10</td>
<td></td>
<td>16</td>
</tr>
<tr>
<td>Tunisia</td>
<td>42</td>
<td>20</td>
<td>-</td>
<td></td>
<td>n/a</td>
</tr>
<tr>
<td>Uganda</td>
<td>38</td>
<td>15</td>
<td>0</td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Zambia</td>
<td>18</td>
<td>11</td>
<td>-</td>
<td></td>
<td>n/a</td>
</tr>
<tr>
<td></td>
<td>1506</td>
<td>11</td>
<td>11</td>
<td></td>
<td>16</td>
</tr>
</tbody>
</table>

**Source:** Various as described, World Bank, consultant analysis
107. The basic data shows:

- Almost all the exchanges are small. Even the larger ones such as Egypt and Nigeria are small in global terms. To put some context to this, the total equity market value of the 17 exchanges is less than 50% of the equity market value of the Philippines stock exchange, itself not seen as a vibrant growth market.

- Except for Egypt, none of the exchanges has a total market value which exceeds 20% of their GDP, an indication that the public capital market is not an important factor in the economy.

- Except for Egypt, none have significant bond markets – the bond market data presented here covers both government and corporate bonds.

- The total number of new companies in the five years to end 2020 is 72, slightly more than one per month across all the 17 exchanges. New companies add to the total size of the market but more than that, a steady stream of new companies attracts investors to the market which boosts liquidity and prices. For context, the Johannesburg Stock Exchange (JSE), which is not a strong exchange for IPOs, had 33 IPOs in that period.

- Except for Egypt, the 17 markets are illiquid. Most of the other exchanges have a turnover to market value ratio (velocity) of between 0 and 10, extremely low by the standards of other world exchanges.

108. However, the figures for market value given above overstate the investability of the markets. Much of the listed stock cannot be traded because it is held by directors, subject to lock-in rules and other similar restrictions. Table 6 shows the percentage of free float (i.e. tradeable) shares for the markets in the study for which data is available. Table 6 also shows the market value and the tradeable market value after applying the free float adjustment (the free float percentages are for 2018 so the comparison with 2020 market values is only indicative).

<table>
<thead>
<tr>
<th>Market Value 2020 – equities USD million</th>
<th>Free float (%) 2018</th>
<th>Adjusted market value 2020, USD million</th>
</tr>
</thead>
<tbody>
<tr>
<td>Botswana</td>
<td>3,302</td>
<td>49</td>
</tr>
<tr>
<td>BRVM</td>
<td>8,100</td>
<td>3</td>
</tr>
<tr>
<td>BVMAC</td>
<td>67</td>
<td>11</td>
</tr>
<tr>
<td>Egypt</td>
<td>41,377</td>
<td>32</td>
</tr>
<tr>
<td>Ghana</td>
<td>9,279</td>
<td>56</td>
</tr>
<tr>
<td>Kenya</td>
<td>21,438</td>
<td>36</td>
</tr>
<tr>
<td>Malawi</td>
<td>2,283</td>
<td>45</td>
</tr>
<tr>
<td>Mauritius</td>
<td>8,872</td>
<td>24</td>
</tr>
<tr>
<td>Nigeria</td>
<td>45,881</td>
<td>38</td>
</tr>
<tr>
<td>Tanzania</td>
<td>6,900</td>
<td>35</td>
</tr>
<tr>
<td>Uganda</td>
<td>5,700</td>
<td>18</td>
</tr>
<tr>
<td>Zambia</td>
<td>2,038</td>
<td>63</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>155,237</strong></td>
<td><strong>34</strong></td>
</tr>
</tbody>
</table>

*Source: Bright Africa 2019 RisCura Group, consultant analysis*

109. The IFC study (cited earlier) mentions that some markets have developed in a satisfactory way, passing through the “early phase” stage but have then settled down to a stable but suboptimal equilibrium. Morocco is quoted as such a market which has significant size but whose growth has slowed. Various donor initiatives have been tried in Morocco, for example the European Bank for Reconstruction and Development (EBRD) supported a project to develop derivative rules, but the market after promising
progress shows a tendency to stagnate. In terms of IPOs the Casablanca Stock Exchange had two in 2016 and only one in the following 4 years (2017 – 2020).

110. As an indication of different results for exchanges in other regions, Table 7 shows four Asian comparator exchanges. Their results have been mixed:

- Market value of equity as a percentage of GDP is over 100% for three of the markets but not for Dhaka which, despite high GDP growth, has not seen a proportionate growth in its market.

- Most remain no more liquid than the 17 African markets though Thailand’s liquidity (velocity) is on par with developed markets.

- All have seen steep rises in market value driven by upward revisions of valuations.

111. The most significant factor is the number of IPOs – 396 over the 5-year period or 6.6 a month over only four exchanges. The success in attracting IPOs has not been even across exchanges. Bangladesh and the Philippines have been notably less successful than Thailand and Indonesia.

<table>
<thead>
<tr>
<th>Number of listed companies</th>
<th>Market value of listed companies USD million</th>
<th>Turnover of listed companies USD million</th>
<th>IPOs</th>
<th>Equity total market value/GDP %</th>
<th>Equity turnover/Total equity market value %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bangladesh (Dhaka)</td>
<td>329</td>
<td>45,939</td>
<td>15,151</td>
<td>28</td>
<td>14</td>
</tr>
<tr>
<td>Indonesia</td>
<td>271</td>
<td>1,598,570</td>
<td>158,627</td>
<td>216</td>
<td>151</td>
</tr>
<tr>
<td>Philippines</td>
<td>743</td>
<td>496,086</td>
<td>36,878</td>
<td>19</td>
<td>137</td>
</tr>
<tr>
<td>Thailand</td>
<td>713</td>
<td>543,165</td>
<td>496,865</td>
<td>133</td>
<td>108</td>
</tr>
<tr>
<td></td>
<td>2,056</td>
<td>2,683,760</td>
<td>707,522</td>
<td>396</td>
<td>120</td>
</tr>
</tbody>
</table>

Source: Consultant analysis

Attracting new listings

112. Attracting companies to listing is an arduous and time-consuming process. A project\(^5\) in Kenya in 2015 assessed why the newly opened Growth Enterprise Market Segment (GEMS) aimed at Small/Medium Enterprises (SMEs) had at the time only attracted one company. Extensive consultation with listed and unlisted companies showed companies did not list because:

- Most prospective companies were family owned and were able to rely on internally generated funds or funds supplied by family members to meet their expansion needs which were generally not ambitious. They had achieved a certain level and were comfortable to remain at that size.

- Their banks were willing to support any needs for additional capital. They had long-standing relationships and banks would readily extend modest loans for working capital with fairly simple, straightforward processes.

- The process of listing is complex, slow and seen as unpredictable.

- Listing implied ownership dilution and being subject to control by outsiders. The governance requirements enshrine this by requiring non-executive directors, separation of chief executive and chair roles etc.

- The share price would be subject to market volatility and uncertainty.

• The accounting requirements are seen as complex and expensive to comply with since few small companies have anything but the most basic book-keeping systems.

• Greater financial disclosure is not seen favourably especially by a smaller business. More transparency may also increase tax liabilities or lead to unwelcome investigations from the tax authorities.

113. The main problem is a lack of appreciation that developing a stock market company listing requires marketing. This requires companies to be educated on the wider value of listing in addition to gaining an alternative source of finance. Companies have limited appreciation of the reputational gains, the ability to use stock to finance takeovers, regular valuations and using equity as leverage. Nor do they appreciate that better accounting and better governance are not just arbitrary penalties but bring benefits which improve the company. Most exchanges appreciate the importance of marketing to investors, with roadshows and conferences being widely used, but fewer appreciate the need to market listings.

114. So, unless prompted and supported, companies may not come forward for a listing. In the most developed markets, intermediaries such as investment banks will seek out prospects for floatation but in developing markets these roles are less apparent or available.

115. The figures in Table 7 show the relative success of Thailand in attracting IPOs, partly supported by a several-year tax break for newly listed companies, but that is not unique to Thailand. Much of Thailand’s success is due to the vigorous promotion of listing by the Stock Exchange of Thailand (SET). The SET has a specific department tasked with promoting and supporting listing. The staff seek out potential new listed companies and work with them to develop their understanding of listing benefits and processes. Once identified, the potential new companies are supported to develop their internal processes and structures – governance, accounting etc. Then the process becomes easier and less daunting for potential new entrants.

CONCLUSIONS ON COMPETITIVENESS OF AFRICAN CAPITAL MARKETS

116. This section presents the key findings on competitiveness from the analysis of the surveys, interviews and other data gathered during the project. Using these findings, a visual model was created with rankings which show the competitive position of the exchanges studied. A more statistical/econometric model was considered but this was conceptually unsuitable. The visual model offers a clearer view. The data supplied by the exchanges and by the qualitative survey (with supporting interviews) generally suggested that the main issues for market participants were linked to smallness of market size – issuers, investors, and liquidity – and these feature strongly in the visual model. The responses also supported the consultant’s long experience working at and with stock exchanges – that the direct costs levied by exchanges and regulators are not major drivers of user participation. Costs viewed in a more diverse way are important, though difficult to measure, and the most important costs associated with trading and listing are not represented by most published fee scales. Appendix C gives the results of the Quantitative Survey. Appendix D gives the summary results of the Qualitative Survey.

Universal infrastructure models and standards

117. It is striking how little diversity there is in trading structures and settlement structures among African markets covered in this study. If this study had been carried out in Europe 35 years ago there would have been almost as many trading models and settlement models as there were exchanges. Some exchanges had dealer-based trading systems, some had pure agency (broker) systems and most had some sort of hybrid system with special types of dealer and broker, each fulfilling specialised roles.

118. Looking now at the European markets this has all changed. Every market has practically the same trading system, all have a public order book with conventional rules on order types, order priorities etc. All have near instantaneous post-trade disclosure, all have auctions to open and close the market, all have circuit breakers and so forth. Many things have brought this about – some regulatory pressure, some IT-driven factors (having a standard system is much cheaper than adding complex extra features) but predominantly it was what all the users required of an exchange. So exchanges, which have
gradually become more commercially focussed, (especially those which have gone fully commercial as listed companies) have been able to comply with the needs of their users.

119. Similarly, each exchange had a different method of settling business – some paper, some dematerialised, different settlement periods etc. Again, now they are all the same – dematerialised T+3, Delivery versus Payment (DvP), with Central Counter Parties (CCPs) in some cases. It has taken over 20 years to travel from the old situation of diverse trading and settlement to a single, homogeneous model.

120. In Africa there is almost no diversity. It has skipped the old model with local peculiarities for a single model. This is one of the striking features from the data survey results. All exchanges have practically the same trading and settlement systems. Africa has the advantage not only of having the internationally accepted models but also of not having to go through the long transformation process which European exchanges and others – South Asian markets had many local trading and settlement peculiarities – have undergone. What is required in terms of infrastructure by global investors and issuers is exactly what all the African exchanges have.

International-standard regulatory models

121. A similar correspondence with international norms exists in regulatory structures among the 17 exchanges covered in the study. Again, if one had looked at Europe or any other region 30 years ago there would have been a range of regulatory structures and organisations. This has now changed to a relatively standard approach (within EU rules). Among the African markets the standard model has been there since the start:

- All the markets have a national regulator with statutory powers.
- All are IOSCO members – which ensures a certain, minimum standard of regulatory powers.
- All have legal prohibitions on common types of market abuse – insider trading and manipulation.
- All regulators have licensing authority over intermediaries.
- All have requirements for issuers of securities to ensure fair presentation of prospectus information.
- All have requirements for regular updates of financial information for listed companies.
- Most have basic corporate governance requirements for listed companies.
- Most have accounting standard requirements for reporting by listed companies – usually IFRS.
- Most have computer-based systems for detecting market abuse.
- Most, but not all, require brokers to have specific capital market qualifications.

122. There is still some diversity which largely reflects differences in market size and levels of financial development:

- The permitted scope of brokerage business varies, with some allowing brokers to offer a wide range of services while others limit brokers to a narrow order execution role. Generally in other regions it has been recognised that limiting the role of brokers reduces their quality and restricts the market but some regulators in less developed markets rightly remain concerned about conflicts of unmanaged interest and the capacity of brokers to manage wider business models.

- Some regulators have delegated some parts of their responsibilities to Self-Regulatory Organisations (SROs). This is an ongoing debate. SROs may have closer awareness of the market and better capacity than national regulators but equally exchanges may be less motivated to regulate their own customers especially if they are organised as private companies.

- Some regulators are funded entirely by charges levied on market users – as IOSCO suggests – but others remain at least partly government funded. The fairness argument for users paying the regulatory costs is widely accepted but in some markets at an early stage of development a self-financing regulator is impractical, so government support is required.

123. Regulatory structures are one aspect, but implementation of regulation and enforcement is another and depends heavily on capacity and commitment to be fully effective. There are likely to be considerable divergences between the regulatory standards of different markets, but this is something of which users
Accessibility of markets getting easier in most markets

124. In 2012, the consultants for this study carried out a project to assess the feasibility of a Pan-African Stock Exchange. The conclusion was that such an entity was unlikely to be feasible in the prevailing situation. The main reason for this was the strong barriers in place to prevent free movement of capital and access to markets for foreign companies. These barriers included restrictions on capital movements and restrictions on foreign companies being listed in the domestic market. This situation appears to have changed considerably.

125. The current situation is of a far more relaxed attitude to foreigners accessing the market. There is a greater acceptance that foreign investors, while they bring risks, also bring significant benefits to local capital markets by allowing new capital and by stimulating improvements in standards. The data gathered was not entirely complete but enough to get a reasonable picture.

- Almost half of the markets reported no restrictions on investment outflows. These include most larger markets where foreign investors are most likely to operate and where the risks of destabilising capital flight are less. Most of the other markets have controls but operate them in a rule-based environment – foreign investors may be deterred by exchange controls, but they are less deterred by predictably-applied restrictions. Many of the larger markets and some of the smaller ones have significant, sometimes majority, ownership by foreign investors.

- Countries have largely removed foreign ownership limits on domestic companies. In some cases, these are retained for sensitive industries, but the limitations only cover a narrow range of industries.

- All the markets permit custodians to operate, and most have globally recognised custodians operating in the country. Custodians are generally preferred by foreign investors to manage their securities holdings.

- All the respondents permit domestic companies to list on foreign markets. In smaller countries, especially, this is beneficial as often there is a single large company in a market – say the telecoms company – whose capital needs exceed the capacity of local investors, and whose domestic market is not yet within the scope of foreign investors. Such a company may have to look abroad.

- Similarly, most exchanges allow foreign companies to list on their domestic market and several of the exchanges have major foreign companies listed. These do not generally trade much since most trading takes place on the larger home market, but the situation indicates openness and also provides investment opportunities for local investors.

- The major markets permit foreign brokers to operate in their markets. In all cases these foreign brokers are required to set up separately managed and capitalised subsidiaries. This is normal practice globally as it is necessary for local regulators to have a local entity to regulate.

126. In summary, the strong barriers which existed have been relaxed in most countries and no longer significantly deter foreign participation.

Business development

127. The discussion so far relates to the market infrastructures which are the environment which supports and sustains a market. The main element in the success of a market is that there are people who want to buy assets and those who want to sell them in sufficient numbers to justify the costs of running the market. This has not been the case in Africa so while the infrastructure is international standard, the

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“failure to thrive” – all the markets studied remain small in relation to their economies and hence their full potential is not being achieved – reflects the lack of buyers and sellers, investors and issuers.

**Investors**

128. A shortage of investors is a universal feature of developing markets. The long-term savings institutions (pensions savings) have not yet developed, the collective savings investments do not exist, and foreign investors are at best transitory participants. In the early stages of market development, the main investors are usually banks and retail investors.

129. Banks are not generally regarded as the “right” investors for capital markets – their timeframes are too short, the assets compete with their normal business lines and prudential regulators usually place substantial haircuts on capital market assets.

130. Retail investors will form the underpinning of the market before other investors have entered. Most markets seek to encourage development of institutional investors because they want their populations to have the benefits of pension provision and other long-term savings vehicles. Some markets remain predominantly retail. Nepal is an example where capital market policy has been to extend stock market investment (which is in practice speculation) to the widest possible section of the general population. Currently between 20 and 30% of the population have active accounts at the national depository.

131. African markets have sought to develop a broader range of investors. Foreign investors, as already noted, have become important in many markets and the legal infrastructure for Collective Investment Schemes (CIS) and pension plans has been developed. However institutional investors, while they exist and command significant funds, have not become actively attracted to the stock market. The data for Nigeria shows that pension funds invest predominantly in foreign bonds and bank deposits while their CIS funds invest predominantly in money market assets. This indicates that, so far, stock exchange and stock exchange intermediaries have not successfully drawn significant savings into the stock market. There is speculation, which is necessary to spark activity, but there is no flow of long-term savings into stock market assets; the stock exchange does not offer a vehicle for the savings of the population at large.

132. The lack of involved investors is one reason for the lack of liquidity in all the exchanges studied but it is also linked to the lack of listed companies and IPOs.

**Issuers**

133. The shortage of issuers is even more acute than the shortage of investors. All the exchanges, even the most successful and highly developed ones, have few listed companies, have market values which are small percentages of their GDPs and have few IPOs. It is often said in development discussions that getting a few large to very large companies to list can be transformative. Listing a major bank, a major mineral company or a major telecom company can give a market an initial boost. Many of the markets studied do have some large companies which dominate their markets. Nigeria has four large companies (two cement and two telecoms) which make up 60% of the total market value. But from then there needs to be a continuous stream of new companies coming to the market. New companies generate excitement in a market and prospects for gain – buying at the IPO in expectation of an early increase in price and because new companies are in their growth phase so offer longer-term capital gains. Growing companies are also interested in acquisitions which generate further activity on the market.

134. A number of exchanges have realised this and have developed growth markets to attract such companies, but the results have generally been disappointing. In part the lack of IPOs probably reflects the fact that many of the countries, especially the smaller ones, do not have many growing companies in growth industries. Evidence suggests that the larger, more developed countries will have companies in IT, marketing, consultancy and distribution which are likely to grow and have need for capital. They also need the other benefits of listing – higher profile, better governance, better accounting, and better incentives for managers and owners.

135. However, the exchanges are competing with other sources of those benefits – banks and fledgling Venture Capital/Private Equity (VC/PE) but these competitors benefit from a strong listed market.
VC/PE investors are medium-term, so they need an exit mechanism. VC/PE exits are through trade sales or listing, with listing probably the more favoured. In addition, bank creditors benefit from the reduction in gearing which is provided when the ratio of debt to equity is reduced.

136. Therefore, all parties benefit from a strong listed market but there is a need for active marketing by exchanges and intermediaries, ideally working together. The listing activities need to be made as simple as possible, by helping companies with the transition – assistance with accounting, governance etc. and the regulatory processes. It is complex to assess the ease or difficulty of the listing process. It is even more difficult to assess the cost of a listing – the regulatory fees and sometimes the underwriting fees may be published but the real costs are far higher. These are not only the transformation costs to ready a company for listing but also the costs generated by the pricing system. Companies selling their shares need reassurance that they are doing so at a fair price. Equally, investors in new companies are taking a risk and need to feel there is some early upside. Getting this balance right is not easy and the mechanism for settling the issue price is sensitive to many structural factors. Most survey respondents use some combination of book-building, auctions and syndication to decide IPO prices – which is positive. Even then the process may be biased – book-building has been manipulated in several countries, Bangladesh being a prime example, and this is easier in smaller markets with few competing members in the book-building or syndication.

137. Given that pricing is hard to measure, the survey focussed on the ease or difficulty of listing. The respondents were asked about the time taken for a typical IPO as an indication of the efficiency of the regulatory processes. Not all responded which suggests that the non-respondents do not know – which may, in itself, be indicative. Of the 11 responses, two indicated less than one month. The remaining nine mainly indicated two months or more, usually over three months. These time frames are too long and indicate there is scope for streamlining the process and for building capacity in the regulator and the intermediaries to reduce the number of times an application is sent back for revision.

Commercial approach

138. Inevitably, given the need to attract new business, a key part of a market’s success lies in the drive of those in charge to develop the market. Some regulators have a specific responsibility but, since all regulators are government owned but with operational independence, their role tends to be limited to facilitating rather than driving forward development. The true driver for development will be the intermediaries and importantly the exchange which has the central role. The more the exchange is driven to develop the market, the more development there will be. To put this in context the study looked at two pieces of data – ownership of exchanges and diversity of assets traded.

Ownership of the exchange

139. Traditionally exchanges were operated as member organisations which tended to do the bidding of their members and to set the interests of the members over those of other market users. Development, therefore, only happened if the members wanted it. Many actions which exchanges have taken (sometimes with encouragement from the regulators), such as changing trading systems, allowing negotiated commissions or increasing surveillance have run contrary to the short-term interests of much of the membership. So, these changes were difficult for member owned exchanges to implement. Other exchanges have been government owned which has also presented barriers to development because of political pressure and inertia. Most exchanges are now privately run and many are listed across the world, including Africa. Therefore, the ownership model gives an indication of the incentivisation of exchanges to develop their market.

140. Of the 17 exchanges examined, five are listed (or about to become listed), five are private companies and seven are member or government owned.

Diversity of assets

141. A number of the studied exchanges trade a wide variety of assets, and this is an indicator of the exchange’s willingness to seek out new trading opportunities. Innovative exchanges tend to display a portfolio of new instruments such as Exchange Traded Funds (ETFs), Real Estate Investment Trusts (REITs) or derivatives. Sometimes the market is not ready for a new product so it does not take off and
may be abandoned but others will succeed and become sources of trading and revenue for the exchange. Derivative exchanges go through a process of continuous innovation with new products being tried and scrapped if they are not successful. The SET in Thailand introduced interest rate futures but these did not succeed and were abandoned, largely because Thai interest rates are closely linked to global rates and the main markets for those are on the Chicago Mercantile and Deutsche Borse. SET then introduced a highly successful retail gold future and option. An exchange must be willing to take a risk on something which may not work – and it has to have the support of the regulator.

142. Only one exchange, Nairobi, among the 17 surveyed offers derivatives but several offer ETFs and REITs. Nigeria offers the most asset types with nine, followed by Mauritius with eight (Mauritius is an unusual and innovative exchange which has created a niche by offering specialised products). At the other end of the scale some only offer two or three products which are appropriate given the stage of development of their market, so diversity of traded assets is an indicator to be considered with care.

**Size of Market**

143. Size of the market is a measure of success, but it is also a major contributory factor – it is no accident that the USA has the biggest, most developed, most flexible capital market in the world. Being the biggest economy is not the only factor however – China’s economy rivals that of the USA in GDP but its capital market is much smaller. Size brings a diversity and abundance of investment, a plethora of high quality and dynamic issuers, economies of scale, liquidity and an abundance of skilled practitioners. By contrast small countries struggle to compete.

144. In Section 4 (Competitive Factors), it is reported from a study that viable capital markets are less likely to develop in countries with GDPs below $30 billion. Many small countries in Asia, Europe and South America have tried and largely failed to develop worthwhile capital markets. Their small size will deter domestic companies from issuing or encourage them to issue in neighbouring, larger markets. Comparing GDPs and market capitalisation of the countries in the survey tends to confirm that GDP and market size are strongly correlated (correlation coefficient is 0.93 for 16 countries – Angola has no equity market so was not included). Figure 1 illustrates this and the gap between the largest and the rest (some country labels had to be omitted for clarity).
Figure 1: Exchange equity market value against GDP

![Diagram showing exchange equity market value against GDP](image)

Source: World Bank, World Federation of Exchanges, Consultant analysis

145. A unique feature of African markets is the existence of successful groupings of countries into single multi-country exchanges. Various attempts to link or combine exchanges in other regions outside Africa have failed. However, globally many exchanges have become conglomerates, which have many of the benefits of groupings. For example, Euronext and Nasdaq each own and operate several national exchanges with a common IT platform. The two African exchange groups have had the effect of offsetting the small size of the economies of some group members giving them access to a larger market. It is not clear whether the viability of these groups depends upon them being in the same currency zone and whether the model is extendible to other African regions. The proposed African Exchanges Linkage Project (AELP) will, when implemented, test whether there is viability in exchange linkages (which are different to a single regional exchange but have the same aim) and a workable model for Africa.

146. The above analysis suggests that all or most of the markets are compliant with international practice in the areas of infrastructure, regulation and accessibility. Since these are basic requirements, meeting them does not confer any special competitive advantage.

147. The areas where there do appear to be competitive advantage are size of market and an amalgam of features which could be termed Business Development Drive (BDD). The amalgam is less precise than size, but it can be represented by a combination of 1) exchange ownership model 2) diversity of tradeable assets and 3) number of IPOs. The value of IPO numbers might be questioned since all the exchanges have extremely low numbers by world standards but this is a regional comparison so it...
148. Exchanges are categorised into four groups using size and BDD and shown in Table 8.

Table 8: Exchange competitiveness assessments

<table>
<thead>
<tr>
<th>Market size</th>
<th>0</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
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<tbody>
<tr>
<td>Small</td>
<td>Malawi</td>
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<td>Rwanda</td>
<td>Botswana</td>
<td>Mauritius</td>
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<tr>
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<td>Zambia</td>
<td>Tunisia</td>
<td>Angola</td>
<td>Uganda</td>
<td>Ghana</td>
<td>BVMAC</td>
</tr>
<tr>
<td>Large</td>
<td>BRVM</td>
<td>Nigeria</td>
<td>Egypt</td>
<td>Kenya</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Consultant analysis

149. The three exchanges in dark red boxes are in danger of being unsustainable. Their potential markets are small and have limited BDD.

150. The five exchanges in paler red boxes are, the analysis suggests, in a challenging situation. They still have small potential markets and show limited BDD. They are state/member owned, have had few IPOs and have a limited product range. Bourse des Valeurs Mobilières de l’Afrique Centrale (BVMAC), notwithstanding the rating, is an operationally successful group.

151. The four exchanges in yellow boxes can be seen as promising but need to continue to improve. They are still in small markets but display better levels of BDD, suggesting that they may be able to overcome the size disadvantage and develop their businesses.

152. The five exchanges in green boxes are in larger economies or regional groupings of economies (except for Mauritius which has developed a highly specific and successful business model which is not limited by the small size of the Mauritius economy), and they have exhibited the drive to expand their business. Egypt will remain constrained by its government ownership but, nonetheless, it has successfully developed its business.

RECOMMENDATIONS FOR INTERVENTIONS

153. The previous section has identified the key drivers of competitiveness. This section details some interventions which the African Development Bank (AfDB) could consider to further the development of African capital markets. The interventions cover:

i) Diversification of traded asset types
ii) Greater use of regional groupings
iii) Monitoring and prevention of market abuse
iv) Corporate governance
v) Improving the environment to attract new listings
vi) Improving the business focus of stock exchanges
vii) Developing institutional investors
viii) Supporting greater availability of regular, reliable and consistent data.

There is a separate section for Ethiopia which focusses on adding to the current work by assessing the corporate demand for finance.
i) Diversification of traded asset types

154. The results of the quantitative survey suggest that many markets in Africa have only a limited number of products – asset types – which they trade. Almost all the surveyed exchanges trade equities, corporate/government bonds (in practice the exchange trading of bonds is very small, as it is in most markets) and maybe a few specialised products, but the range is limited. Several trade Collective Investment Schemes (CIS) and a few trade Real Estate Investment Trusts (REITs) but only one of the exchanges studied trades derivatives.

155. In some ways this is to be expected as most are relatively new markets, and the local financial system has not developed the demand for a wider range of traded assets. However, there is no commercial reason for this limited approach. Even a new, relatively small exchange can offer a wider range of tradeable products. For example, countries with a significant Islamic population could offer Islamic Finance assets such as sukuk (currently available only in Sudan, Nigeria and Egypt) or countries with stronger environmental interests could develop green bonds. Most countries in the continent have high infrastructure needs so infrastructure bonds and securitisation could also offer a route to raise funds.

156. In very developed markets with highly competitive participants and highly commercial exchanges there will be an impetus for the introduction of new assets. In developing markets this does not happen at the start. Many new products are not successful but it is part of the development process to see which assets are attractive to local users and to judge the appropriate timing in the development cycle. Pump-priming activities by development partners can give initial support. In other regions development partners have supported feasibility/demand studies to assess the readiness of the local market for new products. Feasibility studies are often followed up with support for rule writing and infrastructure enhancements – for example the European Bank for Reconstruction and Development (EBRD) has supported the Casablanca Stock Exchange in writing derivative rules. AfDB could usefully offer similar interventions to diversify the product range and increase the income of African exchanges.

157. AfDB could benefit the capital markets by assisting this development in Africa by:

- Conducting feasibility studies in countries with a narrow asset range. The studies would include assessing supply, demand, and infrastructure requirements.
- Depending on the results of the feasibility study, assist in drafting rules or regulations leading to a time-bound action plan for implementation.
- Assist the regulator and exchange in the introduction of the new product.

ii) Greater use of regional groupings

158. There are the two successful regional groupings – Bourse Régionale des Valeurs Mobilières (BRVM) and Bourse des Valeurs Mobilières de l’Afrique Centrale (BVMAC) – which are an unusual feature of African capital markets. Both of these groupings are based on currency areas which reduced some of the barriers especially those linked to exchange control. The approach has attractions for other groupings which do not map on to common currency areas. The challenges for smaller capital markets are well known:

- Fixed costs of running and regulating a market
- Costs for investors up setting up in a small market
- Limitations on large national issuers which are too big for the local market
- Lack of domestic investors which leads to low liquidity.

159. Africa has many smaller countries where the viability of a separate capital market is doubtful. The smaller countries have several options:

- Join groupings like BRVM or BVMAC. The risk is that the largest members of the group will, inevitably, dominate. The capital markets of Côte d’Ivoire and Senegal in BRVM and Cameroon in BVMAC are much bigger than those of other group members. It is likely that the larger countries will become the financial hubs for the group.
• Outsource their capital market to a larger neighbour and have their companies listed there. This has not proved popular elsewhere and means that the smaller members never develop any capital markets capacity, expertise or employment. Ireland is an example which was part of the UK stock exchange until the mid-1980s and has since found it somewhat difficult to carve out a viable, local niche – its current focus is on becoming a specialist listing venue for CIS instruments.

• Adopt a midway approach where capital markets are distributed among the group members and share common facilities (such as IT platforms) and have common standards. Market intermediaries and listed companies are passported throughout the group. The EU (which is not a single currency area) is the best example of this. Most of the EU stock exchanges are now part of larger groups but the distributed market model means that smaller financial centres are able to carve a business role based on their local expertise so retaining the employment and other benefits of having local capital market activities.

• Continue as independent markets but risk struggling to offer services that meet international standards and, over time, lose their companies and investors to a larger market. The African Exchanges Linkage Project (AELP) could present a further alternative. It is a system for linkages between brokers which is essentially a correspondent broker network, so it avoids many of the settlement, regulatory and other challenges of inter-exchange linkages (which have been tried in other parts of the world with little success). At some point this could be attractive to smaller exchanges enabling local brokers to offer a wider market to their customers. However the initial and understandable focus of AELP on the largest markets means it will not initially help the smaller countries.

160. AfDB could benefit the capital markets by assisting in this development in Africa by conducting a study on the best way of helping smaller countries to develop viable and sustainable capital markets which allow them to have the benefits of a capital market without handing over to a larger market and losing the local benefits of an active financial sector. This would need to involve the successful groupings and other incipient groupings such as the East African Federation and existing groupings such as the Southern African Development Community to provide a viable and acceptable way forward.

iii) Monitoring and prevention of market abuse

161. Detection and prosecution of market abuse is a key factor in raising investor confidence and encouraging investor participation. The survey results showed that all the surveyed markets had legal prohibitions on abusive practices but that is only the beginning of an effective regime to prevent market abuse which requires development in six areas:

i) **IT infrastructure.** Surveillance systems offer sophisticated techniques for identifying abuse and building evidence for prosecution. Most of the surveyed markets had a computerised surveillance system and several had installed the Nasdaq trading system which includes a surveillance module using the SMARTS system which is well regarded by the industry.

ii) **Staff capacity.** IT can only go so far. It is also necessary for the staff charged with monitoring and prosecuting market abuse to have a good understanding of abusive techniques, clues to such abuse taking place and skills to collect and manage evidence. Most suppliers of surveillance systems will offer a level of training especially in configuration of alerts, but more extensive training is required. Sometimes developed markets will provide assistance; for example Uzbekistan is trying to develop surveillance capacity and is being supported by the US SEC which is providing long-term embedded experts and secondments for local staff.

iii) **Clarity of regulatory responsibilities.** Globally countries differ in how they organise their market abuse regulation. In some the exchange has the frontline role as a part of its market supervision role. The exchange will have the market abuse surveillance responsibility delegated to them under a Self-Regulatory Organisation (SRO) arrangement but will pass cases along with evidence to the regulator for further investigation and enforcement action which may include working with national prosecutors where criminality is suspected. The SRO arrangement will delineate the responsibilities of the agencies. In other markets the exchanges have limited responsibility for market abuse and the regulator takes the main role conducting
real-time and off-line surveillance and gathering evidence for prosecution. This is essentially a policy choice – though the tendency has been away from exchange-based regulation in recent times. One important factor is that in markets with multiple trading venues (say an equity market and a separate derivatives market), centralisation in the national regulator which oversees all markets will ensure that cross-market abuse is more likely to be detected and enforcement action taken.

iv) **Legal structure.** Market abuse warrants penalties and usually there is a range of sanctions from administrative fines levied by the regulator through to criminal convictions. It is essential that this structure is appropriate and effective. An example of where this is not the case is Nepal where the sanctions available are a fine of up to NPR 300,000 (approximately USD 2,500) or forfeiture of any profits made from the abuse or one year in prison. The prison option requires a very high level of proof which the regulators are not able to supply. Unsurprisingly market abuse is quite common in Nepal. It is also important for judges to have an understanding of markets and market abuse. Training can be supported by development partners – for example, the EBRB has funded the training of judges in Ukraine and other Eastern European countries and the Asian Development Bank (ADB) has funded training in Bangladesh among other countries.

v) **Escalation processes.** Successful prosecution requires cooperation between agencies and processes/agreements to support that cooperation. For example, cases which might lead to criminal sanctions are usually prosecuted by a Department of Justice (DOJ) or similar, whereas lesser offences are subject to administrative sanctions (for example fines, suspensions, public censure). For this to work there needs to be a solid relationship between the regulator, the DOJ, and the police authorities.

vi) **Political support and legal protection for regulators.** In some jurisdictions there can be outside pressure from influential individuals for a more relaxed approach to regulation and this may sometimes deter regulators from prosecuting cases with sufficient vigour. It is also sometimes the case that regulatory staff do not have sufficient legal protection from being sued by market players though international Organization of Securities Commissions (IOSCO) compliance requires this. The norm is for staff to have legal protection if they are acting in good faith in accordance with their legal role. Lack of political support and legal immunity can impair effective prosecution of market abuse and are difficult to resolve though enshrining strong legal protections can help.

162. The AfDB could benefit African capital markets and so support African financial sector development by:

- Assisting in the acquisition of IT infrastructure by funding and assisting with procurement plans.
- Arranging for capacity building for surveillance staff perhaps by setting up links with foreign regulators offering on-site training or secondments.
- Assisting in the drafting of SRO agreements between agencies or otherwise fostering close cooperation and clarity between agencies such as between the regulator and prosecution authorities.
- Supporting external assessment of legal/regulatory arrangements to ensure there are no gaps through which abusers can operate. This would include legal protection/immunity for regulatory staff.
- Supporting drafting of MOUs or similar agreements between the regulator and the other parts of the criminal justice/national courts.
- Supporting training for legal professionals including prosecutors and judges to enable them to operate confidently in complex market abuse cases.
iv) Corporate governance

163. The survey results suggested that most of the surveyed markets had some regulations regarding Corporate Governance (CG) requirements. The survey did not provide enough information for an evaluation of the codes or regulations, so it was not possible to comment on the standards of governance – though they are likely to be relatively low based on experience of other developing markets. In support of this the FTSE Quality of Markets Matrix, which allocates countries into one of the four index groups (Developed, Advanced Emerging, Secondary Emerging and Frontier) considers only 12 African countries for eligibility and of these only two, South Africa and Egypt, are not classed as Frontier markets7. Of the ten African Frontier Markets only three pass on the criterion “Fair and non-prejudicial treatment of minority shareholders” which is generally taken as one of the planks of good CG.

164. This data suggests that there is scope for improvement of Corporate Governance Codes or their enforcement in Africa. Inevitably there is a level of conflict between good CG and attracting companies to listing – another area where work is required. Companies can be deterred from listing by what they see as onerous CG requirements but that is the point of Small/Medium Enterprise (SME) markets which generally have less demanding CG and free float requirements than those applying to the main list. In order to form a view about SME markets it is necessary to understand the strengths and deficiencies of the current CG requirements.

165. CG issues are not unique to Africa and have been an almost universal feature of developing markets. There are also weaknesses in developed markets. This is only partly a consequence of weak CG regulation – if market users do not understand or do not see the point of CG regulations then even the best are unlikely to be followed. This is an issue, in great part, of managerial professionalism in private companies. Attempts to alleviate this by raising professionalism have been tried in other countries notably in South East Asia where the International Finance Corporation (IFC) has sponsored and supported embryonic Institutes of Directors – successfully in Thailand, with good potential but too early to be sure of results in Vietnam and with limited impact, so far, in Myanmar.

166. In the near term, the AfDB could usefully sponsor a CG assessment of a group of African countries. This would involve assessments of existing codes with international standards – such as the Organisation of Economic Cooperation and Development (OECD) standards. IFC have also supported the ASEAN Corporate Governance Scorecard scores and ranks the ASEAN Countries. This is credited with bringing improvements or, at least, a desire for improvement.

v) Improving the environment to attract new listings

167. One of the striking facts from the basic data is the lack of companies which have listed on African exchanges. In all countries where the consultants have experience, including African countries, companies will cite many factors deterring them from seeking a listing – disclosure requirements, high professional fees, no need for more finance, onerous CG requirements etc.

168. Structural solutions have been tried elsewhere and in Africa such as setting up special SME boards for example in Kenya but these have not been very successful in attracting new companies. The problem seems to be in issues relating to areas of process and marketing.

- Process. The responses to the qualitative survey suggest that the process for listing is often complex and long. This is not uncommon in developing markets because the professional infrastructure (including merchant banks, corporate finance brokers, lawyers and accountants familiar with IPOS) is underdeveloped. In advanced markets the professional support for listing is well developed and professional firms have great experience in preparing documents in the way required by the regulator. In less developed markets the professionals (both in the support services and at the regulator) have less experience which leads to more rejections of documents and delays in processing by the regulator. This is a self-perpetuating cycle – the greater skill levels and capacity

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will only come if there are more listings, but more listings will only come if the process is improved. So how can the cycle be broken? It is possible to make a start on improving the process by using some relatively well-tried interventions. In a report prepared for the Dar-es-Salaam Stock Exchange the authors suggest improvements to the listing process and make specific recommendations which include:

- Developing a Service Level Agreement (SLA) for prospectus approval at the regulator which commits the regulator to a maximum turn-around time for reviewing and commenting on an IPO prospectus. This would not be an absolute commitment in all cases because some prospectuses are poorly drafted, and some cases are complex, but it sets a general standard which should be adhered to and is better for the applicant than complete uncertainty.

- Automating the application process using IT. Prospectus rules often insist that submissions are provided in hard copy. This slows the process, is expensive and places a storage burden on all participants. Electronic submission is not difficult and is part of standard regulator software packages.

- Standardising prospectus content by providing templates. This reduces the risk of omissions and the need to refer back to the applicant or reject the application. It simplifies the process for professional firms and improves their efficiency as well as increasing the efficiency of the regulator. The standard would require specific modifications (for example for industries such as mining) but would broadly be the same for all companies. It would also represent a building block for mutual recognition of prospectuses across different markets facilitating cross-listing which allows companies to access wider pools of capital.

AfDB could take a lead, in cooperation with African Securities Exchanges Association (ASEA), in drafting model SLAs and model prospectus templates.

- **Marketing and support.** Simply improving processes or even introducing SME markets with more relaxed requirements, while important, will not bring potential listed companies to the exchanges. To improve the flow of companies the exchanges need to:

  - study the range and types of potential listed companies in their markets i.e. the potential supply, the industries they are in, how they are financed, their governance arrangements, their views on governance, the robustness of their financial systems etc.

  - study the requirements of investors – especially institutional investors: the types and sizes of investor, what those investors most value when evaluating a company as an investment, their minimum requirements of a company in terms of disclosure and governance and if they are more willing to accept different standards from smaller, potentially high-growth companies etc.

  - identify potential listed companies possibly in cooperation with intermediaries, approach them to persuade them of the wider benefits of listing for companies which see themselves as growth companies, provide marketing material to gain initial interest (the JSE’s Speed Coaching Series and the Nairobi Stock Exchange IBUKA initiative which offers nursery, non-trading boards for potentially listed companies are African examples), and support identified potential listed companies and coach them in how to meet the requirements. Many exchanges such as Thailand have “nursery” arrangements for potential companies in order to make listing less daunting and more understandable.

169. The AfDB could usefully survey a number of exchanges to gather data on how exchanges approach these challenges – and indeed arrange study tours or similar explorations to see how listing marketing works successfully in other exchanges.

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8 DSE Product and Service Development Plans, January 2018) BTA Consulting
vi) Improving the business focus of stock exchanges

170. Evidence of the past two decades in Africa and in other regions suggests that a stronger business focus of the stock exchange has a positive impact on market development. Exchanges which are commercially-focused are more likely to:

- Introduce new products and other innovations which bring commercial benefits to the exchange but also represent developments which support the overall capital market.
- Be less influenced by non-commercial stakeholders such as central banks and government officials or by special interest groups such as stockbrokers, and more influenced by investors and issuers.

171. Globally a process of demutualisation, or otherwise converting stock exchanges to be commercial companies, has taken place. Most significant stock exchanges are now either private companies or listed companies. There are exceptions for example in Saudi Arabia – though a listing is now planned – and in Thailand where the exchange, (because of its unusual ownership structure) is not yet a private company though structural changes have made it close to one in operation and it certainly has a commercial focus in its decision making.

172. In Africa several exchanges are listed (including four of the surveyed exchanges) or operate as private companies (five of the surveyed exchanges). But the survey data showed also that two of the surveyed exchanges remain mutually owned and five are government owned. The Ethiopian exchange, when it commences operation, is planned to be majority privately owned.

173. The development of local capital markets would be enhanced if the exchanges of Africa moved towards private ownership and, ultimately, listing. But this is challenging for some exchanges where their current size could not sustain a viable business. That said, the costs of running an exchange are continually being reduced. So, on balance, stricter regulatory requirements will raise costs but this can be offset by use of increasingly standardised and therefore lower priced IT systems.

174. The potential for intervention by AfDB is somewhat limited here as exchange ownership usually concerns national policy but the AfDB could support the process by:

- Stating a conviction that private ownership of exchanges is a good and attractive option to support market development – making it a long-term objective for almost all exchanges.
- Supporting regional grouping initiatives to share costs and so improve commercial sustainability and also support less formal resource-sharing arrangements where feasible – for example sharing IT platforms where communications infrastructure is adequate.
- Setting guidelines for exchange governance. Some exchanges will probably remain in the government or mutual sector, but they should be encouraged to develop commercial company structures, for example by having properly constituted management boards. They should expand the board membership to include representatives of market users.

vii) Developing institutional investors

175. Capital markets tend to start out as predominantly retail markets with a mix of wealthy individuals, a speculative retail market with small transactions and a market for foreign investors with larger transactions. This is clearly not a sustainable long-term situation and as the market develops retail investors begin to invest for predictable life events, predominantly old age. Institutional investors develop to meet those needs through government sponsorship of pension schemes for the mass pension market. Similarly mutual funds develop for the pension market where investors want control over the investments and to meet more general savings needs.

176. Pension funds in Africa are gaining some traction and assets are increasing as set out in Table 9.
Table 9: Pension fund assets

<table>
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<tr>
<th></th>
<th>Pension fund assets as % of GDP (OECD 2020)</th>
<th>GDP 2020 USD bn</th>
<th>Est. Pension fund assets USD bn</th>
<th>Market Value domestic equity 2020 USD bn</th>
<th>Est Pension fund assets as % of equity market value</th>
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</tr>
<tr>
<td>Nigeria</td>
<td>8.0</td>
<td>432</td>
<td>34.6</td>
<td>45.9</td>
<td>75</td>
</tr>
<tr>
<td>Tanzania</td>
<td>8.3</td>
<td>62</td>
<td>5.1</td>
<td>6.9</td>
<td>75</td>
</tr>
<tr>
<td>Uganda</td>
<td>7.7</td>
<td>38</td>
<td>2.9</td>
<td>5.7</td>
<td>51</td>
</tr>
</tbody>
</table>

Source: OECD Pension reports, website research

177. However, even at their relatively low level of assets they could swamp domestic equity markets if they were to move into equities. In practice, most of the funds’ securities investment is in bonds (government or foreign) with little in equities. The explanation for this is unclear. It may be a result of restrictive mandates or regulations, or it may just be lack of investment management capacity in the pension funds. Given the length of the pension fund liabilities, bonds are not a particularly good asset allocation and in schemes where the majority of the members are younger, as is the case in Africa, the best asset allocation is a substantial weighting of equities.

178. There is less information available on mutual funds, but the expectation is for a similar situation. Where there is information, such as in Nigeria, it shows that over half of the funds are invested in money market assets and equities are less than 5% as set out in Table 10.

Table 10: Pension fund assets August 2020

<table>
<thead>
<tr>
<th>Asset type</th>
<th>Value of holding (N bn)</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity</td>
<td>544.8</td>
<td>4.8</td>
</tr>
<tr>
<td>Foreign bonds</td>
<td>6,386.5</td>
<td>56.3</td>
</tr>
<tr>
<td>Bank deposits</td>
<td>1,638.8</td>
<td>14.4</td>
</tr>
<tr>
<td>T-Bills</td>
<td>1,004.7</td>
<td>8.9</td>
</tr>
<tr>
<td>Corporate bonds</td>
<td>701.0</td>
<td>6.2</td>
</tr>
<tr>
<td>Commercial paper</td>
<td>245.2</td>
<td>2.2</td>
</tr>
<tr>
<td>Real estate</td>
<td>218.3</td>
<td>1.9</td>
</tr>
<tr>
<td>Other</td>
<td>608.8</td>
<td>5.4</td>
</tr>
<tr>
<td>Total</td>
<td>11,348.0</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: Nigeria SEC Statistical Bulletin

179. This is clearly not a good long-term situation, but the lack of detailed information restricts the possibility of making strong recommendations here. Governments should support the development of pension funds, and they do. But the prime motivation is the need to provide for populations that are increasingly likely to need retirement provision rather than because it is beneficial for the capital market.

180. The AfDB could assist African capital market development by supporting in-depth analyses of the institutional investor landscape as a first step.
Supporting greater availability of regular, reliable and consistent data

181. There is currently a shortage of good information on African capital markets. This deficiency covers a range of data types:
   - Basic statistical data – number of listed companies, value of trading etc.
   - Structural data on how the markets are organised – how the trading system works, how settlement works, how surveillance is done, who owns the exchange and other infrastructure etc.
   - Data on market users especially investors and their holdings.
   - Data on other parts of the market – venture capitalists, Private Equity (PE), mutual fund operators etc.

182. Globally, exchanges have traditionally provided data as part of their marketing. Investors and issuers considering a market will want to know current and historical information about the assets available, liquidity etc. Such information also provides value to the exchanges who can benchmark themselves against other exchanges. It also encourages academics and consultants to carry out research.

183. Some data is now available. After the drafting of this report, ASEA has again started to provide some information on its website. Other information is available on exchange/regulator websites, but it is not complete, sometimes inconsistent and is often hard to locate.

184. AfDB could benefit the capital markets by assisting in this development by:
   - Working with ASEA to collect, produce and disseminate information in addition to that newly available on the website.
   - Working with ASEA to support inter-exchange working groups to agree definitions and conduct surveys.
   - Sponsoring basic research projects to build further information beyond basic statistics into the structural data (systems, investors etc.).

Ethiopia

185. Ethiopia is on the cusp of starting a capital market. It is being well supported. The plans for developing a regulator and exchange are sound and follow best practices. When the market commences it should be an effectively structured operation.

186. Like all African markets that were studied, it may well face a shortage of tradeable assets. The development intentions include divestment of state owned entities which will give a major impetus to the market. There is also a need for a steady flow of new listings from the private sector. It is understood that there is an Over-The-Counter (OTC) type of market in existence. The AfDB could support an examination of those companies with an extension to a corporate finance demand study for other Ethiopian companies. This would give a grounding for the new exchange as to where it could look when marketing the listing product.

CONCLUSION

187. The AfDB is already very active in the capital markets space and has a number of current and past projects, most especially in the field of regional integration, which cover the majority of the recommendations presented.

188. Therefore the analyses and recommendations in this report essentially support the current interventions. The exchange rating approach suggests which markets may need the greatest improvement to become sustainable and the proposed interventions summarise the options for progress.
APPENDIX A: AFRICAN STOCK EXCHANGES QUESTIONNAIRE / QUANTITATIVE DATA QUESTIONNAIRE (SUMMARY)

Basic Metrics

1. Range of Assets Available – What assets are traded on the stock exchange? For example: equities, corporate bonds, government bonds, mutual/investment funds, REITS, financial derivatives.
2. SME Board – Does the stock exchange have a special list or board for SMEs or growth companies?
3. Number of Listed Companies – Latest end year value (indicate year) including SME Board if applicable.
4. New Companies in Last 5 Years – Total new companies over latest 5 years including SME Board.
5. Market Value of Listed Companies – Latest end year value (indicate year) including SME Board – in local currency.
6. Value of Listed Debt Instruments – Latest end of year value (indicate year) for all types of bonds.
7. Total Turnover of Equities – Latest year total traded value including SME Board if applicable – in local currency.
8. Total Turnover of Bonds – Latest year total traded value-split between government bonds, corporate bonds and other bonds if applicable – in local currency.
9. Derivative Trading – Indicate types of derivative traded (e.g. stock index options, futures etc.)
10. Other Instruments – Please indicate nature and traded value of other instruments traded such as mutual funds or REITs.
11. Number of Investors – Latest estimate of number of investors (indicate date).
12. Number of Depository Accounts – Current number of investor accounts at the securities depository.
13. Foreign Investor Involvement – If foreign investors are present in the equity market, what is their approximate share of ownership and turnover over the last 3 years?
14. Foreign Investor Involvement – If foreign investor are present in the fixed income market, what is their approximate share of turnover for Bonds and Treasury Bills over the last 3 years?

Competitive Drivers

Regulatory Quality

15. Do the securities market have a legally constituted securities regulator? For Exchange under a Securities Law.
16. Is the regulator a member of IOSCO (indicate type of member)?
17. Do the national law and/or regulations prohibit common types of market abuse such as insider trading and market manipulation?
18. Does the regulatory agency (or the exchange) have a computer system for surveillance of trading and detection of market abuse?

Settlement Infrastructure

19. Is the transfer of money and stock settled via an electronic system?
20. Are shareholders held in dematerialised form or as paper certificates?
21. Is the system Delivery versus Payment, meaning that transfer of money and stock in settlement takes place simultaneously?
22. Is there a Central Counterparty, meaning an organisation which guarantees settlement through a system of margin payments?
23. Is there a fund to compensate investors in the event of a default by a broker or other intermediary?
24. Are investors permitted to use custodian banks (meaning international banking organisations that manage investors' holdings)?

Trading

25. Does the exchange offer remote electronic display of orders or quotes?
26. Are there priority rules on the sequence in which orders are executed?
27. Are trade details published electronically after the trade?
28. Are there special facilities or rules facilities for block trades (large trades)?
29. Are real-time prices available electronically to investors and others?
30. Are broker commissions fixed or negotiable?
31. Approximate % level of average commission for retail, institutional and foreign investors.

**Intermediaries / Brokers**

32. Are intermediaries (stockbrokers etc.) required to be licensed by the regulatory agency?
33. Are intermediaries subsidiaries of banks and other Financial Institutions or independent companies or a mixture of both types?
34. Are staff and owners of intermediaries required to have qualifications specifically for the securities market?
35. What activities are licensed intermediaries allowed to conduct?
36. How is the financial strength of intermediary firms monitored by the regulator?

**Issuer Regulations and Costs**

37. Are there regulations governing the need for and content of prospectuses?
38. How is the price decided for IPO issues? For example by auctions, book-building or fixed price offers?
39. Are facilities available to underwrite IPO and other share issues?
40. How much are underwriting costs for share issues?
41. How much are regulator and exchange costs for share issues?
42. How much are legal and other professional costs for share issues?
43. Are their regulatory corporate governance requirements for listed companies?
44. Are listed companies required to report using specific accounting standards?
45. Approximately how long does it take to complete the listing process?

**Regulator and Exchange Institutional Strength**

46. How many staff does the regulator have?
47. How is the regulator funded?
48. How many staff does the stock exchange have?
49. What is the nature of ownership of the stock exchange? For example owned by members, private company or listed company.

**Access to the Market**

50. Are there exchange controls on portfolio investment outflows? Are the controls rule-based or on a case-by-case basis?
51. Are their exchange controls on portfolio investment inflows?
52. Can foreign companies be listed on the stock exchange?
53. Can domestic companies be listed on the stock exchange in a different country?
54. Are foreign-owned brokers permitted to use the market?
55. Are there restrictions on foreign-ownership of domestic companies?

**Taxation**

56. Are investment profits (capital gains) subject to income tax or capital gains tax?
57. Are dividends and bond interest subject to income tax?
58. Are stock exchange transactions subject to a transaction tax or Stamp Duty?
59. Are foreign investors subject to special taxes?
### APPENDIX B: AFRICAN STOCK EXCHANGES QUESTIONNAIRE / QUALITATIVE DATA QUESTIONNAIRE (SUMMARY)

<table>
<thead>
<tr>
<th>Type of Institution</th>
<th>Regions and countries of investment experience</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>The ratings set out below requested for each of the following regions/countries (Nigeria, Ghana and BVRM):</td>
</tr>
</tbody>
</table>

#### Factors that deter companies from listing (Important, Quite Important, Not important) and assessment of the country situation (Excellent, Acceptable, Poor) for each of the factors:

1. Lack of investors
2. Small size of market
3. High cost of process
4. High effort required to show compliance with listing requirements
5. Difficulty or slowness of listing process
6. Requirement for increased disclosure
7. Corporate governance requirements
8. Lack of awareness of marketing
9. Absence of growth market segment
10. Attractive venture capital/private equity alternative
11. Exposure to excessive market volatility
12. Lack of market liquidity
13. Fear of increased tax burden
14. Lack of underwriting facilities
15. Lack of support services – lawyers, accountants, advisors

#### Factors that attract companies to listing (Important, Quite Important, Not important), their importance and country assessment (Excellent, Acceptable, Poor):

1. Lower Cost of capital
2. Equity finance more flexible than debt finance
3. Raising corporate profile among investors and banks
4. Improving credit standing and leverage
5. Regular pricing of share
6. Specific tax advantages for listed companies
7. Opportunity to attract new, more diverse board members

#### Factors affecting attractiveness of stock exchange for investors (Important, Quite Important, Not important) their importance and country assessment (Excellent, Acceptable, Poor):

1. Attractiveness of growth prospects of country
2. Availability of attractive corporate investments
3. Quality and timeliness of corporate disclosures
4. Market abuse, regulation and enforcement
5. Standards of corporate governance and enforcement
6. Exchange controls and other restrictions on cross-border transfers
7. Reliability and timeliness of settlement
8. Availability of custodians for international investors
9. Cost of settlement
10. Liquidity of secondary market
11. Accessibility and fairness of trading system
12. Cost of trading – system and commissions
13. Quality of skills in brokerage firms
14. Levels of transaction taxes
15. Taxes on dividends and interest
16. Taxes on capital gains
17. Tax treatment of foreign investors
APPENDIX C: RESULTS OF QUANTITATIVE SURVEY – 17 EXCHANGES

1. This section reports on the findings in the quantitative survey. The results cover 11 exchanges in the terms of Reference (TOR) and the 6 additional exchanges which supplied data. For each topic the summary results are tabulated followed by a discussion of key findings. Generally, the results in the tables have been coloured to highlight good features (green) and weak features (red) plus some midway features (yellow).

**Assets Traded**

Table C1: Assets Traded

| Asset Type                  | Angola | Botswana | BRVM | BVMAC | Cape Verde | Egypt | Ghana | Kenya | Malawi | Mauritius | Nigeria | Rwanda | Sudan | Tanzania | Tunisia | Uganda | Zambia | No. |
|-----------------------------|--------|----------|------|-------|------------|-------|-------|-------|--------|-----------|---------|--------|--------|----------|---------|--------|--------|-----|-----|
| Equities                    | ✓      | ✓        | ✓    | ✓     | ✓          | ✓     | ✓     | ✓     | ✓      | ✓         | ✓       | ✓      | ✓      | ✓        | ✓       | ✓      | ✓      | 16  |
| ETFs                        | ✓      | ✓        | ✓    | ✓     | ✓          | ✓     | ✓     | ✓     | ✓      | ✓         | ✓       | ✓      | ✓      | ✓        | ✓       | ✓      | ✓      | 6   |
| CIS                         | ✓      | ✓        | ✓    | ✓     | ✓          | ✓     | ✓     | ✓     | ✓      | ✓         | ✓       | ✓      | ✓      | ✓        | ✓       | ✓      | ✓      | 7   |
| REITs                       | ✓      | ✓        | ✓    | ✓     | ✓          | ✓     | ✓     | ✓     | ✓      | ✓         | ✓       | ✓      | ✓      | ✓        | ✓       | ✓      | ✓      | 3   |
| Preference Shares           | ✓      | ✓        | ✓    | ✓     | ✓          | ✓     | ✓     | ✓     | ✓      | ✓         | ✓       | ✓      | ✓      | ✓        | ✓       | ✓      | ✓      | 1   |
| Depository Receipts         | ✓      | ✓        | ✓    | ✓     | ✓          | ✓     | ✓     | ✓     | ✓      | ✓         | ✓       | ✓      | ✓      | ✓        | ✓       | ✓      | ✓      | 2   |
| Treasury Bills              | ✓      | ✓        | ✓    | ✓     | ✓          | ✓     | ✓     | ✓     | ✓      | ✓         | ✓       | ✓      | ✓      | ✓        | ✓       | ✓      | ✓      | 3   |
| Government Bonds            | ✓      | ✓        | ✓    | ✓     | ✓          | ✓     | ✓     | ✓     | ✓      | ✓         | ✓       | ✓      | ✓      | ✓        | ✓       | ✓      | ✓      | 14  |
| Muni/State Bonds            | ✓      | ✓        | ✓    | ✓     | ✓          | ✓     | ✓     | ✓     | ✓      | ✓         | ✓       | ✓      | ✓      | ✓        | ✓       | ✓      | ✓      | 2   |
| Supranational Bonds         | ✓      | ✓        | ✓    | ✓     | ✓          | ✓     | ✓     | ✓     | ✓      | ✓         | ✓       | ✓      | ✓      | ✓        | ✓       | ✓      | ✓      | 1   |
| USD Govt. Bonds             | ✓      | ✓        | ✓    | ✓     | ✓          | ✓     | ✓     | ✓     | ✓      | ✓         | ✓       | ✓      | ✓      | ✓        | ✓       | ✓      | ✓      | 1   |
| Corporate Bonds             | ✓      | ✓        | ✓    | ✓     | ✓          | ✓     | ✓     | ✓     | ✓      | ✓         | ✓       | ✓      | ✓      | ✓        | ✓       | ✓      | ✓      | 16  |
| Structured Products         | ✓      | ✓        | ✓    | ✓     | ✓          | ✓     | ✓     | ✓     | ✓      | ✓         | ✓       | ✓      | ✓      | ✓        | ✓       | ✓      | ✓      | 1   |
| Green Bonds                 | ✓      | ✓        | ✓    | ✓     | ✓          | ✓     | ✓     | ✓     | ✓      | ✓         | ✓       | ✓      | ✓      | ✓        | ✓       | ✓      | ✓      | 1   |
| Sukuk                       | ✓      | ✓        | ✓    | ✓     | ✓          | ✓     | ✓     | ✓     | ✓      | ✓         | ✓       | ✓      | ✓      | ✓        | ✓       | ✓      | ✓      | 3   |
| Financial Derivatives       | ✓      | ✓        | ✓    | ✓     | ✓          | ✓     | ✓     | ✓     | ✓      | ✓         | ✓       | ✓      | ✓      | ✓        | ✓       | ✓      | ✓      | 1   |
| **Number of asset types traded** | 5     | 5        | 4    | 3     | 5          | 7     | 6     | 6     | 3      | 8         | 9       | 3      | 3      | 3        | 3       | 3      | 3      | 2   |
| SME Board                   | N      | Y        | Y    | Y     | N          | Y     | Y     | Y     | Y      | Y         | Y       | N      | Y      | Y        | Y       | Y      | Y      | 78  |

ETFs = Exchange-Traded Funds
CIS = Collective Investment Schemes (mutual funds and investment funds)
REITs = Real-Estate Investment Trusts
Key Observations from Survey Results

2. The exchanges covered by the quantitative survey reported that they traded a wide range of assets covering equity and equity-related shares, bonds, sukuk and derivatives.

3. All but one of the exchanges trade equities which are the main product line, as they are globally for stock exchanges. The exception was Angola where only bonds are listed and traded. Most exchanges have set up a special SME board to cater for the needs of smaller companies.

4. All exchanges reported that they traded government bonds (Sudan trades them in sukuk form rather than conventional bonds). Many exchanges globally are the point for listing of government bonds and may offer some trading facilities, but in most cases, there is little, if any, on-exchange trading. The transactions are negotiated privately and may be reported through the exchange’s trading system, but price discovery (and usually settlement) is done elsewhere. Therefore, the economic and commercial benefit for the exchange is limited.

5. The same is frequently true of corporate bonds which 14 of the 17 exchanges trade. They are listed on the exchange, but most trading takes place through off-exchange negotiation. The exchange has a bigger regulatory role than with government bonds but a similarly limited trading role.

6. Beyond these staples, exchanges offer a range of equity-related products mostly collective investment funds and specialised collective investments – Exchange Traded Funds (ETFs) and Real Estate Investment Trusts (REITs).

7. Only one exchange, Nairobi, offers derivative trading which requires sophisticated investors, regulation and systems but which has been a growth business for exchanges elsewhere.

8. The larger and more developed exchanges offer the widest range of products – upwards of six in four cases. A wide range of products reflects the higher level of sophistication of the market users and so is a measure of the development of the market. While the introduction of new products can distract from mainstream development, it does indicate a level of innovativeness and willingness to take development risks both at the exchange and at the regulator.

Regulation

Table C2: Regulation

<table>
<thead>
<tr>
<th></th>
<th>Angola</th>
<th>Botswana</th>
<th>BRVM</th>
<th>BVMAC</th>
<th>Cape Verde</th>
<th>Egypt</th>
<th>Ghana</th>
<th>Kenya</th>
<th>Malawi</th>
<th>Mauritius</th>
<th>Nigeria</th>
<th>Rwanda</th>
<th>Sudan</th>
<th>Tanzania</th>
<th>Tunisia</th>
<th>Uganda</th>
<th>Zambia</th>
</tr>
</thead>
<tbody>
<tr>
<td>Does the securities market have a legally constituted securities regulator?</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Is the regulator a member of IOSCO?</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
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<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Do the national laws and/or regulations prohibit common types of market abuse such as insider trading and market manipulation?</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
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<td>Y</td>
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<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
</tbody>
</table>

9 As at mid 2022 equity IPOs are commencing.
Key Observations from Survey Results

9. All responding exchanges showed that they have successfully developed the essential regulatory structures:

- All have legally constituted national regulators.
- All have managed to achieve International Organization of Securities Commissions (IOSCO) membership. IOSCO membership shows that the regulator has been through a process of assessment and been adjudged to comply sufficiently with IOSCO principles for regulators, in particular:
  - Having clarity of its role and responsibilities.
  - Having adequate powers to inspect, monitor and enforce.
  - Having adequate operational independence.
  - Having the power to work with and share information with other domestic and foreign regulators.
- All have legal prohibitions on a range of types of market abuse particularly insider trading and market manipulation. These provisions are important in encouraging investor confidence in the fairness of the market, particularly so for retail investor participants.
- However, legal provisions have limited impact without detection capabilities. This role may fall to either the regulator or the exchange depending upon the chosen regulatory model, but it is vital that they have to right tools for detection. Most of the responding markets had computerised systems to carry out surveillance for possible market abuse (either at the exchange or at the regulator). Of the markets surveyed, 14 had some type of electronic system for surveillance (at the exchange or at the regulator or both) and only three did not have some form of surveillance system.

Settlement System

Table C3: Settlement System

<table>
<thead>
<tr>
<th>Angola</th>
<th>Botswana</th>
<th>BRVM</th>
<th>Cap Verde</th>
<th>Egypt</th>
<th>Ghana</th>
<th>Kenya</th>
<th>Malawi</th>
<th>Mauritius</th>
<th>Nigeria</th>
<th>Rwanda</th>
<th>Sudan</th>
<th>Tanzania</th>
<th>Tunisia</th>
<th>Uganda</th>
<th>Zambia</th>
</tr>
</thead>
<tbody>
<tr>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
</tbody>
</table>

Is the transfer of money and stock settled via an electronic system?

<table>
<thead>
<tr>
<th>Angola</th>
<th>Botswana</th>
<th>BRVM</th>
<th>Cap Verde</th>
<th>Egypt</th>
<th>Ghana</th>
<th>Kenya</th>
<th>Malawi</th>
<th>Mauritius</th>
<th>Nigeria</th>
<th>Rwanda</th>
<th>Sudan</th>
<th>Tanzania</th>
<th>Tunisia</th>
<th>Uganda</th>
<th>Zambia</th>
</tr>
</thead>
<tbody>
<tr>
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<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
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<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
</tbody>
</table>

Are shareholdings held in dematerialized form or as paper certificates?

<table>
<thead>
<tr>
<th>Angola</th>
<th>Botswana</th>
<th>BRVM</th>
<th>Cap Verde</th>
<th>Egypt</th>
<th>Ghana</th>
<th>Kenya</th>
<th>Malawi</th>
<th>Mauritius</th>
<th>Nigeria</th>
<th>Rwanda</th>
<th>Sudan</th>
<th>Tanzania</th>
<th>Tunisia</th>
<th>Uganda</th>
<th>Zambia</th>
</tr>
</thead>
<tbody>
<tr>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
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<td>N</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
</tbody>
</table>

Is the system Delivery versus Payment?

<table>
<thead>
<tr>
<th>Angola</th>
<th>Botswana</th>
<th>BRVM</th>
<th>Cap Verde</th>
<th>Egypt</th>
<th>Ghana</th>
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<th>Nigeria</th>
<th>Rwanda</th>
<th>Sudan</th>
<th>Tanzania</th>
<th>Tunisia</th>
<th>Uganda</th>
<th>Zambia</th>
</tr>
</thead>
<tbody>
<tr>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
</tbody>
</table>

Is there a Central Counterparty?

<table>
<thead>
<tr>
<th>Angola</th>
<th>Botswana</th>
<th>BRVM</th>
<th>Cap Verde</th>
<th>Egypt</th>
<th>Ghana</th>
<th>Kenya</th>
<th>Malawi</th>
<th>Mauritius</th>
<th>Nigeria</th>
<th>Rwanda</th>
<th>Sudan</th>
<th>Tanzania</th>
<th>Tunisia</th>
<th>Uganda</th>
<th>Zambia</th>
</tr>
</thead>
<tbody>
<tr>
<td>N</td>
<td>N</td>
<td>(Y)</td>
<td>(N)</td>
<td>(Y)</td>
<td>(Y)</td>
<td>(Y)</td>
<td>(Y)</td>
<td>(Y)</td>
<td>(N)</td>
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<td>(Y)</td>
<td>(Y)</td>
<td>(Y)</td>
<td>(Y)</td>
<td>(Y)</td>
</tr>
</tbody>
</table>
Is there a fund to compensate investors in the event of a default?  

<table>
<thead>
<tr>
<th>Country</th>
<th>Angola</th>
<th>Botswana</th>
<th>BRVM</th>
<th>BVMA C</th>
<th>Cape Verde</th>
<th>Egypt</th>
<th>Ghana</th>
<th>Kenya</th>
<th>Malawi</th>
<th>Mauritius</th>
<th>Nigeria</th>
<th>Rwanda</th>
<th>Sudan</th>
<th>Tanzania</th>
<th>Tunisia</th>
<th>Uganda</th>
<th>Zambia</th>
</tr>
</thead>
<tbody>
<tr>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
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<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
</tbody>
</table>

Are investors permitted to use custodian banks?  

<table>
<thead>
<tr>
<th>Country</th>
<th>Angola</th>
<th>Botswana</th>
<th>BRVM</th>
<th>BVMA C</th>
<th>Cape Verde</th>
<th>Egypt</th>
<th>Ghana</th>
<th>Kenya</th>
<th>Malawi</th>
<th>Mauritius</th>
<th>Nigeria</th>
<th>Rwanda</th>
<th>Sudan</th>
<th>Tanzania</th>
<th>Tunisia</th>
<th>Uganda</th>
<th>Zambia</th>
</tr>
</thead>
<tbody>
<tr>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
</tbody>
</table>

Note: (Y) indicates the question may have been mis-interpreted.

**Key Observations from Survey Results**

10. The responding markets all indicate that they have modern settlement systems:
   - All have electronic transfers of stock and cash
   - Almost all have stock held in dematerialised form in a central depository
   - All offer Delivery versus Payment (DvP) meaning that stock and cash are exchanged simultaneously in the settlement process.

11. African markets are all either relatively new and so have moved directly to electronic, dematerialised systems or have been able to upgrade from traditional certificate-based systems. All these innovations will have required extensive legal reform to enable electronic transfers etc. as well as appropriate IT systems.

12. Nigeria has moved to a Central Counterparty System (CCP) where a central entity is designated as the counterparty to every transaction and takes margin payments from participants to reduce the risk of loss from default. These are essential for derivative markets and globally are also becoming the norm in cash markets. The table indicates those that gave a positive response in the survey.

13. All of the markets have, or soon will have, funds to compensate investors for losses incurred from settlement failures. Generally, these funds have to build up over time and in the early stages are only adequate to protect small investors – but it is essential to make a start on developing compensation funds.

14. Custodian banks are important for foreign investors who use global custodians to manage their securities assets across their range of investments in different countries. Without these it is unlikely that foreign investors will become significant participants. Almost all the surveyed markets had the infrastructure to support custodian banks. Permission for custodians generally requires regulatory changes.

**Trading System**

**Table C4: Trading System**

<table>
<thead>
<tr>
<th>Country</th>
<th>Angola</th>
<th>Botswana</th>
<th>BRVM</th>
<th>BVMA C</th>
<th>Cape Verde</th>
<th>Egypt</th>
<th>Ghana</th>
<th>Kenya</th>
<th>Malawi</th>
<th>Mauritius</th>
<th>Nigeria</th>
<th>Rwanda</th>
<th>Sudan</th>
<th>Tanzania</th>
<th>Tunisia</th>
<th>Uganda</th>
<th>Zambia</th>
</tr>
</thead>
<tbody>
<tr>
<td>Does the exchange offer remote electronic display of orders or quotes?</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>N*</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Are there priority rules on the sequence in which orders are executed?</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
</tbody>
</table>

*Kenya does not have a CCP. Derivative clearing is managed by settlement banks.*
**Key Observations from Survey Results**

15. Trading systems are a key product offering of stock exchanges. Historically there has been considerable diversity in the method of trading but trading has now been standardised and there is a wide range of software packages offering standard order-exposure trading. As with settlement systems the responding markets in the survey have, or are about to acquire, modern trading systems. All of them offer:

- Remote display of orders
- Price/time priority rules
- Post trade publication of transaction information
- Real-time information for market users.

16. Most offer special arrangements for block (large) trades which benefit larger investors in illiquid markets – domestic institutions if they exist and foreign investors.

### Intermediaries

**Table C5: Intermediaries**

| Angola | Botswana | BRVM | BVMAC | Cape Verde | Egypt | Ghana | Kenya | Malawi | Mauritius | Nigeria | Rwanda | Sudan | Tanzania | Tunisia | Uganda | Zambia |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Are intermediaries (stockbrokers etc.) required to be licensed by the regulatory agency? | Y | Y | Y | Y | Y | Y | Y | Y | Y | Y | Y | Y | Y | Y | Y |
| Are intermediaries subsidiaries of banks and other financial institutions (S) or independent companies (I) or a mixture of both types (M)? | I | M | M | M | M | I | M | M | M | M | M | M | M | M | M |
### Key Observations from Survey Results

17. The regulation, structure and capacity of intermediaries are important factors in capital market development. The key points from the survey are:

- **All regulators exercise the authority for licensing stockbroking intermediaries. Without such a license it is not legal to offer stockbroking services.**

- **Stockbrokers can be independent operators or subsidiaries of other financial institutions, particularly banks. Historically there has been a regulatory preference for independent brokers but this is no longer the regulatory philosophy in most markets and brokers are permitted, sometimes encouraged, to be linked to other financial institutions. As subsidiaries, brokers are likely to have greater capital resources, be generally better staffed and to have opportunities to sell a wider range of services. Most of the respondents to the survey permit a mixture of independents and subsidiaries.**

- **Linked to this is the scope of stockbroking firms. In traditional markets brokers were confined to a limited range of activities – essentially collecting and executing client orders. This has generally been extended to allow brokers to offer advice and research, but they may not be permitted to engage in other activities such as fund management and corporate finance. Foreign investors are more likely to prefer stockbrokers with a wide range of activities or full-service brokers.**

- **The level of skill of individual staff members in stockbroker firms is crucial to the development of the market. Brokers have an important role in guiding less sophisticated investors and, if allowed by their business scope, to advise on a wide range of complex capital market activities. Globally most markets require staff and principals of brokers to have specific capital market qualifications (in addition to requirements for general standards of education) and many have teamed up with international training institutes to provide training and manage examinations. Most respondents to the survey had such requirements.**

- **Broker commissions were traditionally set by regulators, but the trend is now to allow negotiated commissions to stimulate competition and innovation though possibly with some scales and**

#### Table: Activity Permission and Commission Rates

<table>
<thead>
<tr>
<th>Country</th>
<th>Activity Permission</th>
<th>Commission Type</th>
</tr>
</thead>
<tbody>
<tr>
<td>Angola</td>
<td>N</td>
<td>F</td>
</tr>
<tr>
<td>Botswana</td>
<td>F</td>
<td>N</td>
</tr>
<tr>
<td>BVMAC</td>
<td>W</td>
<td>F</td>
</tr>
<tr>
<td>Cape Verde</td>
<td>N</td>
<td>F</td>
</tr>
<tr>
<td>Egypt</td>
<td>F</td>
<td>F</td>
</tr>
<tr>
<td>Ghana</td>
<td>N</td>
<td>F</td>
</tr>
<tr>
<td>Kenya</td>
<td>N</td>
<td>N</td>
</tr>
<tr>
<td>Malawi</td>
<td>N</td>
<td>N</td>
</tr>
<tr>
<td>Mauritius</td>
<td>N</td>
<td>N</td>
</tr>
<tr>
<td>Nigeria</td>
<td>F</td>
<td>W</td>
</tr>
<tr>
<td>Rwanda</td>
<td>N</td>
<td>W</td>
</tr>
<tr>
<td>Sudan</td>
<td>F</td>
<td>N</td>
</tr>
<tr>
<td>Tanzania</td>
<td>F</td>
<td>N</td>
</tr>
<tr>
<td>Tunisia</td>
<td>F</td>
<td>W</td>
</tr>
<tr>
<td>Uganda</td>
<td>N</td>
<td>N</td>
</tr>
<tr>
<td>Zambia</td>
<td>W</td>
<td>N</td>
</tr>
</tbody>
</table>

- Narrow range (N) = trading, research and advice
- Wide range (W) = trading, advice and corporate finance
- Full service = trading, advice, corporate finance, fund management
protection for retail investor charges. The split among the respondents was roughly 50/50 between fixed and negotiated. However, data on transaction costs presented in Table C1 show that some of the markets where commissions are negotiated have high average rates of commissions.

Issuers

Table C6: Issuers

<table>
<thead>
<tr>
<th></th>
<th>Angola</th>
<th>Botswana</th>
<th>BRVM</th>
<th>BVMAC</th>
<th>Cape Verde</th>
<th>Egypt</th>
<th>Ghana</th>
<th>Kenya</th>
<th>Malawi</th>
<th>Mauritius</th>
<th>Nigeria</th>
<th>Rwanda</th>
<th>Sudan</th>
<th>Tanzania</th>
<th>Tansia</th>
<th>Uganda</th>
<th>Zambia</th>
</tr>
</thead>
<tbody>
<tr>
<td>Are there regulations governing the need for and content of prospectuses?</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td></td>
<td></td>
</tr>
<tr>
<td>How is the price decided for IPO issues? Auctions (A), book-building (B), fixed price offers (F), Mixture (M)?</td>
<td>M</td>
<td>M</td>
<td>F</td>
<td>F</td>
<td>M</td>
<td>M</td>
<td>B</td>
<td>F</td>
<td>M</td>
<td>B</td>
<td>F</td>
<td>F</td>
<td>B</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Are facilities available to underwrite IPOs and other share issues?</td>
<td>Y</td>
<td>Y</td>
<td>Y**</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Are their regulatory corporate governance requirements for listed companies?</td>
<td>Y</td>
<td>Y</td>
<td>N*</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Are listed companies required to report using specific accounting standards?</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Approximately how long does it take to complete the listing process (in months): &lt;=1 months, 1-2 months, over 2 months?</td>
<td>&lt;=1</td>
<td>&gt;2</td>
<td>1-2</td>
<td>&gt;2</td>
<td>&gt;2</td>
<td>1-2</td>
<td>&lt;=1</td>
<td>&gt;2</td>
<td>&gt;2</td>
<td>&gt;2</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>* = In progress</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>** = Syndication</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
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<td></td>
</tr>
</tbody>
</table>

Key Observations from Survey Results

18. The markets surveyed have all adopted the fundamental building blocks of issuer regulation:

- All require issuers to produce a prospectus and the rules set requirements for the prospectus contents. The required disclosures are a challenge for many companies in developing markets, so it is likely that compliance is variable but the basic building blocks and the basic principle of the need to inform investors are well established.

- Almost all have or are setting up codes of corporate governance. Corporate governance codes tend to cover similar ground, have the same aims and impose similar requirements. Again, compliance is challenging but the basics are in place. In some countries, for example the BRVM market, donors
are working with local regulators and companies to improve the professionalism of managers and appreciation of the importance of corporate governance.

- Almost all require companies to report using standardised and internationally acceptable accounting standards. Most seem to require some version of International Financial Reporting Standards (IFRS). As noted elsewhere, the standards may not be as strictly and robustly applied in the less developed markets, but the principle is established.

19. Procedures and support for IPOs are established, though the number of IPOs is very low. There are adequate systems for pricing new shares though book-building and more sophisticated techniques for price determination, and for managing the risk through underwriting or syndication.

20. The most negative feature aside from, but probably contributing to, the low number of IPOs is the relatively slow pace of IPO processing leading to a long timeline for approval. Potential companies will often cite the slowness of IPOs (compared to bank loans for example) as a reason not to list. Therefore, it is important that systems are as streamlined as possible to reduce excessive referrals and expedite the process.

Regulatory and Development Capacity

Table C7: Regulatory and Development Capacity

<table>
<thead>
<tr>
<th>Table C7: Regulatory and Development Capacity</th>
</tr>
</thead>
<tbody>
<tr>
<td>Angola</td>
</tr>
<tr>
<td>How many staff does the regulator have?</td>
</tr>
<tr>
<td>How is the regulator funded (M=Market, G=Government)?</td>
</tr>
<tr>
<td>How many staff does the stock exchange have?</td>
</tr>
<tr>
<td>What is the nature of ownership of the stock exchange (G=Government, M=Member-owned, P=Private company, L=Listed company)?</td>
</tr>
</tbody>
</table>

*Listing in progress

Key Observations from Survey Results

21. Staffing levels of regulators reflect the size and development level of the market as would be expected. However, an effective regulator needs to have a range of skills and be able to carry out a variety of
activities which can prove difficult with a staff below 30. Staffing of stock exchanges also reflects the size and scope of the market.

22. Most of the regulators are self-financing, producing revenue for charges on market users. This is the preferred way as it frees the regulator from the limitations and challenges associated with central government budgets and reinforces the independence of the regulator. It also allows the regulator to draw itself away from government employee pay scales which are usually not appropriate for attracting the necessary quality of employee in an industry where salaries are generally above those of government employees. IOSCO’s assessments show a preference for self-funding regulators while recognising that early stage markets will not be able to sustain a regulator from market payments alone and will require government assistance.

23. Stock exchange ownership is an important determinant of market development. The traditional models of member owned or government owned have lost favour and exchanges are increasingly operated as private companies or, for the most developed, as listed companies. Private stock exchanges are better able to resist the conflicts of interest that arise with member and government owned exchanges. However, in early stage markets the stock exchange may not be commercially viable without government (or other) assistance. Of the 17 exchanges, four have become listed companies and six are private companies.

Accessibility

### Table C8: Accessibility

<table>
<thead>
<tr>
<th></th>
<th>Angola</th>
<th>Botswana</th>
<th>BVMAC</th>
<th>BRVM</th>
<th>Cape Verde</th>
<th>Egypt</th>
<th>Ghana</th>
<th>Kenya</th>
<th>Malawi</th>
<th>Mauritius</th>
<th>Nigeria</th>
<th>Rwanda</th>
<th>Sudan</th>
<th>Tanzania</th>
<th>Tunisia</th>
<th>Uganda</th>
<th>Zambia</th>
</tr>
</thead>
<tbody>
<tr>
<td>Are there exchange controls on portfolio investment outflows?</td>
<td>N</td>
<td>R</td>
<td>R</td>
<td>N</td>
<td>N</td>
<td>R</td>
<td>N</td>
<td>R</td>
<td>N</td>
<td>N</td>
<td>C</td>
<td>R</td>
<td>R</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td></td>
</tr>
<tr>
<td>(N= No controls, R= Rule-based controls, C=Case-by-case controls)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Are there exchange controls on portfolio investment inflows?</td>
<td>N</td>
<td>N</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>Y</td>
<td>N</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>Y</td>
<td>Y</td>
<td></td>
</tr>
<tr>
<td>Can foreign companies be listed on the stock exchange?</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td></td>
</tr>
<tr>
<td>Can domestic companies be listed on the stock exchange in a different country?</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td></td>
</tr>
<tr>
<td>Are foreign-owned brokers permitted to use the market?</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>Y</td>
<td>N</td>
<td>Y</td>
<td>N</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td></td>
</tr>
<tr>
<td>Are there restrictions on foreign ownership of domestic companies?</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td></td>
</tr>
</tbody>
</table>

### Key Observations from Survey Results

24. Openness to the rest of the world is a valuable driver of domestic capital market development. Access to other markets for domestic participants (investors, issuers and intermediaries) provides a competitive stimulus and allowing foreign participants to access the domestic market is an effective way to drive up standards and innovation. At the same time, relatively fragile economies will need to protect themselves against the full rigours of international capital flows. If restrictions are necessary, then their deterrent
effect on foreign investors and other participants can be mitigated to some extent by having clear rules and processes.

25. The results of the survey suggest that African capital markets have generally become more open to the world over the past decade or so. Twelve of the countries covered report having no restrictions on portfolio investment outflows with seven having no restrictions and five having restrictions but using rule-based processes rather than case-by-case, and therefore less predictable, application of the rules.

26. Almost all of the countries surveyed allow foreign companies to list on the domestic market and allow domestic companies to list in foreign markets. General ownership restrictions are now rare and where they do exist, they apply only to highly sensitive industries. Nine countries do not prohibit foreign brokers from operating in their markets though for regulatory reasons they will require a domestic presence as is common in all markets.

**Taxation**

**Table C9: Taxation**

<table>
<thead>
<tr>
<th></th>
<th>Angola</th>
<th>Botswana</th>
<th>BRVM</th>
<th>BVMAC</th>
<th>Cape Verde</th>
<th>Egypt</th>
<th>Ghana</th>
<th>Kenya</th>
<th>Malawi</th>
<th>Mauritius</th>
<th>Nigeria</th>
<th>Rwanda</th>
<th>Sudan</th>
<th>Tanzania</th>
<th>Tunisia</th>
<th>Uganda</th>
<th>Zambia</th>
</tr>
</thead>
<tbody>
<tr>
<td>Are investment profits (capital gains) subject to income tax or capital gains tax?</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>Y*</td>
<td>N*</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>Y</td>
<td>N</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Are dividends and bond interest subject to income tax?</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y*</td>
<td>Y**</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>Y</td>
<td>Y</td>
<td>Y*</td>
<td>Y*</td>
<td>Y*</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Are stock exchange transactions subject to a transaction tax or Stamp Duty?</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>Y</td>
<td>N</td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>Y</td>
<td>N</td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Y* = Bonds yes, equity no

Y** = Bonds no, equity yes

N*=planned 2023

27. Taxation is an important determinant of investor behaviour. The issue is not only whether taxes are levied on investment income, which seems reasonable on grounds of fairness, but also because of the possibility of inadvertently biasing investment decisions. The details of taxation are beyond the scope of this study but there are some important differences across the respondent countries:

- Most countries do not subject capital gains to any kind of taxation. This can be seen as encouraging the market, but it can also be seen as encouraging a speculative element and being unfair as a significant part of investment income is untaxed. A perception of fairness is important if there is to be popular consensus in support of capital market development.

- Most countries do tax income from dividends and from bond interest though some exempt some types of income.

- Transaction taxes are widely regarded as bad for capital market development as they increase the costs of transaction business and so damage market liquidity. At the same time, they are easy to levy and collect which makes them attractive to impoverished governments. About half of the respondent companies have some form of transaction tax. These differences might deter foreign
investors when choosing between a country with transaction taxes and one without but the sense of the consultants, based on experience of many markets, is that within reason transaction taxes are not much of a deterrent.

Investors

28. In the survey, markets were asked to indicate the number of investors and depository accounts. The data collected was not sufficiently consistent to draw conclusions about domestic investors though some insights into the importance of foreign investors were contributed.

Foreign Investors

29. Foreign investment percentages, as submitted by the exchanges, are shown in Table E10. The level varies from less than 1% to a maximum of 85%. The largest markets have significant percentages of foreign holdings of equities – 65% for Kenya for example, and some of the smaller markets (notably Tanzania and Uganda) have dominant levels of foreign holdings. Applying the foreign ownership percentages to the 2020 total equity market value figures (column 4) gives an estimate of the USD value of foreign holdings. Across the 11 respondents, foreign investment represents 36% of total market value. Egypt, Kenya and Nigeria collectively represent 70% of the foreign investor total.

Table C10: Foreign Investment Percentage

<table>
<thead>
<tr>
<th></th>
<th>% Foreign investor ownership</th>
<th>Market value 2020 USD</th>
<th>Foreign ownership 2020 USD (est.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>BRVM</td>
<td>12.0</td>
<td>8,100</td>
<td>972</td>
</tr>
<tr>
<td>Cape Verde</td>
<td>0.8</td>
<td>897</td>
<td>7</td>
</tr>
<tr>
<td>Egypt</td>
<td>21.0</td>
<td>41,377</td>
<td>8,689</td>
</tr>
<tr>
<td>Ghana</td>
<td>49.0</td>
<td>9,279</td>
<td>4,547</td>
</tr>
<tr>
<td>Kenya</td>
<td>65.0</td>
<td>21,438</td>
<td>13,935</td>
</tr>
<tr>
<td>Mauritius</td>
<td>15.0</td>
<td>8,872</td>
<td>1,331</td>
</tr>
<tr>
<td>Nigeria</td>
<td>40.0</td>
<td>45,881</td>
<td>18,353</td>
</tr>
<tr>
<td>Rwanda</td>
<td>3.0</td>
<td>3,526</td>
<td>106</td>
</tr>
<tr>
<td>Tanzania</td>
<td>80.0</td>
<td>6,900</td>
<td>5,520</td>
</tr>
<tr>
<td>Tunisia</td>
<td>0.5</td>
<td>8,587</td>
<td>43</td>
</tr>
<tr>
<td>Uganda</td>
<td>85.0</td>
<td>5,700</td>
<td>4,845</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>160,558</strong></td>
<td><strong>58,347</strong></td>
<td></td>
</tr>
</tbody>
</table>

30. Indications from the two exchanges which also gave turnover suggest that foreign investors are considerably more active traders than domestic investors. This is consistent with findings in regions outside Africa.

Domestic Investors

31. As noted, information about domestic investors was scarce though the little that was submitted suggested that retail investors are the most significant domestic investors – Kenya reported some two million depository accounts and Tanzania reported 550,000. Again, this is consistent with other developing markets where institutional investment has yet to become significant.

32. That said, there are indications that other potential investor types are emerging. Domestic pension funds, in particular, are becoming increasingly significant investors. Table C11 shows the percentage of GDP represented by pension fund assets in a selection of countries covered by the OECD pension fund.
reports. These range from a high of 47.2% in Botswana to a low of 1.5% in Egypt. The average of the percentages is 13.2% which is relatively normal for developing countries, higher than India (9.3%) but considerably lower than Brazil (28.2%). Weighting the average by GDP gives a substantially lower figure of 6.9% because of the relatively low pension assets to GDP ratio of the two largest economies, Egypt and Nigeria.

### Table C11: Pension fund assets

<table>
<thead>
<tr>
<th>Country</th>
<th>Pension fund assets as % of GDP 2020</th>
<th>GDP USD bn 2020</th>
<th>Est. fund USD bn</th>
<th>Pension assets</th>
<th>Market domestic equity USD bn</th>
<th>Value 2020</th>
<th>Est Pension fund assets as % of equity market value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Botswana</td>
<td>47.2</td>
<td>15</td>
<td>7.1</td>
<td>3.3</td>
<td>214</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Egypt</td>
<td>1.5</td>
<td>365</td>
<td>5.5</td>
<td>41.4</td>
<td>13</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ghana</td>
<td>5.7</td>
<td>69</td>
<td>3.9</td>
<td>9.3</td>
<td>42</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kenya</td>
<td>13.3</td>
<td>101</td>
<td>13.4</td>
<td>21.4</td>
<td>63</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Malawi</td>
<td>16.4</td>
<td>12</td>
<td>2.0</td>
<td>2.3</td>
<td>86</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mauritius</td>
<td>11.1</td>
<td>11</td>
<td>1.2</td>
<td>8.9</td>
<td>14</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nigeria</td>
<td>8.0</td>
<td>432</td>
<td>34.6</td>
<td>45.9</td>
<td>75</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tanzania</td>
<td>8.3</td>
<td>62</td>
<td>5.1</td>
<td>6.9</td>
<td>75</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Uganda</td>
<td>7.7</td>
<td>38</td>
<td>2.9</td>
<td>5.7</td>
<td>51</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>75.7</td>
<td>145.0</td>
<td>52</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

33. Even given the relatively low weighted average of pension assets, the current funds are facing a challenge to invest the money domestically. Most funds are heavily biased towards debt investment which for countries with young populations is not prudent as a result of asset/liability mismatch. Kenya, for example, invests 46% of its pension fund assets in bonds and only 16% in equity despite Kenya having one of the continent’s most developed equity markets. If they were to shift towards equity investment, they would rapidly run up against a constraint of too few assets. As Table C11 shows, the assets in Kenya’s pension funds are equivalent to 63% of the total equity market value of the Nairobi Securities Exchange – and foreign investors already hold 65% of the total market value. A similar situation exists in Uganda where the National Social Security Fund already owns a third of the free float of shares listed on the Uganda Securities Exchange. The situation is even more extreme in Botswana where pension assets are over 3200% of the listed equity on the Botswana Stock exchange.

### Cost of Trading

34. Total transaction costs are an important factor affecting the decisions of investors. High transaction costs reduce the potential for gain from investment strategies. Transaction costs are closely linked to liquidity which reflects the ease with which investors can open and close securities positions. In illiquid markets transaction costs are high and, in a circular fashion, high transaction costs contribute to an illiquid market.

35. Transaction costs cover a range of charges. The main distinction is between explicit costs and implicit costs.

- **Explicit costs** – commissions, settlement fees, taxes, transaction levies etc. which appear on the bills paid by the investors. They are relatively easy to identify though accurate measurement can be difficult because of a) complex scales and b) the complexity of the product – for example whether the brokerage commissions cover charges for advice or research. Explicit costs are most significant for smaller transactions and so most relevant for retail investors.

- **Implicit costs**, for large orders, are usually many times larger than explicit costs. Implicit costs are more challenging to measure as they reflect and vary with market conditions and are not specifically itemised or even measured on the investor’s bill. They include bid-ask spread, market impact, delay

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costs and opportunity costs. Implicit costs are usually associated with larger transactions and so are most relevant for larger investors – investing institutions and foreign investors.

36. Explicit costs for African exchanges vary considerably but are generally higher than in more developed markets. Some data was gathered from the qualitative survey, but it was both incomplete and at the same time more detailed than was required. Instead, a 2018 report has been used – Bright Africa 2019 by RisCura Group (cited as source). This report shows the main types of transaction costs for a sample of African exchanges. The data (which is tabulated in Appendix C, Table C1) show “round-trip” costs, i.e. the cost of buying and selling and so represent the cost taken out of a buy and sell transaction. This data is presented in Figure C1.

**Figure C1: Explicit transaction costs 2018 (% of transaction value), sample of African stock exchanges**

![Figure C1: Explicit transaction costs 2018 (% of transaction value), sample of African stock exchanges](image)

*Source: Bright Africa 2019, RisCura Group*

37. In addition to these charges, some governments levy transaction taxes, indicated as green in Table C9.

38. These costs, particularly those in the smaller, less-developed markets are rather high. Round-trip commission rates average 1.36% with the highest rates in the smaller, less-developed markets. In some markets, commission rates are negotiable – Botswana, Egypt, Ghana, Mauritius, Nigeria and Uganda. Commission rates are relatively low in Egypt and Nigeria but high in the others indicating that negotiation has not been a factor leading to lower commissions in less-developed markets. Other charges are also high with exchange and settlement fees averaging 0.53% and other fees averaging 0.18%.

39. In large part the high charges reflect:

   a) The small size of the market meaning that costs cannot be spread over a large number of transactions. Costs of running settlement systems and staffing stockbrokers are, to a considerable extent, fixed. The economies of scale which allow lower charges in developed and larger African markets are not available.

   b) The limited number of intermediaries and brokers which again reflects the smallness of the markets and limits the scope for competition to drive down charges.
APPENDIX D: RESULTS OF QUALITATIVE SURVEY—NIGERIA, GHANA, WEST AFRICA (BRVM)

1. The questions are given in Appendix 2. As stated in the report, the results were less successful than those for the quantitative survey. The results are based on survey results from just a few respondents and consultant interpretation.

Nigeria

2. Only one factor about attracting companies to list, the opportunity to attract new and more diverse board members, was rated as Not Important.

3. The country situations were assessed as Excellent or Acceptable with the exception of specific tax advantages for listed companies which was rated as poor.

Ghana

4. All factors were rated Very or Quite Important apart from the availability of venture capital/private equity, rated as Not Important, though this may have been a misinterpretation of the question.

5. The country situations were assessed as Excellent or Acceptable with the exceptions set out below which were rated as Poor.

6. Country factors rated as Poor acting as a deterrent to company listing were:

- Absence of growth market segment
- Attractive venture capital/private equity alternative
- Lack of market liquidity
- Fear of increased tax burden
- Lack of underwriting facilities.

7. Country assessment about factors that attract companies to listing rated as Poor were:

- Lower cost of capital
- Equity finance more flexible than debt finance
- Improving credit standing and leverage
- Specific tax advantages for listed companies.

8. Country assessment factors affecting attractiveness of stock exchange for investors rated as Poor are:

- Standards of corporate governance and enforcement
- Liquidity of secondary market
- Cost of trading, system and commissions.

BVRM

9. All the factors raised in the qualitative survey and interviews were rated Very or Quite Important. None were rated as Not Important.

10. The country situations are generally assessed as Acceptable with the exceptions set out below which are rated Poor.

11. Country factors rated as Poor acting as a deterrent to company listing are:
- Small size of market
- Difficulty or slowness of listing process
- Absence of growth market segment
- Attractive venture capital/private equity alternative (though this may not be correct)
- Lack of market liquidity.

12. Country assessment about factors that attract companies to listing rated as Poor are:

- Lower cost of capital
- Specific tax advantages for listed companies.

13. Country assessment about factors affecting attractiveness of stock exchange for investors rated as Poor are:

- Cost of settlement
- Liquidity of secondary market
- Cost of trading, system and commissions
- Levels of transaction taxes.