# The Capital Markets Soundness Report (CMSR)

## Volume XVI


*"Charting a Recovery Path for the Capital Markets Industry in Kenya Post Covid-19: Reset; Reprioritize; Reconfigure"*

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## SPECIAL MESSAGE FROM THE AG. CHIEF EXECUTIVE

**Mr. Wycliffe Shamiah, FCPA**
**Ag. CE, Capital Markets Authority, Kenya**

Welcome to the 16th edition of the Capital Markets Soundness Report covering events in the third quarter of the year 2020. Uncertainty has continued to characterize the year with effects of the covid-19 pandemic observed across jurisdictions and markets. The first half of the year 2020 witnessed immense monetary and fiscal Government interventions, aimed at sustaining and protecting economic performance amidst the health and economic impacts of the covid-19 pandemic. Most global economies closed down to prevent the spread of the pandemic across borders.

We have now began to witness the gradual opening of global economies, albeit progressively, with efforts by Governments to institute transmission mechanisms from primarily National policies to a more laissez faire environment, increasingly incorporating the private sector.

The role of Micro, Small and Medium Enterprises (MSME) continue to be a key focus area noting their impact in economies, particularly within the Sub Saharan region as strategic efforts and interventions are made to ensure business continuity, sustainability and anticipated growth in the coming years post covid 19 .

Despite the challenges that the financial markets have faced in the course of the year, outlook remains optimistic as financial markets practitioners redirect efforts towards capitalizing businesses to restore their sustainability and growth in the medium term to long term.

The Authority continues to undertake reforms in stride to propel activity within the domestic capital markets with a critical input being the ongoing review of the Capital Markets (Securities)(Public Offers Listing and Disclosures) Regulations 2002; policy and regulatory interventions to support changes in businesses operations over the years and technological advancement, informed by engagements with our key stakeholders.

As we chart a recovery path for business and industries in our motherland post the pandemic period, I urge you to continue engaging with us in providing strategic input to accelerate take-off, once major economic driving factors show stability and the global economy fully opens up.

I hope that this report continues to inform your strategic initiatives and decision making in your day to day business as you remain steadfast in contributing towards the realization of Kenya's Vision 2030 that aims to transform this economy into a middle-income country by the year 2030.My sincere gratitude to you as a key player in the attainment of success within the Capital Markets in Kenya.

I remain hopeful, that as the path towards recovery takes shape, we will all contribute towards the deepening of our markets and prosperity of the Kenyan economy with the Capital Markets playing its rightful role of mobilizing and allocating capital to players within the industry.

Happy Reading!

**FCPA Wycliffe Shamiah,**

**AG. CHIEF EXECUTIVE**

## EDITORIAL

**Mr. Luke Ombara**
**Director, Regulatory Policy and Strategy, CMA**

The 16th edition of the Soundness Report features measures that Governments across the globe have taken to open local economies to abate the economic losses realized so far by the Covid 19 Pandemic. The last two quarters were largely characterized by immense Government policy interventions in a bid to fight the Pandemic while maintaining minimum economic activity to stop the spread of the virus.

However, almost a year since the scourge and resultant adverse consequences were witnessed in China, many countries have put in measures towards re-opening economies, with restrictions eased and productive sectors of the economies opened. This has however been undermined by the possibility of a second wave sweeping the globe as already observed in countries like France, the United Kingdom and Brazil.

Despite these concerns, the financial markets continue to look into the future to inform strategy and policy formulation to activate economic recovery. This informs our theme for this quarter "***Charting a Recovery Path for the Capital Markets Industry in Kenya Post Covid-19: Reset; Reprioritize; Reconfigure".*** To bring this into perspective, we delve into the new measures being considered for adoption in the assessment and determination of credit risk for borrowers – both corporate and retail post-Covid as resumption of market centered credit assessment is anticipated in the coming months.

Further, new regulatory interventions continue to be observed with the International Organization of Securities Commissions (IOSCO) developing a consultative paper on how its regulatory members can adopt and implement Artificial Intelligence (AI) and Machine Learning (ML) as a solution to business operations and functions, identifying five primary uses of AI and ML within the Capital Markets industry. In addition, IOSCO published 11 good practices to enhance the practices and processes on deference in a bid to strengthen international cooperation across jurisdictions. On a jurisdictional level, the

European Union launched a short-term prospectus for listed companies in a bid to promote and ease listing processes for issuers. Within the Sub-Saharan Africa, Mauritius published a licensing criterion for peer to peer lending within the country through its P2P lending rules. This follows Nigeria's publication of crowdfunding rules in the last quarter as the continued role of technology and capital raising platforms takes center-stage in the era of technological revolution for efficiency, profitability, as well as growth of businesses and industries in their quest for capital sourcing.

As a pointer to growing investor interest and recovery in the global issuance markets, the World Bank successfully issued a 10-year USD 3 Bn global bond in August 2020, with the issuance attracting huge demand from global investors leading to an order book of over USD 4.6 Bn against a targeted USD 3 Bn. Complimentarily, activity on shariah based instruments primarily the sukuk was observed during the quarter with the Islamic Development Bank issuing a debt sustainability sukuk valued USD 1.5 Bn in response to covid-19. In the same vein, Malaysia launched a 500 Mn Ringit sukuk for covid-19 recovery that was offered through digital banking platforms.

Further, this Edition examines developments within the East Africa region with Ethiopia publishing a bill aimed at setting up a Capital Markets Authority and an exchange in its quest to develop its capital markets.

On the domestic front, the capital. markets remained resilient with investors diversifying into non-traditional Securities such as Exchange Traded Fund (ETFs), Real Estate Investment Trusts (REITs) and Equity Derivatives all of which reflected increased turnover. More FinTech solutions were presented to the Authority for approval to test in the regulatory sandbox, while new innovative products and services were facilitated

To further appreciate perspectives and analyses of the developments herein referenced, I urge you to indulge in reading the report and take note of the Authority's interventions and steps aimed at positioning the Kenyan Capital Markets as a destination choice for the investors across the globe.

The report was subjected to stakeholder engagement on Friday, 23rd October 2020 through an online webinar, in the face of the pandemic, where contents of the report were presented and discussed prior to publishing.

Enjoy your read!

**Mr. Luke E. Ombara**

**DIRECTOR, REGULATORY POLICY & STRATEGY**

## 1.0 Special Feature – The Evolution of Credit Risk assessment in the Face of the Covid-19 Pandemic

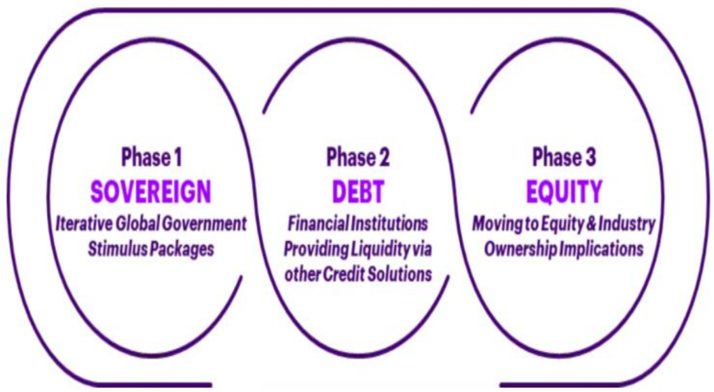
Throughout the life of the Covid-19 pandemic, policy makers have pursued a vision of seeking to balance the health, economic and financial risks posed by the pandemic, with the dynamics evolving month on month.

In the initial months of the pandemic, globally and domestically, the major challenge for financial institutions was the need to develop essential strategies for liquidity management. This essentially saw Central Banks across the globe make key monetary policy interventions aimed at ensuring proper liquidity management of their economies. In their role as the banker of Government, they increased government bond purchases, indirectly financing a large part of the resultant increase in budget deficits needed to address the crisis.

According to a July report by the Financial Times, in only a few weeks, most of the major Central Banks increased the size of their balance sheets by 7 to 16 per cent of their gross domestic product, which is more compared to the two years following the 2008 financial crisis. Another instrument that central banks adopted in very large scale in this crisis has been the provision of lender-of-last-resort facilities [1]to the banking sector. Most of these have been through open-market operations and discount window lending. Other measures included frequent reviews of the benchmark Central Bank Rate[2].

Further, the pandemic subjected new dynamics to microfinance institutions in structuring their on-lending facilities to clients a MFIs have largely afford clients a margin of flexibility to cope with emergencies when publicly funded safety nets fall short. However, as the pandemic manifests into different phases as summarized in figure 2 below, the role of financial institutions in promoting economic activity is equally evolving, with regulators and market intermediaries across financial sector segments at the center of such developments. One key area that is currently under focus is the assessment of credit quality and loan impairments of clients and investors.

**Fig 1: Phases of the Credit Crisis - World Economic Forum**




*Source: Accenture*

First, there's the sovereign phase where the banking industry is primarily a transmission mechanism for public policy decisions. Here, the public sector balance sheet, rather than the banks, shoulders the risk. Second is the debt phase, where the burden for providing capital and liquidity will fall principally on the banks and fixed income investors.

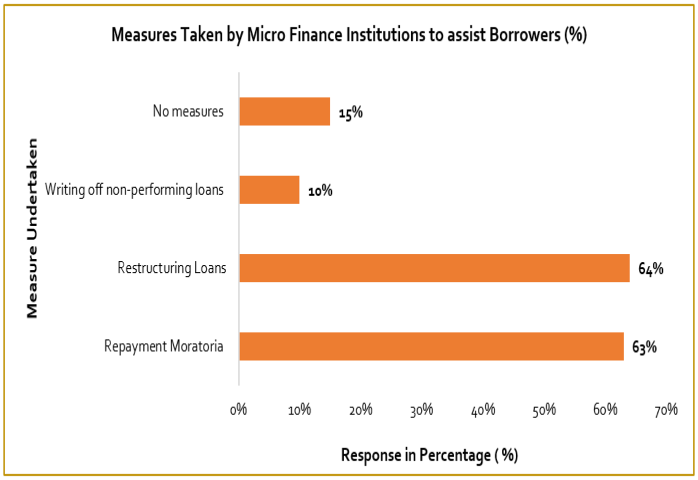
[1] Market Maker of Last Resort (MMLR) activities occur when central banks address market illiquidity by directly buying a wide range of risky financial assets or accepting them as collateral. That allows asset holders to obtain cash by lending these securities out, rather than having to dump them into the market. Such interventions are designed to prevent self-reinforcing runs on specific financial products, including money market mutual funds, commercial paper, leveraged bond funds and asset backed securities.

[2] https://www.ft.com/content/5a1a1e9c-6f4d-11ea-89df-41bea055720b

Finally, as it becomes clear that businesses of all sizes may be unable to repay outstanding debt, we will enter phase three, with some countries already experiencing effects of this phase in their economies. This is the equity phase, which will require restructuring and changes in ownership. It is important to note that these three phases are not sequential they are already happening in parallel. Banking and capital markets players will need to find ways to navigate these three phases while balancing the needs of customers, shareholders, and the broader public good.[3] This is informed by the fact that banks around the world face an imminent credit crisis as their clients struggle to stay afloat and meet loan repayments. In the US alone, by mid financial year 2020, the top banks had made provision for almost $60 billion of non-performing loans.

To bring this to perspective, the Consultative Group to Assist the Poor (CGAP) conducted an assessment in July 2020, where nearly 300 participants from 30 countries joined CGAP workshops to discuss how the COVID-19 crisis was affecting MFPs and their funders, microfinance investment vehicles (MIVs), in terms of renegotiating and restructuring debt claims on distressed MFPs.

**Fig 2: Measures Taken by MFIs to Assist Borrowers**




*Data as of 22nd July 2020 … N=147*
*Source: CGAP Global Pulse Survey of Micro Finance Institutions*

**Fig 3: CGAP Defined Path from Crisis to Recovery for MFIs**


*Source: CGAP*

The MFIs that responded to CGAP's pulse survey report that, on average, 18 percent of their portfolios have been placed under moratoria or rescheduled. In some cases, regulators mandated moratoria. In others, they encouraged moratoria by enabling FSPs to treat paused loans on their balance

[3] https://www.weforum.org/agenda/2020/07/banking-force-for-good-covid-driven-credit-crisis/

sheets as though they were still performing. The degree of prescriptiveness varied widely across regulators, but often lenders retained great discretion over when to offer and how to structure moratoria. Some of the key aspects to be aware of include the following:

i. Levels of debt subordination and seniority.

ii. Collateral (secured vs. unsecured) or other form of credit enhancement (guarantee, etc.)

iii. Currency of obligation

iv. Term or maturity of payment obligations, such as timing of payment schedule and nature of payment obligation (e.g., bullet, amortizing, demand, etc.)

v. Creditor structure such as fixed term vs. open-ended funds, public sector vs. private sector lenders, and local vs. foreign lenders.

vi. Legal limitations and regulatory constraints imposed on creditors.

vii. Documentation covenants and events of default (e.g., scope, triggers, and implications for other loans such as cross-default vs. cross-acceleration).

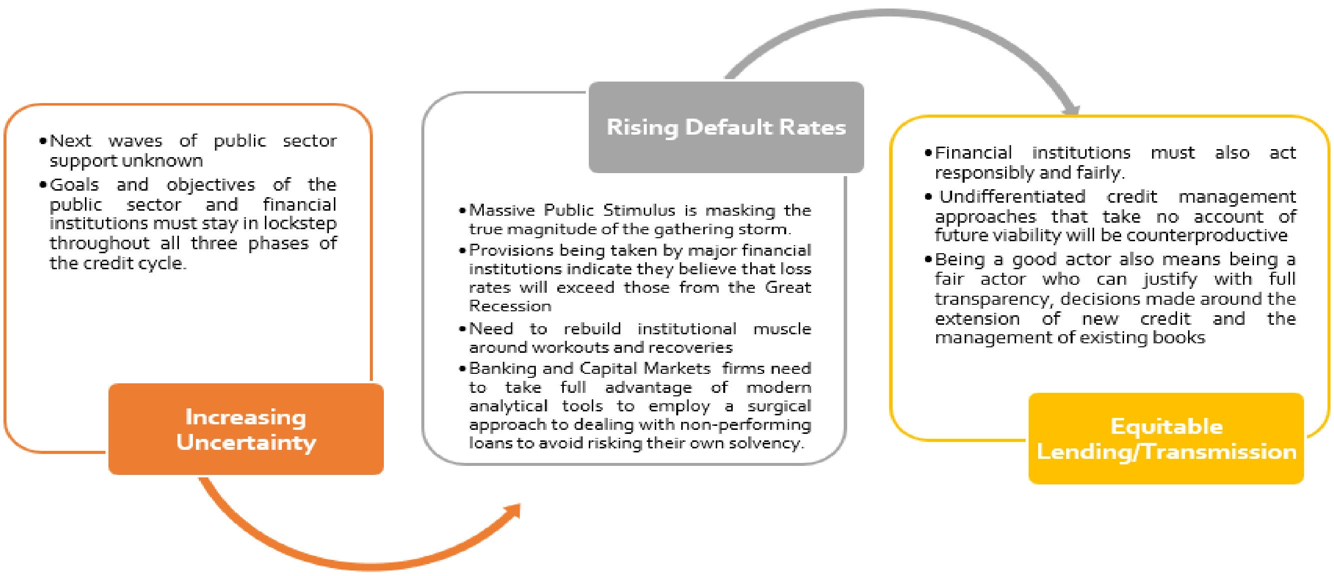
viii. Presence of other creditor claims, such as shareholder loans or affiliate or network management fees.

Like banks, the Capital Markets sector equally needs to establish analytical, personalized credit management to support clients, satisfy shareholders and enable the restructuring of the economy. As it unfolds, financial institutions will need to effectively manage a series of risks.

On the other hand, firms/intermediaries need to remember the 3 Rs: reset, reprioritize, and reconfigure their business strategies to adapt to the current and near-term situation. They will need a firm grip on fiscal policy to identify where they can fill the breach as good actors. At the same time, they have to be prepared to roll with a few punches along the way, because recoveries are rarely smooth, upwards motions. In other words, firms must start thinking about risk management as a part of, rather than distinct from, their overall strategic objectives.[4]

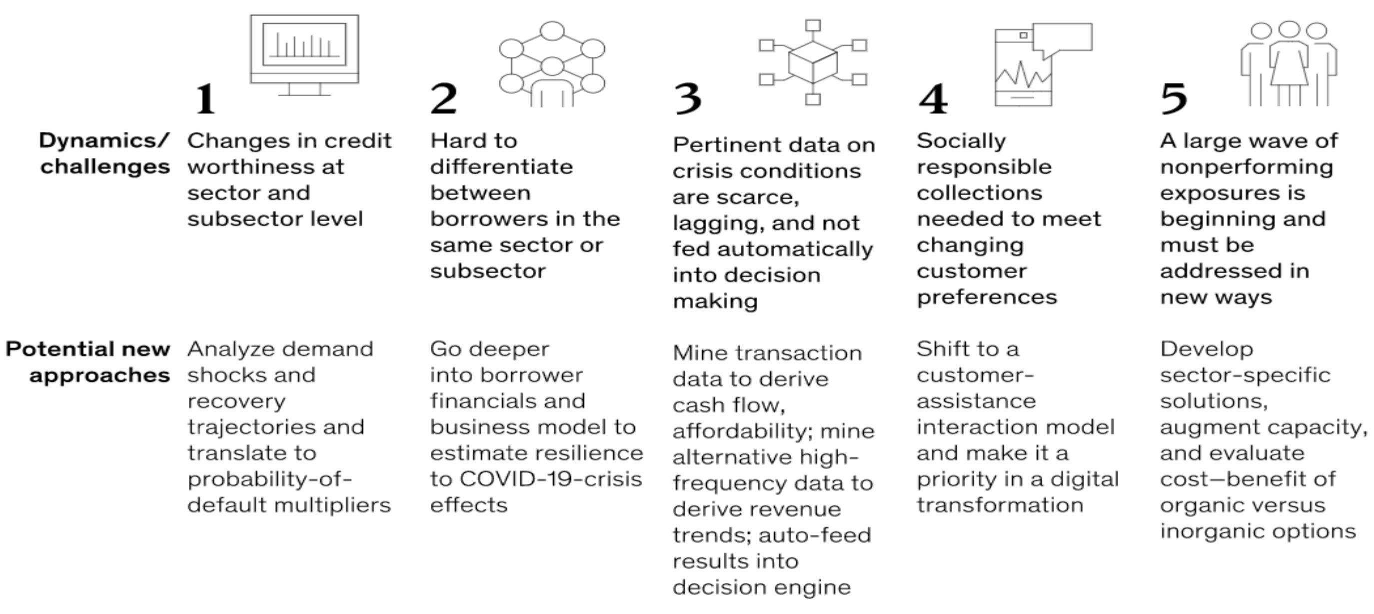
[4] https://www.weforum.org/agenda/2020/07/banking-force-for-good-covid-driven-credit-crisis/

**Fig 4: Phases of a Credit Crisis**




*Source: World Economic Forum*

**Fig 5: Dynamics, Challenges and Potential New Approaches to Credit Risk**




*Source: Mckinsey & Company Global*

With major repositioning in the financial markets, real-time, price-driven events (such as margin calls) have posed a greater threat to financial stability, though they do not lend well to conventional stress testing and risk models. The Bank of England projects that UK GDP could fall by 14% in 2020, which is three times more severe than the assumed decline in its latest stress test scenarios. The regulators are concerned about the fair treatment of corporate customers when negotiating new or existing debt facilities.

How economies will emerge from the pandemic remains uncertain, and more behavior-driven data and predictive analytics may be required to gain a more timely and accurate view of financial resilience post-Covid-19. Regulatory stress testing has, to date, focused on economic swings, rather than operational disruptions. But as the pandemic shows, fraud concerns, disruptions to communication networks, and prolonged absence of critical staff have posed a greater material threat to the resilience and stability of financial systems. This highlights the need for scenarios to be considered both in terms of operational resilience and prudential stress testing.

Remote working in most countries has proved more effective than previously envisaged, with firms' IT systems remaining resilient. Such shifts should require regulators to take a more balanced view of technology risks versus people risks, most jurisdictions have allowed key workers in financial service sector to work from home.

According to global risk regulator report for July 2020, viability of adopting remote working more broadly and permanently in the financial sector industry, systems and controls required to ensure data protection and prevent internal fraud may come into sharper supervisory focus. At the same time, the assumptions behind having disaster recovery sites scattered across the country may be called into question as the pandemic can cause large-scale operational failures, hitting all markets simultaneously[5].

Financial institutions need to prove to regulators that their operations, systems and processes conform to accepted risk practices. Therefore, financial sector regulators need to step up regulatory engagement and response strategies, fine-tune investment budget allocation and reconsider model development and validation rules as some of the no-regret moves.

**Management Review:**

- *The Covid-driven credit crisis will likely be a two to three-year cycle depending on how the public health crisis shapes the macroeconomics. Given this prediction, the banking and capital markets industries need to continue to look for ways to be shock absorbers rather than shock amplifiers and to work collaboratively to help build stronger, more resilient communities. More strategic decision making will be required in the recovery period post the pandemic with consultations between licensed entities and their respective regulator encouraged.*

[5] https://www.globalriskregulator.com/Subjects/Reporting-and-Governance/The-aftermath-of-Covid-19-is-likely-to-result-in-greater-regulatory-oversight

- *Further, more collaboration with governments, multilateral development banks and other capital providers should be promoted.*
- *When money is in short supply, the most valuable currency is information. Developing and managing information flows between MFPs and their creditors, as well as between creditors, will be key to bringing collaborative resolutions to the challenges facing MFPs and their funders as they confront the health and economic consequences of this pandemic.*
- *However, the challenges will not be limited to debt restructuring. The crisis is testing resilience of the whole microfinance sector and of its capacity to successfully navigate into the recovery stage.*
- *Covid-19 has weakened the value of the data used in rating systems within the financial markets – making them unreliable. For example, all the data relied upon to test an SME's credit risk is likely to be considered outdated due to the immediate economic shock caused by the pandemic. Rating SMEs with data from before the crisis – from 18 months ago (balance sheets) to 2-3 months ago ( Credit Registries) – is no longer relevant as it fails to provide an accurate assessment of a business 'current situation.*
- *However, new technologies have proven to offer innovative solutions such as open banking. Open banking enables real-time, more personalized data on which to base risk and credit scoring. Open banking data can provide risk management teams with the ability to score a company on its capacity to generate revenue. A business' liquidity and transaction data can be measured by the transactions in its bank account. It is this data that is considered most relevant and important now by finance specialists.*
- *The Authority will also include in its policy proposal submissions to the National Treasury for the FY 2021/22 a proposal to consider provision for mandatory listing by MSMEs qualified to access funds from the Governments Credit Guarantee Scheme as a measure of promoting corporate governance and transparency in the use of proceeds for business growth, subject to stakeholder engagement and participation.*

## 2.0 Global Developments

### 2.1 Shift in Covid-19 Funding and Administration Approach

The abrupt surgency and spread of the Covid-19 pandemic into global economies necessitated emergency response across countries, the African continent included. Most countries had not made contingency provisions in their budgets to cater for such an eventuality. In response, many countries reprogrammed their existing budgets, activated contingency reserves, and adopted supplementary budgets.

To further mobilize resources and accelerate emergency spending, many countries created dedicated Covid-19 extrabudgetary funds (EBFs). To examine budgetary mechanisms adopted by countries in response to the pandemic, the World Health Organization conducted a survey in June 2020 where it was established that more than 40 countries had established funds to support their broader response to the Covid-19 crisis, the majority of which were extrabudgetary.

An Extra Budgetary Fund can be defined as a set of accounts or a government entity engaged in "*financial transactions, often with separate banking and institutional arrangements, that are not included in the annual state budget law*" (Allen and Radev 2006). Excluding social security and health funds, EBFs account for about 15 percent of central government expenditure across a range of advanced, middle-income, and low-income economies, or close to 50 percent if social security and health funds are included[6].4 Examples include special purpose funds (of which Covid-19 funds are an example), development funds, savings funds, trading funds, and investment funds.

**Fig 6: Covid-19 Funds Around the World**

*Source: COVID-19 Funds in Response to the Pandemic, IMF COVID-19 Special Series, 26th August 2020 Issue*

According to the IMF assessment, the list spans countries with different administrative and Public Finance Management traditions, legal frameworks, and income levels. Some of these countries routinely create and use extrabudgetary funds in normal times, for example, funds for road maintenance, health, and social security (Kutzin and others 2010). In other countries, the creation of COVID-19 funds marks a break from a more unified approach to budgeting and spending[7].Several drivers behind the creation of such funds include i. The need to establish centralized and high-level control and management of Covid-19 measures, for example, under the President's Office; ii. To raise and pool together public and private resources, which standard budget

[6] COVID-19 Funds in Response to the Pandemic, IMF COVID-19 Special Series

[7] In Azerbaijan and Uruguay, for example, spending by extrabudgetary entities (other than social security funds) typically accounts for 15 and 30 percent of GDP, respectively. In other countries, like Colombia and Mexico, it represents less than 1 percent of GDP. In sub-Saharan Africa, it ranges between 1 and 7 percent of GDP (data are for 2018 from IMF Government Finance Statistics (GFS): https://data.imf.org/GFS).

practices may not allow; iii. Bring together different sectors and regional and local governments affected by the pandemic to facilitate implementation of emergency spending; iv. Streamline or bypass some steps in the budgeting, spending, or procurement processes which, however necessary in normal times, may slow down the response to the crisis; and v. Separate Covid-19 spending from other spending to enhance financial transparency and accountability, and create a clearly defined audit trail.

The WHO assessment however revealed that, and for good reasons, EBFs are often regarded as suboptimal. A primary factor for the suboptimality is the fact that the creation of EBFs can fragment policymaking and implementation and cloud the understanding of a government's fiscal operations. Moreover, in the absence of strong safeguards, the existence of EBFs with independent spending authority can dilute accountability and weaken fiscal control, creating significant fiscal risks and corruption vulnerabilities.

A post review on the rush to set up Covid-19 funds by various countries has led in some cases to a legal vacuum, in which the purpose, management structures, and oversight mechanisms of the funds are not sufficiently defined. The need for governments to respond swiftly to the emergency under high public pressure has often led to the relaxation of

ex ante financial controls and standard procurement processes without any safeguards being put in place. While such policies can effectively accelerate spending in some contexts, they can also create significant governance vulnerabilities, particularly when the funds operate outside government systems, are managed by officials not familiar with good principles of PFM, and are not subject to robust transparency and reporting standards. Finally, while most of the funds were created to deal with the emergency situation, there is the risk that some governments will seek to broaden their operational mandate, and extend the duration of the funds after the pandemic has ended. Different legal instruments have been used to establish COVID-19 funds.

In many countries, they result from presidential decrees (examples include Azerbaijan, Colombia, Côte d'Ivoire, Tunisia), sometimes by virtue of the powers arising from a state of emergency. In others, they were established by the legislature through a new law (Austria, Italy, Mexico), an amendment to an existing law (Nigeria), or by decisions of the council of ministers (Lebanon, Mauritania). In some countries within the British Commonwealth tradition, they were created by regulations issued by the Ministry of Finance permitted under the organic budget law (Ghana, Kenya, Mauritius).

**Table 1: Covid-19 Funds - Revenue Sources**

| Mostly Public | Mostly Private | Public, Private and External |
|---|---|---|
| Austria, Columbia, Hungary, France, Italy, Liberia, Mexico, Sierra Leone, Ukraine, Uruguay, Zambia | Benin, Cameroon, Gabon, Ghana, Iraq, Jordan, Lebanon, Mali, Mauritius, Niger, Pakistan, South Africa, Tunisia, Uganda, Zimbabwe | Armenia, Azerbaijan, Bhutan, Botswana, Chad, Democratic Republic of Congo, Cote d'Ivore, Djibouti, Equatorial Guinea, Kenya, Lesotho, Mauritania, Morocco, Nepal, Nigeria, Senegal, Sri Lanka, Togo |

*Source: WHO survey conducted in March 2020 and desk reviews undertaken in May and June 2020*

The extent to which the funds' objectives are specified in law varies. Some countries have left the scope vague. In Ghana, for example, the fund's mandate extends to all activities that complement the efforts of the government to combat the pandemic. Other countries have defined their funds' mandate more explicitly: in Austria, for example, it is to "stabilize healthcare funding, stimulate the labour market, maintain public order, and stabilize companies' liquidity."

**Table 2: Covid-19 Funds: Integration with Public Finance Management Systems**

| Off-Budget | Off-Budget, Using Regular PFM Channels | On-Budget |
|---|---|---|
| Armenia, Cameroon, DRC, Cote d'Ivore, Gabon, Honduras, Iraq, Jordan, Kenya, Lebanon, Lesotho, Mali, Nepal, Niger, Pakistan, Sierra Leone, SA, Tunisia, Uganda | Azerbaijan, Benin, Bhutan, Botswana, Colombia, Djibouti, Equatorial Guinea, Ghana, Italy, Liberia, Mauritius, Togo, Zimbabwe | Austria, Chad, France, Hungary, Mauritania, Mexico, Morocco, Nigeria, Senegal, Ukraine, Uruguay, Zambia |

***Note:*** *"On-budget" as defined by the WHO assessment guidelines means that the fund is an account, program or subprogram within the existing budget system and is fully integrated into budget execution and control procedures.*

The scope of the fund in Botswana is defined in even greater detail and includes interventions such as wage subsidies, loan guarantees, building-up strategic grain reserves, medical supplies and equipment, and citizen evacuation. In other cases (Benin, Sierra Leone) the scope is not defined and has evolved on a largely ad hoc basis. Covid-19 funds are generally not managed by line ministries but have their own governance arrangements. In Sierra Leone, for example, the fund sits under the President, while in Azerbaijan it reports to the Cabinet.

The Ministry of Finance or Treasury can play various roles, from fund administration (Kenya, Mexico) to general oversight (Côte d'Ivoire, Mauritius), while in some cases the Treasury plays no role at all (Mauritania). In a few cases, private sector entities manage the fund. This is the case of the South Africa Solidarity Fund, which is managed by a private entity and is subject to the same accountability requirements as public benefit organizations[8].

**Management Review:**

- *The establishment of Covid-19 funds aimed at addressing emergency needs in the face of the pandemic forwards key lessons for consideration by Capital Markets regulators in the current environment as most also consider the establishment of Capital Markets specific funds aimed at cushioning Capital Markets participants from the effects of the pandemic.*
- *In its medium-term recovery strategy post the pandemic, the Authority is forwarding as a policy proposal to the National Treasury, the establishment of a Capital Markets Fund for Small and Medium Enterprises to support the entities in transitioning through the effects of the pandemic. Borrowing from the potential gaps that could arise based on how the fund is established, management commits to engaging with the National Treasury in ensuring that the fund is covered on matters i. Legal Mandate ii. Purpose of funds and sources of finance iii.*

[8] Special Series on COVID-19 - August 26, 2020 COVID-19 Funds in Response to the Pandemic

*Management and Oversight iv. Spending Procedures v. Transactions vi. Monitoring and Evaluation vii. Transparency and Accountability and viii. Audit Procedures.*

- *Constitutionally, the Micro and Small Enterprises Authority is charged with the responsibility of overseeing the functioning processes of MSMEs, the Authority will review the best fitting legislation upon which the fund may be established. Whether the MSME Act, CMA Act or the Public Finance Management Act.*

## 2.2 Sustained Issuance of Capital Markets Products to Support Funding for Covid-19 Measures

### 2.2.1 World Bank Prices New USD 3 Billion 10-Year Global Bond

On 19th August 2020, the World Bank (International Bank for Reconstruction and Development, IBRD, Aaa/AAA) priced a USD 3 billion 10-year global benchmark Sustainable Development Bond maturing on August 26, 2030.Extremely strong demand from global investors for the USD benchmark was observed leading to an orderbook of over USD 4.6 billion, with more than 130 investor orders, anchored by Central Banks and official institutions. Other investors included bank treasuries, asset managers, as well as pension and insurance funds.

The 10-year benchmark pays a semi-annual coupon of 0.75% per annum and has an issue price of 99.415% and a final spread of 15.35 basis points over the 0.625% US Treasury August 30, 2030 reference bond, offering investors a yield of 0.811%. Joint lead managers for this transaction are Bank of America Merrill Lynch, HSBC, J.P. Morgan, and Wells Fargo Securities, with the bond listed on the Luxemburg Stock Exchange.

**Table 3: Investor Distribution Summary on World Bank Bond**

| Investor Distribution by Investor Type | | Investor Distribution by Region | |
|---|---|---|---|
| Central Banks/Official Institutions | 42% | Asia | 46% |
| Asset Managers/Insurance/Pension Funds | 32% | EMEA | 38% |
| Banks/Bank Treasuries/Corporates | 26% | Americas | 16% |

*Source: World Bank*

Islamic finance is based on Islamic law and is guided by a set of moral and ethical principles. These include honesty and transparency, as well as the prohibition of usury (riba), uncertainty (gharar), and speculation (mayssir). Islamic economic system encourages welfare (maslaha), promotes wellbeing (falah), and prevents harm (mafsadah). Transactions rest on contracts that promote partnerships, profit and loss sharing, as well as links to the real economy. In times of crises such as Covid-19 pandemic, such principles support mechanisms that bridge the financial disparities in many countries[9].

While Islamic finance could play an important role in the Islamic world's recovery from COVID-19, the governments are expected to initiate and lead projects that rebuild economies and societies. The pandemic has highlighted the need to rethink the provision of healthcare services. New conversations on supply chains and critical infrastructure are

[9] http://imfn.org/islamic-finance-and-prospects-for-weathering-covid-19

also required. To this end, sukuk (bonds) could provide innovative and sustainable sources of finance for recovery and regeneration projects.

While sukuk can mobilize financing for a variety of sustainable projects, the market has recently witnessed the development of sustainable and responsible investment (SRI) and green sukuk. Issuance of pandemic sukuk can be traced back to 2017, when the World Bank first mooted the idea of pandemic bonds to support the Pandemic Emergency Financing (PEF) facility. This mechanism provides funding to developing countries that are at most risk of serious disease outbreaks. PEF becomes available once an outbreak reaches predetermined levels of contagion and spreads across international borders.The following are some of the countries issuing Sukuk during Covid-19 period:

### 2.2.2 Islamic Development Bank Issues (IsDB) US$ 1.5 Billion Debut Sustainability Sukuk in Response to COVID-19

Islamic Development Bank successfully priced the 5-year Trust Certificates under its US$25 billion Trust Certificate Issuance Programme. It was priced at par with a profit rate of 0.908% to be payable on semi-annual basis. This is the Bank's second public issuance in 2020. Proceeds from the debut Sustainability issuance will be exclusively deployed towards social projects under IsDB's

Sustainable Finance Framework, with a focus on access to essential services and SME financing and employment generation categories under the umbrellas of 'SDG-3: Good Health and Well-Being' and 'SDG-8: Decent Work and Economic Growth' for its 57 Member Countries, to assist them in tackling the aftermath of the COVID-19 pandemic. The project categories are identified as per the guidelines standards set by from the International Capital Market Association (ICMA) under its Sustainability Bond Guidelines (2018) and Social Bond Principles (2018)[10]."

The issuance, the first ever AAA-rated Sustainability Sukuk in the global capital markets, is one of the many initiatives that IsDB has undertaken as part of its wide-ranging response to COVID-19 pillared on the Respond, Restore and Restart framework in its Member Countries. It marks the second trade based on the Bank's Sustainable Finance Framework, which also served as the foundation upon which the Bank issued its debut €1 billion Green Sukuk in November 2020.

The distribution was well diversified with 53% allocated to Middle East & North Africa, 37% to Asia, 8% to Europe, and 2% to others including US Offshore. 79% was allocated to central banks and official institutions, 16% to bank treasuries and 5% to fund managers and private banks.

### 2.2.3 Malaysia launches 500 million-ringgit sukuk for COVID-19 Recovery

Malaysia's finance ministry on 18th August 2020 launched a 500 million-ringgit ($119.45 million) sukuk as part of the government's efforts to raise funds for their coronavirus economic recovery plan.The Sukuk Prihatin will be offered on digital banking platforms from Aug 18 to Sept 17, 2020 offering a 2% profit rate over a two-year maturity period[11].

### 2.2.4 Egypt plans first sukuk offering in bid to reduce debt burden

According to Egypt's Ministry of finance, the country is planning to issue its first sukuk, or Islamic bonds, in both local

[10] https://www.isdb.org/news/islamic-development-bank-issues-us-15-billion-debut-sustainability-sukuk-in-response-to-covid-19

[11] https://www.nytimes.com/reuters/2020/08/17/world/asia/17reuters-malaysia-sukuk.html

and international markets in the current fiscal year. Before the virus struck, the Egyptian government made headway in ending its reliance on short-term borrowing.

In February 2020, it met its target of tripling the size of Treasury bond sales and raising the share of longer-dated debt to 40% of annual domestic issuance, double the level in the fiscal year that ended June 2018. Mohamed Hegazy, head of the Finance Ministry's debt management unit, indicated that, Sukuk will help the country diversify its investor base as well as reduce the borrowing cost given that yields on sukuk are less than bonds[12].

**Management Review:**

- *The Capital Markets industry has seen innovative investment models with increased alignment towards sustainable financing instruments such as green bonds, social investment bonds and blue bonds. In the same vein, Islamic finance related instruments anchored on Islamic principles. Sukuks, shariah compliant bonds have been profiled in this pandemic season, further expanding the pool of capital markets instruments available for issuers.*
- *The Authority has been a key proponent on the use and growth of Islamic finance products in the industry facilitating capacity building across its market intermediaries as well as the Government of Kenya to spearhead sukuk offerings within the East African region through issuance of corporate and sovereign sukuk respectively.*
- *Further, the Authority is working closely with the National Treasury and the Financial Sector Deepening Africa in ensuring a sovereign sukuk issuance come to light in the short to medium term, in light with the provisions of the Government's medium term plan for the period 2018-2023.*
- *As a progressive regulator, the Authority is currently involved in the process of project evaluations ahead of a planned sovereign green bond issuance under the auspice of the National Treasury and the World Bank. The exercise is expected to result in the issuance of the first sovereign green bond issuance within the East African region, as the adoption of sustainable financing approaches grows in the country and region.*

## 2.3 Cross-border Corporation on FinTech Oversight

### 2.3.1 IOSCO Publishes Consultative Paper on Artificial Intelligence and Machine Learning

Over the last couple of years, inventions in the technology have taken a new trajectory, one that seeks to digitize and automate most of the tasks and services. Some of these inventions have been so drastic, so much that they seek to mimic the human anatomy in their functioning such as the use of Artificial Intelligence and Machine Learning.

Firms have adopted these technologies so as to improve on their service delivery and automate some of the tasks. The use of these technologies come with benefits and risks, and it is therefore necessary for the industry to be cognizant of both aspects. Since these advancements have touched on every industry, it has left the regulators of the different sectors of the economy with the huge task of outlining the guidelines on how to utilize these technologies to keep the risks at bay. A jurisdictional scan on initiatives by various regulators in addressing risks associated with AI and ML is summaries in table 4. It is against this background that the IOSCO(International Organization of Securities Commissions) in its mandate to assist in market development, strengthening market infrastructure and implementation of appropriate

[12] https://www.arabianbusiness.com/politics-economics/449889-egypt-plans-first-sukuk-offering-in-bid-to-reduce-debt-burden

regulation, released a consultation paper on 25th June 2020 to guide securities' markets regulators on how to regulate the market intermediaries utilizing Machine Learning and Artificial Intelligence technologies[13].

**Table 4: Initiatives Taken by Other Bodies**

| Institution | Year | Details on Artificial Intelligence and Machine Learning Interventions Undertaken |
|---|---|---|
| Financial Stability Board (FSB) | November 2017 | FSB released a report ("*Artificial intelligence and machine learning in financial services Market developments and financial stability implications"*) analyzing the benefits and risks that come with the use of AI and ML, therefore looking at the implications this would have on financial stability.[14]<br>The following aspects summarize the content of the paper:<br>• An efficient financial system will be achieved when the use of AI and ML is embraced.<br>• The use of AI and ML will lead to more interconnectedness between financial markets and other unrelated institutions.<br>• Application of AI and ML may lead to overreliance on outsourced services and this would need an adjustment in the regulatory frameworks to outline the mechanisms of handling third parties.<br>• If the AI and ML algorithms are not well interpreted, this could cause macro-level risks.<br>• The risks of utilizing AI and ML should be weighed before embarking on them such as issues around privacy of data, cybersecurity and conduct risks. |
| International Monetary Fund | June 2017 | The IMF released a report on Fintech and Financial Services whose aim was to set pace on having an economic framework and the opportunities that lie in the use of AI and ML[15].Further to this, the IMF went a notch higher to show opportunities for utilization of AI and ML in its own operations. |
| Institute of Internal Auditors (IIA) | 2017 | IIA [16]published directives guiding firms on the need to introduce AI auditing frameworks which would help in evaluating the positive and negative impacts of AI. |

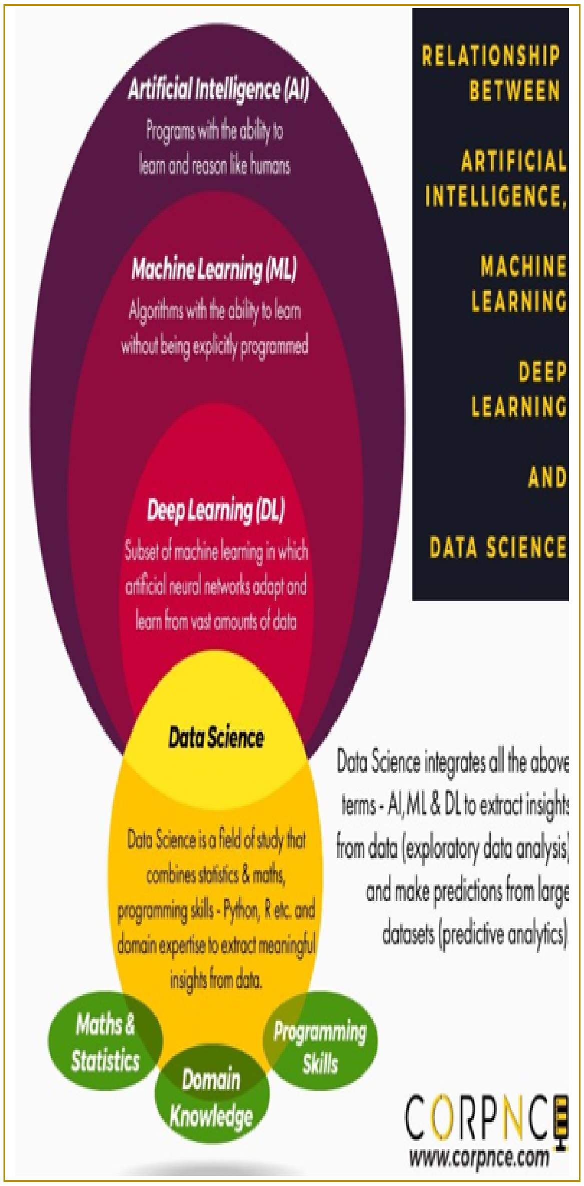
[13] https://www.iosco.org/library/pubdocs/pdf/IOSCOPD658.pdf
[14] https://www.fsb.org/wp-content/uploads/P011117.pdf
[15] https://www.imf.org/en/Publications/Staff-Discussion-Notes/Issues/2017/06/16/Fintech-and-Financial-Services-Initial-Considerations-44985
[16] https://global.theiia.org/knowledge/Pages/Global-Perspectives-and-Insights-Archives.aspx

| Institution | Year | Details on Artificial Intelligence and Machine Learning Interventions Undertaken |
|---|---|---|
| European Commission | April 2019 | The European Commission published draft guidelines addressing the issue of ethics in the use of AI.[17]The following 3 factors summarize the content of the guidance paper:<br>• The use of AI should fit in and comply with the regulatory frameworks in place.<br>• The use of AI should adhere to human ethics and values.<br>• The use of AI should be sound technically and socially. |
| The International Technology Law Association (ITechLaw) | May 2019 | ITechLaw released a paper outlining the principles that should be adhered to when using AI as follows;<br>• AI should promote ethics and should benefit the whole society.<br>• Accountability should be promoted.<br>• There should be transparency and no form of discrimination<br>• The use of AI should be reliable and safe<br>• Data privacy should be adhered to |

*Source: Various Institutional References*

[17] https://ec.europa.eu/futurium/en/ai-alliance-consultation/guidelines#Top

**Fig 7: Artificial Intelligence and Machine Learning in Summary and Primary Differences**

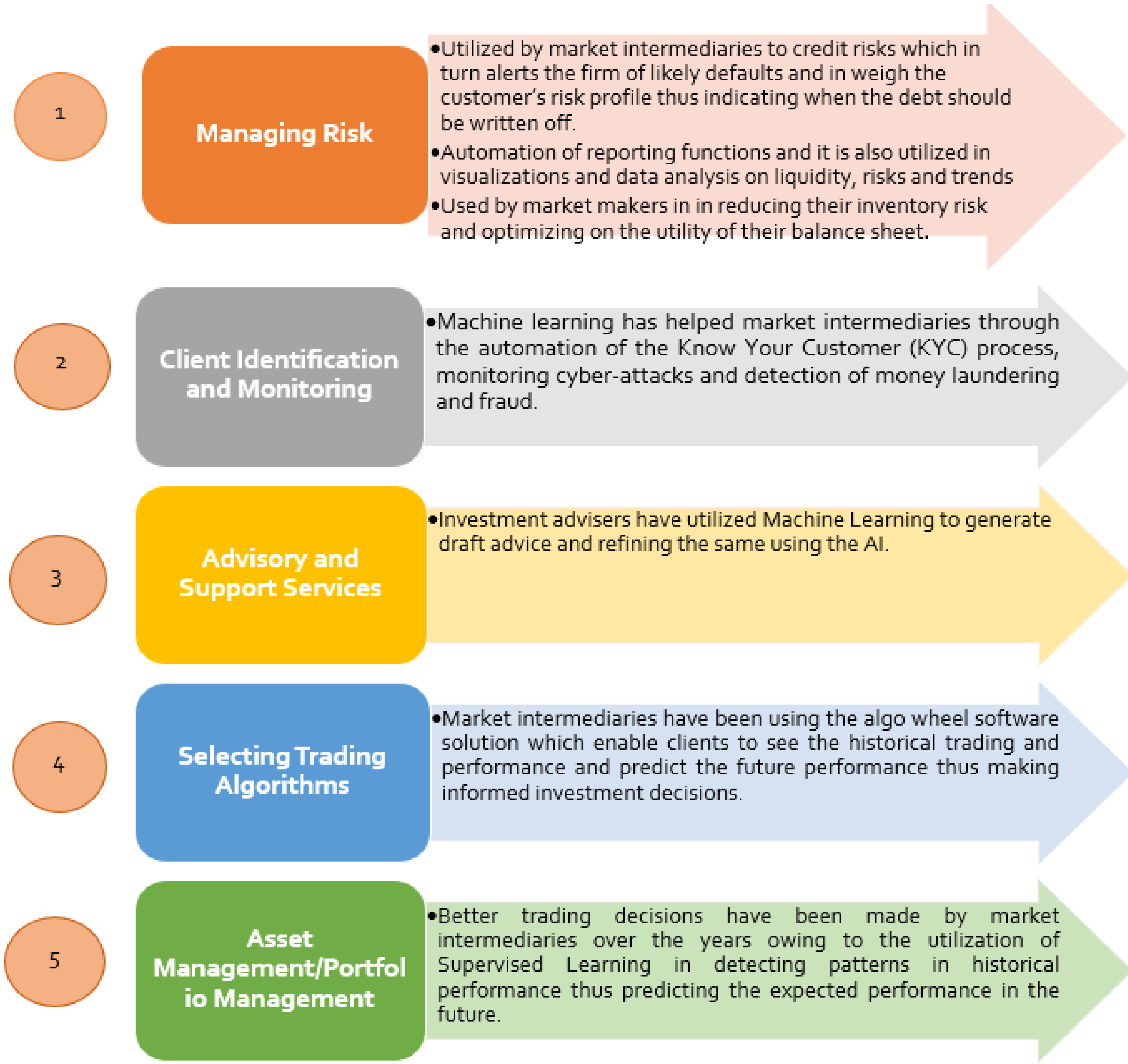



| | Artificial Intelligence | Machine Learning |
|---|---|---|
| 1 | AI is broader than ML. It uses computers to imitate the cognitive human functions | ML is a subset of AI, where machines have the ability to think and perform actions based on their past experiences. They can change their algorithm as per the data sets on which they are operating. |
| 2 | The aim of AI is to increase the chances of success and not accuracy | ML focuses on accuracy rather than success |
| 3 | AI is not a system; it can be implemented within a system to operate on computer programs that can work smart. | In ML, the system can work and learn from datasets |
| 4 | The goal is to stimulate natural intelligence to solve complex problems | The goal is to learn from data for a certain task to maximize the performance of the machine on the task. |
| 5 | AI is primarily used in decision making | ML allows the system to learn from previous experiences |
| 6 | Develops a system to mimic humans, thus the systems can respond and behave in certain circumstances | Helps in creating self-learning algorithms |
| 7 | Helps in finding optimal solution | Will go after the solution, without thinking much about the optimal solution |
| 8 | Leads to intelligence or wisdom | Leads to knowledge[28] |

*Source: Hackernoon*

According to IOSCO's Consultation Paper, five primary uses of Artificial Intelligence and Machine Learning amongst member countries were identified and herein summarized in figure 8 below;

**Fig 8: Primary Uses of AI and ML based on IOSCO's Consultation Paper – 2020**




*Source: IOSCO*

In addition to the uses of Artificial Intelligence and Machine Learning, the paper also provides an assessment of key challenges and oversight areas that interviewed industry participants had experienced in the implementation of Artificial Intelligence and Machine Learning offer technological solutions within the Capital Markets industry.

**Fig 9: Potential Risks Posed by Use of Artificial Intelligence and Machine Learning - IOSCO**

**Governance and Oversight**

- Firms **did not establisn new functions to address risks stemming from AI and ML** - still utilized existing risk control processes
- Firms **did not view technical expertise amongst senior management** as a crucial factor in the transition process

**Algorithm Dvpt, Testing and Monitoring**

- Most firms **did not have specific development and experimentation/testing frameworks** for the use of AI and ML.

**Data Quality Bias**

- Quality of the **data is very crucial as it determines the kind of output one is going to get** which in turn informs their decisions to be taken
- IOSCO's Fintech Network Committee identifed procedures for evaluating ethical use of AI and ML to include; i. Beneficence ii. Non-malfeasance iii. Human Anatomy iv. Justice and v. Explainability

**Transparency and Explainability**

- In order to promote transparency in firms, AI and ML algorithms should be easily understood by all the stakeholders such as regulators and clients.
- Regulators require extensive disclosures on all the firm's activities.

**Outsourcing**

- Most firms do not have the technical expertise on the use of AI and ML hence they resulted to outsourcing these services. Outsourcing these services comes with risks such as breach on data privacy, high risks of cyber-attacks and operational risks.

**Ethical Concerns**

- Firms should be careful to ensure that the outputs of the models do not discriminate anyone

[18]

The consultation paper was therefore developed to help its member countries address the referenced risks above for safer, efficient and stakeholder friendly implementation of Artificial Intelligence and Machine Learning solutions for the Capital Markets industry. Solutions forwarded for consideration by regulators are summarized below.

---

[18] i. **Beneficence**-The models should be done for the good of the investors and to promote integrity in the market ii. **Non-malfeasance**-Use AI and ML to identify any misconduct iii. **Human anatomy**-Humans should be in control of the model and restrict them on what they should do iv. **Justice**-Ensuring that there is accountability by senior management on any outcomes of the model and promoting transparency to all the stakeholders v. **Explainability**-The outcomes of the model can be explained extensively.

**Table 5: Proposed Solutions for AI and ML Implementation for Consideration by Regulators - IOSCO Consultative Paper 2020**

| | Proposed Measure | Risks to be Addressed | Actionable Points for Regulators |
|---|---|---|---|
| 1 | Introduction of a senior management position whose deliverables will be to oversee the development, testing, implementation and controls of AI and ML. | To promote accountability in the use of AI and ML and ensure robust oversight of the whole process from testing, deployment and monitoring stages. | -Require firms to have the following in place;<br>1. A deep understanding and technical expertise on how to utilize AI and ML and a clear understanding of the goal of the process.<br>2. Have in place robust control and governance frameworks including external models to ensure that the outcomes from AI and ML are thorough.<br>3. Have documented methodologies on the use of AI and ML and the whole business, which will be subjected to audits.<br>4. Evaluate whether the technology commensurate with the company's risk appetite, adherence to ethics and clients' risk tolerance. |
| 2 | Require firms to continuously test and monitor algorithms to verify results of AI and ML techniques. | -This will ensure that the model is refined and ready for use before it is dispensed to the live environment. | Require the Following<br>1. Testing should not be done in the live environment but instead in a secluded environment before the implementation of the technology. This ensures that AI and ML show their behavior for both stressed and unstressed market conditions and the techniques can function in a way that complies with the regulatory obligations.<br>2. After deployment, performance of the output from AI and ML should be evaluated on real time basis. A well tested "kill switch" functionality" should be introduced and key personnel should have access to it.<br>3. Involve Risk and compliance functions in the development and testing stages to ensure that the risks involved are weighed beforehand.<br>4. Due to possibility of drastic changes in the ML and AI behaviours companies should do an overhaul change of the traditional oversight and testing procedures to AI and ML oriented testing and monitoring procedures. |
| 3 | Require firms to have technical expertise and experience in the field of data science before they can embark on developing, testing, deploying, | To handle the issue of outsourcing and the risks that come with it. | 1. The firm's staff should have technical expertise and experience ranging from front line officers, risk management and compliance staff and the senior management.<br>2. Firms should deliberate on the possibility of having multi-disciplinary teams from all the functions of the business which will utilize this technology. |

| | | | |
|---|---|---|---|
| | monitoring and overseeing the use of AI and ML. | | 3. Have model continuity plans just in case one of the lead data scientists leaves the company. |
| 4 | Require firms to identify their outsourcing needs and how to manage the outsourced service providers and monitor their performance to ensure there is accountability. | Deal with the issue of over relying on outsourced services. | Firms should conduct initial and continuous due diligence of the third parties being onboarded.<br>Firms should have clear service level agreements and contracts which tackle the responsibilities, key performance indicators and the scope of the job of the third party.<br>Adhere to IOSCO principles on outsourcing whenever there is a need to outsource. |
| 5 | Regulators should determine the level of disclosures to be required from the firms both to their customers/clients and to the regulators. | -This will deal with the risks associated with transparency and explain ability. | Disclose sufficient information on the use of AI and ML to customers and clients to help them understand the implications on the Firm's products.<br>Use simple language that can be understood by the investors to facilitate them in making informed decisions. |
| 6 | Regulators should consider requiring firms to have robust controls that will ensure that the data utilized in AI and ML is of good quality and has no biases. | -This will address issues revolving around data quality of the models. | 1. Ensure that the sample taken is a true representation of the whole population and that the data is relevant, complete and of good quality. Additionally, firms should be very keen on their data sources.<br>2. Biases may occur in the process of collecting the data or in the way this data is handled. Firms should therefore ensure that the outputs of AI and ML and the data are evaluated to ensure there is no bias. |

*Source: IOSCO*

The International Organization of Securities Commissions (IOSCO) has exposed the consultation paper to stakeholder review with period of receiving feedback extended until **26th October 2020**. Thereafter, in the event the guidance is approved and implemented, anticipated benefits to regulators and Capital Markets industry participants will include the need to ensure that firms have in place appropriate and robust control frameworks that will cater for all the risks involved in transitioning from traditional algorithms to AI and ML algorithms.

**Management Review:**

- *Through its regulatory sandbox platform, the Authority has continuously advocated for technological innovations for Capital Markets players. As firms move towards digitizing most of their functions, it is anticipated that AI and ML based business solutions may be submitted for review by the sandbox review committee, to which the Authority intends to leverage on the outcome of the consultation paper developed by IOSCO in assessing key risk factors forwarded by AI and ML based algorithmic solutions.*

- *Further, and as forwarded by the Consultation Paper, the Authority will review its internal regulatory and supervision systems to ensure that such solutions are assessed based on the following factors: i. Extent of disclosures to clients and other stakeholders ii. Technical expertise of a firm and its staff iii. Need for testing of the models before implementation iv. Issues revolving around outsourcing these services from third parties v. The role of senior management and the level of accountability required from them and vi. Continuous monitoring of the AI and ML models vii. Documentation of all processes viii. Accuracy and unbiased data and ix. Cybersecurity.*

### 2.3.2 IOSCO publishes Good Practices on processes for deference

On 26th June 2020, the board of the International Organization of Securities Commissions (IOSCO) published a series of eleven good practices on processes for deference to assist regulatory authorities in mitigating the risk of unintended, regulatory-driven market fragmentation and to strengthen international cooperation[19].IOSCO defines deference[20] as "*the reliance that authorities places on one another as they regulate and supervise cross-border market participants*."

Deference procedures are considered essential as they assist in the formation of efficient capital flows globally, as regulatory authorities often seek to balance three important considerations; i. Facilitating market access to foreign market participants seeking to conduct business on a cross-border basis ii. Maintaining appropriate levels of investor protection and iii. Managing systemic risks[21].

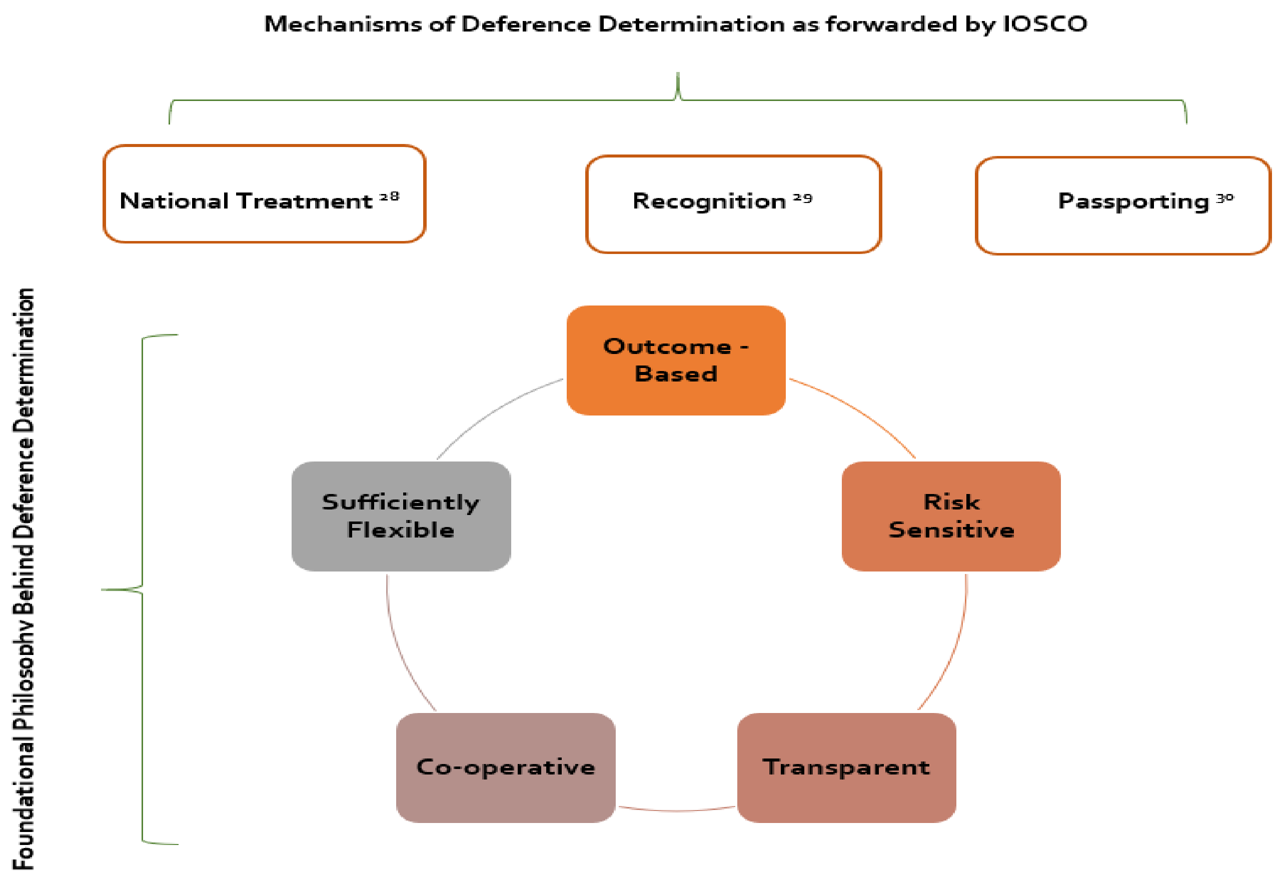
Over the years it has been noted that unintended market fragmentation has occurred among jurisdictions mainly because of revisions in most of the jurisdictions' regulatory frameworks after the global financial crisis in 2008.It is against this background that the IOSCO in its mandate has sought to address the issues of fragmentation and set the good practice of the deference process. Additionally, given that the IOSCO members defer to one another often the organization is obligated to give guidance on the process.

[19] https://www.iosco.org/news/pdf/IOSCONEWS572.pdf

[20] https://www.iosco.org/library/pubdocs/pdf/IOSCOPD629.pdf

[21] https://www.iosco.org/library/pubdocs/pdf/IOSCOPD659.pdf

**Fig 10: Dimensions of the Scope of IOSCO's Deference - Deference Determination and Foundational Philosophies**




*Source: IOSCO*

IOSCO's work on this exercise is dated back to 2013 when the G20 member nations stated that regulatory authorities should be able to defer among themselves when the regulatory framework should be able to defer to each other when it is justified by the quality of their respective regulatory and enforcement regimes, based on similar outcomes, in a non-discriminatory way, paying due respect to home country regulation regimes.

Since then, various taskforces have been established that have developed reports upon which the eleven good practices are anchored. The Eleven Practices provided for on deference by the IOSCO are herein summarized in table 6 below.

**Table 6: IOSCO's 11 Deference Good Practices**

| No | Area of Good Practice |
|---|---|
| 1 | Assessing authorities to consider the most appropriate arrangements for **ensuring transparency about their deference processes**. Authorities could consider publishing information and/or supplementing legislation in their jurisdiction where necessary, to give more clarity on the process. Issues for consideration include i. Steps in the assessment process; ii. Criteria and methodology that will form the basis for the deference determination iii. Scope of, and possible limitations, to a deference determination iv. Language of use as part of on-going communication and information-sharing v. High-level, indicative, timeframes towards which both parties will seek to work, to the extent practical and appropriate in the circumstances. |
| 2 | **Criteria for making an outcomes-based assessment** of the assessed jurisdiction /firm |
| 3 | When Authorities are making a deference determination, they could consider important factors such as the **nature and degree of risks that entities from another jurisdiction may pose to their markets** and/or market participants /investors. |
| 4 | Assessing Authorities could consider the most appropriate level of **engagement with the authority and/or firm in the assessed jurisdiction throughout the determination process**, such as facilitating regular check-in points with the view to ensuring the process remains on track. |
| 5 | Authorities in assessed jurisdictions or firms could in turn **consider how to engage constructively throughout the entire determination process and to cooperate fully with the assessing authority.** |
| 6 | If a full deference determination is not otherwise practical or appropriate, assessing authorities could **consider the appropriate scope of deference determinations**, depending on the overall outcome of their assessment. |
| 7 | Following an assessment, assessing authorities could **consider clarifying and providing feedback to the assessed jurisdiction or firm regarding the key facts and circumstances under which a deference determination has been decided** – including where this determination is negative |
| 8 | Authorities in assessed jurisdictions are encouraged to **consider sharing regulatory developments in their jurisdiction with the assessing jurisdiction through regular communication between regulatory Authorities**, if these developments may impact existing deference determinations. Authorities could also consider sharing relevant regulatory developments in international fora, where appropriate. |
| 9 | Assessing authorities are **encouraged to consider sharing developments in their regulatory framework which may lead to a review of their deference determinations** as early as possible to allow authorities in assessed jurisdictions to closely monitor these ongoing developments and act appropriately. |
| 10 | Where a deference decision may be revoked, within the scope of their competence and as appropriate, Authorities could consider: i. Putting in place processes to inform the assessed jurisdiction or firm and to consider any remedial action to the extent possible; and/or ii **Proposing other tools or measures instead of outright revocation or declining to renew a deference determination** or its parts, while the parties seek to remedy issues identified. |
| 11 | Once it has been decided to revoke a deference determination, authorities could consider appropriate steps to implement the revocation, including communications and notice to market participants in order to mitigate cliff-edge risks to investor protection, market integrity and financial stability objectives and allow for the smooth reorganization of market activities. |

*Source: IOSCO*

**Management Review:**

- *The Authority, as a member of IOSCO welcomes the prescribed good practices on deference, some of which have been referenced in reviewing applications from firms located oversees with different regulatory regimes in its responsiveness to foreign investor participation in the Kenyan market.*
- *Further, the Authority will review the practices as provided by IOSCO to align with this institution's domestic provisions and practices on deference to promote international cooperation and positioning Kenya as a destination of choice for foreign investors in the region.*
- *Management will ensure the new deference principles guide the operations of the regulatory sandbox, in the review of cross border applications provided for within the regulatory sandbox policy guidelines. Further, an assessment of application of IOSCO deference principles will be assessed against current practice to domesticate and comply to the greatest extent possible..*

## 2.4 Measures to Fast-Track Capital Raising /Listings

### 2.4.1 European Union Announces Launch of a Short-Term Prospectus for Listed Companies

As part of the European Union's Capital Markets Recovery Package, the EU announces on 24th July 2020, its proposal for a new type of short-form prospectus for companies that have a proven track record in the public market ('EU Recovery Prospectus'). The aim of the EU Recovery Prospectus is to enable companies' access new funding in a short time period to help with the economic recovery from the covid-19 pandemic. *It aims to help companies raise equity so that they can restore sustainable debt-to-equity ratios and become more resilient.*

It will be available for secondary offerings of shares and will only be available for 18 months. Incorporation of information by reference will be allowed and that information will not count in the maximum size of 30 pages. Key characteristics of the prospectus include i. It will be a single document of only 30 pages ii. Will have a two-page summary iii. Focuses purely on the essential information that investors need to make an informed decision and iv. Have minimum content requirements as summarized in table 7 below;

**Table 7: Minimum Information to be Included in the EU Recovery Prospectus**

| | Component |
|---|---|
| 1 | Name of the Issuer, Member State of incorporation, link to issuer's website |
| 2 | Responsibility Statement |
| 3 | Risk Factors |
| 4 | Financial Statements |
| 5 | Trend Information |
| 6 | Final Offer Price and amount of shares, including firm commitment from shareholders above 5% and names of the underwriters |
| 7 | Where and when to subscribe the shares |
| 8 | Reasons for the offer and use of proceeds |
| 9 | Working Capital Statement |
| 10 | Conflict of Interest |
| 11 | Shareholding after the issuance |

This simplified prospectus route will be available to issuers that have been trading on a regulated market or an SME Growth market continuously for at least 18 months and want to do a secondary offering of shares. The reduced disclosure in the prospectus is expected to reduce the cost of drawing up a prospectus and make the document easier to understand. It should also make review by the national competent authorities easier and so the prospectus approval period for these prospectuses will be reduced to 5 working days.

**Other proposed amendments**

The European Commission is also proposing the following amendments to the Prospectus Regulation that are intended to facilitate fundraising by banks.

i. **Supplementary prospectuses**

Financial intermediaries are currently required to inform investors of the possibility that a supplement to a prospectus will be published and, under certain circumstances, to contact investors on the same day that a supplement is published. The scope of investors to contact as well as the deadline in which to contact them has caused difficulties for financial intermediaries. The amendment clarifies their obligations. Financial intermediaries will only need to:

a. Inform those investors that have purchased and subscribed for securities through them of the possibility of the publication of a supplement, provided that the purchase or subscription was agreed between the time when the prospectus had been approved and the closing of the offer period or the time when trading on a regulated market had begun, whichever occurs later.
b. After publication of a supplement, contact those investors benefiting from a withdrawal right. The deadline for contacting them is extended to one working day from the publication of the supplement.

ii. **Withdrawal rights**

To safeguard investors, the period during which a withdrawal right can be exercised by investors is extended from two working days to three working days from the publication of the supplement.

iii. **Credit unions**

The threshold for an offer by a credit union of non-equity securities issued in a continuous or repeated manner without a prospectus will be raised from EUR 75 million to EUR 150 million. This measure will also only be temporary and available for 18 months.

This legislative proposal on amendments to the Prospectus Regulation is part of a set of measures to facilitate the economic recovery post-COVID-19 pandemic which also includes a legislative proposal amending MiFID II [22]and a legislative proposal amending the framework on securitization, including the Securitization Regulation8 and the Capital Requirements Regulation. 3 Main Features of the MIFD II amendments include;

- Level of information provided to clients, in particular professional clients such as large corporate and financial institutions, will now be more targeted to their needs. They will receive fewer automated mandatory disclosures. Information will no longer be provided on paper, except if retail clients specifically request so. Furthermore, investment firms will no longer have to perform certain types of assessments – called "product governance" – for certain types of products, since these products can be considered suitable for all types of clients, including retail clients.

- Changes to derivatives rules for which the underlying value is a commodity, such as gas or electricity.

[22] MiFID II sets out rules for investment firms that are active in the EU's financial markets. These rules dictate how investment firms should interact with investors and how they should organise the markets where the trading takes place.Main featured of the MiFID II amendments include;

These derivatives are important for companies whose primary business is in these commodities, in order to obtain cover against risks. The changes ensure that euro denominated EU commodity markets can grow so that the real economy is in a better position to shield themselves from future risks in commodity price movements. The changes will not affect agricultural commodity products, in particular products used for human consumption.

- Finally, rules guiding the provision of research on small and mid-cap companies and on fixed income instruments will be partially revisited. The e exceptional circumstances resulting from the coronavirus pandemic have instilled a sense of urgency into the debate on investment analysts' research. Increasing the visibility of European companies, in particular SMEs, to investors will promote more investment for the economic recovery.

- This legislative proposal also aims to complement the objectives of the Capital Markets Union to diversify market-based sources of financing for companies. By making it easier for companies listed in the EU to issue shares, this initiative would contribute to facilitating capital-raising by companies. In this regard, this proposal would be in line with the recommendation of the High-Level Forum on the Capital Markets Union10 published on 10 June 2020 that highlighted the need to alleviate listing rules, also referring to the Prospectus Regulation. The changes to the Prospectus Regulation will, once in force, be directly applicable in Member States. If brought into force before the end of 2020, the changes will also be directly applicable in the UK. Under the European Union (Withdrawal) Act 2018, the amended Regulation will continue to apply in the UK after the transition period ends and we would anticipate that the UK will issue a statutory instrument to amend the Regulation so that it will work in a UK context.

**Management Review:**

- *Management is continuously reviewing its strategic regulatory interventions for the Capital Markets informed by regulatory gap assessments conducted over the years. Like other responsive regulators, the Authority has embarked on a process of reviewing some of its key regulatory provisions in line with best practice aimed at promoting the Capital Markets as a solution to capital access by economic agents.*
- *In the current financial year, the Authority is undertaking a review of its public offers regulations as well as regulations for Collective Investment Schemes aimed at making regulatory provisions of the Capital Markets more competitive and favorable for the industry. While this process begun in the last financial year, management plans to use this opportunity to equally incorporate any new amendments or ideas that the market may share as part of its regulatory response to the effects of the Covid-19 pandemic to market operations.*

## 2.5 Fiscal. Monetary and Capital Market Interventions in the Covid – 19 Era during the review Period

**Table 8: Measures Taken By Governments, Central Banks and Financial Sector Regulators to boost mitigation against impact of Covid-19 during the Quarter in Select Jurisdictions**

| Jurisdiction | Fiscal interventions | Monetary Interventions | Capital Markets Interventions |
|---|---|---|---|
| **United Kingdom** [23] | • Tax and spending measures to support households and families during the health emergency which include<br>1. Additional funding (£48.5 billion) for the National Health Service, public services and charities;<br>2. Strengthening the social safety net to support vulnerable people (by £8 billion) by increasing payments under the Universal Credit scheme as well as expanding other benefits. | • The Monetary Policy Committee (MPC) voted unanimously to maintain bank rate at 0.1 per cent.<br>• The Monetary Policy Committee (MPC) voted unanimously for the Bank of England to continue with its existing programmes of UK government bond and sterling non-financial investment-grade corporate bond purchases, financed by the issuance of central bank reserves, maintaining the target for the total stock of these purchases at £745 billion. | • Considering the amendments to the Capital Requirements Regulation (CRR) in response to the Covid-19 outbreak (the CRR 'Quick Fix') the Prudential Regulatory Authority(PRA) has decided to terminate its temporary approach to Value At Risk (VAR) back-testing exceptions from September 30, 2020. From October 1, 2020 onwards, firms should no longer apply any commensurate reduction in Reduction in risks- not- In Variance (RNIV) capital requirements.<br>• Financial Conduct Authority (FCA) announced temporary relief for issuers who choose to use the amended International Financial Reporting Standard (IFRS) 16 during the Covid-19 pandemic and its aftermath. |

[23] https://www.gov.uk/government/collections/financial-support-for-businesses-during-coronavirus-covid-19
https://www.bankofengland.co.uk/coronavirus
https://www.bankofengland.co.uk/prudential-regulation/publication/2020/var-back-testing-exceptions-temporary-approach
https://www.bankofengland.co.uk/-/media/boe/files/monetary-policy-report/2020/august/monetary-policy-report-august-2020

| Jurisdiction | Fiscal interventions | Monetary Interventions | Capital Markets Interventions |
|---|---|---|---|
| **China** [24] | • An estimated RMB 4.6 trillion (or 4.5 percent of GDP) of discretionary fiscal measures have been announced which includes;<br>1. Increased spending on epidemic prevention and control;<br>2. Production of medical equipment;<br>3. Accelerated disbursement of unemployment insurance and extension to migrant workers;<br>4. Tax relief and waived social security contributions; and<br>5. Public investment. | | • Chinese regulators vow to expand stock connect in further market opening. |
| **Singapore**[25] | • The Authorities have announced several measures since February to August amounting to about S$100 billion which includes Support to households, businesses, cover rental costs, enhancement of financing schemes, and additional support for the self-employed and industries most directly affected (aviation, tourism, construction, transportation, arts and culture).<br>• The Authorities have increased their contingencies funds for unforeseen expenditure needs and set | • On July 29 2020, the Monetary Authority of Singapore (MAS) called on locally incorporated banks headquartered in Singapore to cap their total dividends per share to 60 percent of the FY2019 level and offer shareholders the option to | |

[24] https://www.unescap.org/sites/default/files/China_COVID%20Country%20profile%20280820.pdf
[25] https://home.kpmg/xx/en/home/insights/2020/04/singapore-government-and-institution-measures-in-response-to-covid.html

| Jurisdiction | Fiscal interventions | Monetary Interventions | Capital Markets Interventions |
|---|---|---|---|
| | aside loan capital of S$20 billion to help businesses and individuals facing cash flow challenges with loan obligations and insurance premium payments. | receive dividends in scrip (as shares) instead of cash.<br>• On Aug 7, 2020 MAS urged Finance companies incorporated in Singapore to also cap their total dividends per share for FY2020 at 60 percent of FY2019's level.<br>• On September 3, 2020, the MAS announced measures to enhance the banking system's access to Singapore dollar (SGD) and US dollar (USD) funding effective September 28, 2020. A new MAS SGD term facility will offer SGD funds in the 1-month and 3-month tenors, complementing the existing overnight MAS Standing Facility. | |

Source: Various

**Management Review:**

- *As expected in major period of crisis as in the covid-19, the role of Government in charting a favorable economic environment in spite of the challenges that arise has remained critical for majority of economies globally through fiscal and monetary policy interventions that seek to reduce the rate at which expected losses accrue in different sectors.*
- *Within the Capital Markets industry, regulators across different jurisdictions have used this period to revise some of the regulations considered restrictive for licensees in a bid to increase liquidity positions of companies to promote business continuity. The UK's initiatives in making amendments to Capital Requirements Regulations , European Union's provision for short term prospectus and IOSCO's great involvement in the development of guidelines and reports on AI and Machine Learning and Deference Good Practices , are all aimed at making Capital Markets more attractive for capital raising.*
- *The Authority, like other responsive regulators has engineered significant regulatory reforms aimed at making the Capital Markets a preferred choice of raising capital and investment by issuers and investors alike. Some key initiatives being undertaken currently include i. Complete overhaul and review of Collective Investment Scheme Regulations, 2001 and ii. Review of the Capital Markets (Securities)Public Offers Listing & Disclosures) Regulations 2002. Others include development of a whistleblower regulations and regulations on Self-Regulatory Organizations.*

## 3.0 Regional and Sub Saharan Africa Developments

### 3.1 The Financial Services Commission (FSC) Mauritius issues the Financial services (Peer to Peer Lending) Rules 2020

On 31st August 2020, the Mauritian Financial Services Commission (**FSC**) published the licensing criteria for Peer-to-Peer ("**P2P**") lending. Prior to this, P2P Operators were operating under the regulatory sandbox licensing. Peer-to-peer lending (P2P lending) is the practice of lending money to individuals or businesses through online services that match lenders with borrowers. P2P lending companies often offer their services online and attempt to operate with lower overhead and provide their services more cheaply than traditional financial institutions.

As a result, lenders can earn higher returns compared to savings and investment products offered by banks, while borrowers can borrow money at lower interest rates, even after the P2P lending company has taken a fee for providing the match-making platform and credit checking the borrower.

The Rules provide for a sound and efficient regulatory environment to support the offer and execution of Peer to Peer lending for the benefit of stakeholders in the non-bank financial services sector of Mauritius. A P2P operator, under these Rules, will facilitate access to finance by matching borrowers and lenders on its online platform[26].

According to Lexology September 2020 report, a P2P operator will consider a request to borrow from any person provided that the funds being sought by the person are applied for to finance a project. The P2P website will prominently disclose a description of the borrowers' project and funds will be made available to borrowers only after the required total funding has been pooled or raised for any

[2626] https://www.btg-mauritius.com/index.php/component/content/article/79-blog/179-fsc-mauritius-issues-the-financial-services-peer-to-peer-lending-rules-2020?Itemid=437 project. This means that if the borrower does not obtain 100% of the funds, it does not get any of the money.

Once a lender agrees to provide funds in its own name, the lender and the borrower enter into an agreement through a P2P lending platform operated by a P2P operator. P2P operators must provide a cooling off period of two business days to borrowers and lenders during which they may cancel their written agreements without the imposition of any penalty[27].The rules provide for limits and restrictions of P2P lending for the borrower, lender and P2P operator summarized in table 10 below;

**Table 9: Limits and Restrictions of P2P Lending for Players in Mauritius – 2020**

| Borrower | Lender | P2P Operator |
|---|---|---|
| The following entities cannot apply for a P2P lending licence:<br><br>i. A collective investment scheme and closed-end fund, as defined in the Securities Act 2005.<br>ii. A public listed entity or any of its subsidiaries.<br>iii. A person that proposes to access a P2P lending platform for further lending to other persons; and<br>iv. Any other scheme as may be determined by the FSC. | The activities of a lender on a P2P lending platform must exclude deposit taking business, in any form. | P2P operator has no carte blanche (*complete freedom to do something*) in regard to the activities it can undertake on the P2P lending platform. It is restricted from carrying out the following activities in **its own name**:<br><br>• Deposit taking business, in any form;<br>• Lending; and<br>• Providing or arranging for any credit enhancement or guarantee. |

Source: Lexology

Specific limits on amounts which apply to lenders and borrowers whenever they transact through P2P Operators are also provided for and summarized in table 10 below.

27 https://www.lexology.com/library/detail.aspx?g=99571839-2a01-4c3f-82ba-061a9407c444

**Table 10: Specific Limits on P2P Lenders and Borrowers**

| Category | Limits | Kshs Equivalent of Limits [28] |
|---|---|---|
| Borrower who is a natural person | Maximum aggregate of MUR[29] 1 million with a minimum of MUR 50,000 | Max – **Kshs. 2,721,007**<br>Min – **Kshs. 136,050** |
| Borrower who is a legal person | Maximum aggregate of MUR 3 million with a minimum of MUR 50,000 | Max – Kshs. **8,163,022**<br>Min - Kshs. **136,050** |
| Lender who is a natural person | Maximum aggregate of MUR 1.5 million | Max – Kshs. **4,081,511** |
| Lender who is a legal person | Maximum aggregate of MUR 3 million | Max – Kshs. **8,163,022** |

*Source: Financial Services Commission Mauritius*

This limit does not apply to sophisticated investors (as defined in the Securities Act 2005) when they lend in any other currency through P2P operators to borrowers that are not resident in Mauritius. It is to be noted that the reimbursement period for the lending through P2P lending platforms must not exceed 84 months. The rules also provide an exhaustive list of obligations that the P2P operator has to fulfil summarized in table 11 below.

**Table 11: Obligations of a P2P Operator - Mauritius P2P Rules**

| | Status | Incorporated in Mauritius and Licensed by the FSC |
|---|---|---|
| 1 | **Stated Capital** | Minimum unimpaired stated capital of MUR 2 Million or its equivalent in any other currency or such higher amount as the FSC may determine |
| 2 | **Board of Directors** | Minimum of 3 directors, one of whom must be an independent director and a resident of Mauritius |
| 3 | **Branch** | May establish a branch outside Mauritius with approval from the FSC |
| 4 | **Shareholder** | A bank cannot be a shareholder unless approved by the FSC |
| 5 | **Insurance** | Must maintain, at all times, a professional indemnity insurance cover commensurate with the nature and scope of its activities |
| 6 | **Office** | Establish an office and have in place relevant information technology infrastructure for carrying out of its business activities with Mauritius |
| 7 | **Escrow Account** | Is required to establish escrow account arrangements with a licensed financial institution in Mauritius in order to facilitate the transfer of funds between lenders and borrowers through which the P2P lending platform will transact. |

[28] Conversions based on Kshs: Mauritian Rupee Exchange Rates for 24th September 2020
[29] Mauritian Rupee

| | | |
|---|---|---|
| 8 | **Consent of Borrowers** | Must obtain consent of borrowers for the purpose of ascertaining their credit profiles from a credit information bureau and upon the grant of funds to the borrowers, forthwith provide particulars of the borrowing to the credit information bureau as may be required |

Source: Lexology

**Management Review:**

- *The increasing growth of technological innovations within the Capital Markets industry has called for flexibility and responsiveness amongst regulators in supporting further growth of such innovations. One key area that has attracted increased regulatory concerns is crowdfunding. In the last quarter, Nigeria launched its crowd funding rules and guidelines in addressing the demand and need of the same within its jurisdiction with Mauritius following closely in the quarter under review.*
- *As a proponent of innovation and through its regulatory sandbox, the Authority has remained supportive in encouraging technological solutions for the industry with firms admitted to the regulatory sandbox standing at 7 as at end September 2020.*
- *Further, to anchor the innovations within a regulatory framework, the Authority has developed a policy framework for the establishment of crowdfunding (P2P being a component ) that has formed the basis for the development of a regulatory framework to facilitate crowdfunding as a capital markets product. Industry players are encouraged to share their thoughts and feedback in the process of developing the framework in line with the constitutional provisions on public participation.*

## 3.2 Ethiopia's Draft Capital Markets Bill to establish a Capital Markets Authority for the East African State

On 21st September 2020, The National Bank of Ethiopia (NBE), the central bank, published a draft Capital Markets Establishment Proclamation for consultation also known as Ethiopia's draft Capital Markets Bill. The bill proposes setting up of a Capital Market Authority regulator with a wide mandate, including promoting the development of capital markets by removing impediments and creating incentives.

It will also have the usual regulatory functions of ensuring a system for orderly, fair, efficient and transparent issuance and trading in securities, protecting investors and reducing systemic risk. Upon its establishment, the Authority will decide when to give a license for the establishment of an Ethiopian Securities Exchange.

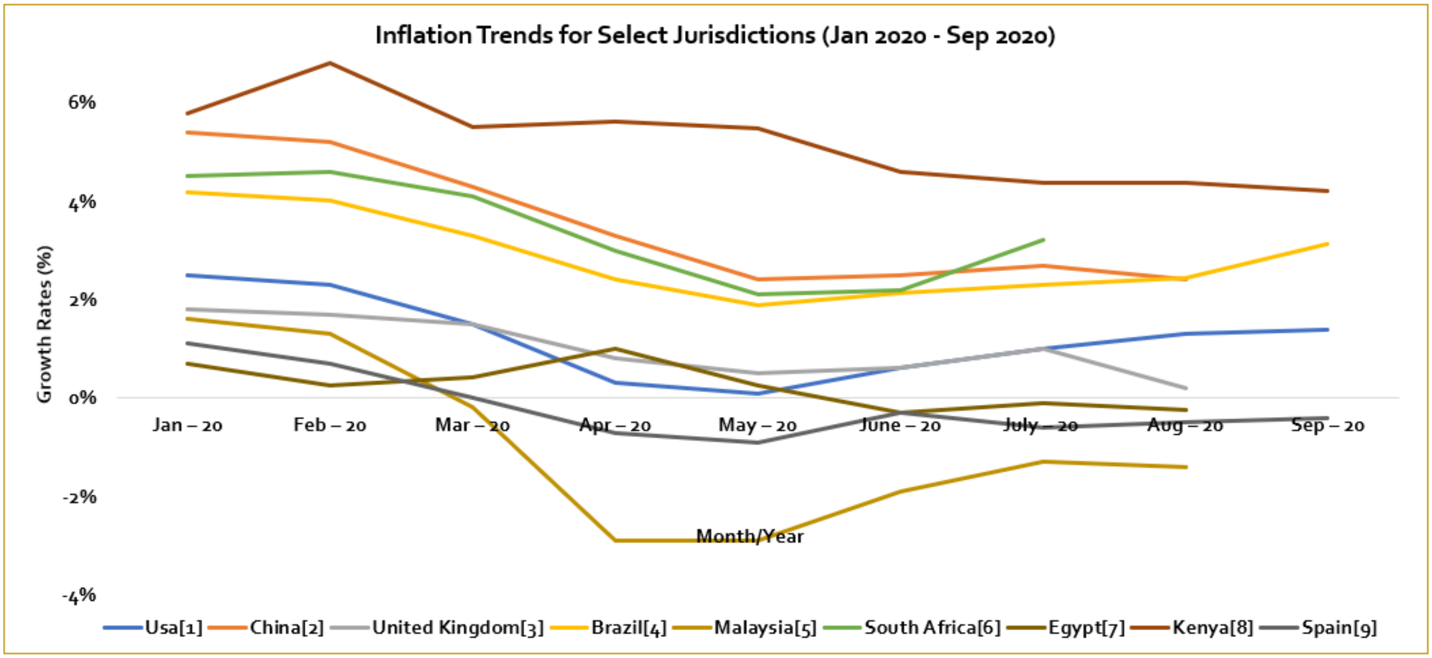
The bill gives provision for the Exchange to provide a trading platform for equities, debt securities, derivative instruments, units in a collective investment scheme, real estate investment trusts (REITs), currency exchange contracts and other products to be declared by the Authority's directive. On ownership, the Government of Ethiopia will be a minority shareholder in the Ethiopian Securities Exchange with a target of 5%-25% of the shareholding. Corporations, capital market intermediaries and international securities exchange operators are expected to hold 25%-55% and individuals 20%-40% of the shares.

The aim is that foreign investors should not own over 25% of the shares. However, if no-one wants to invest in owning a stock exchange, then Government could own 100%.

## 3.3 Comparative Analysis on Performance of Key Indices Across Jurisdictions

### 3.3.1 Inflation Trends

**Fig 11: Comparative Jurisdictional Inflation Trends (Jan 2020 - Sep 2020)**




*Source: Statista/Trading Economics; *Missing Data for SA, UK and Malaysia for the month of August 2020; Brazil data is as at May 2020.*

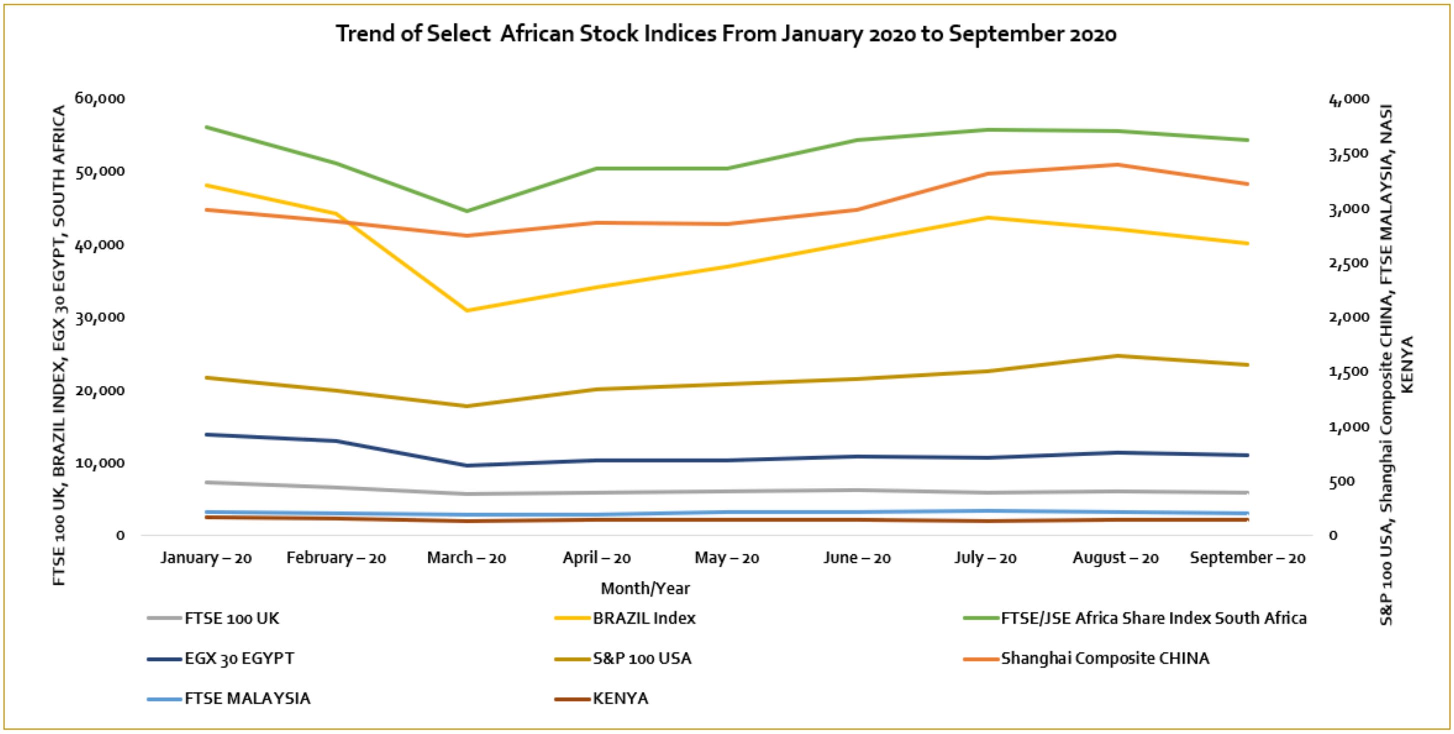
A comparative analysis of inflation across select jurisdictions shows a relatively stable inflation rate compared to other jurisdictions such as Egypt and Malaysia that recorded significant month on month deviations in inflation rates between January 2020 and July 2020. Malaysia recorded the biggest decline in its inflation rate in a decade in April 2020 on the back of weaker transport prices amid nationwide movement restrictions in the face of Covid-19 environment.

**Management Review:**

- *Inflation trends in 2020 across jurisdictions as observed in figure 9 have seen countries record very inflation levels with countries such as Egypt and Spain, recording negative inflation levels, also known as deflation, and the USA having a near miss in the month of May 2020. Persistent period of deflation often results in decreased economic growth and activity as deflation increases the real value of debt – and therefore reducing the spending power of firms and consumers. In the long run, this leads to economic stagnation and high unemployment.*
- *Kenya's inflation levels have remained positive in the face of the covid-19 pandemic with the country recording a ten-month low of 4.36 percent in August of 2020, unchanged from July 2020.*
- *However, within the review period, most countries have experienced greater stability in key macroeconomic indices including inflation with the trend expected to be sustained to the end of the year as more positive news emerges on the potential of having a covid-19 virus in the coming months leading to December 2020 in some countries, Kenya included.*

### 3.3.2 Trend of Performance of Stock Indices Across Select Jurisdictions

**Fig 12: Comparative Review of Stock Indices of Select Jurisdictions (Jan 2020 - Sep 2020)**




*Source: World Federation of Exchanges/* https://www.african-markets.com/en/stock-markets/use

A comparative analysis of stock indices across select jurisdictions generally surged during the review period as investors cheered positive news of a potential COVID-19 treatment, economic stimulus, and reopening of various economies. As the election season in United States moves into high gear as November draws near, majority are keen to see whether and how the uncertainty about the US elections would be reflected in the stock market. However, the past performance in stock markets during electioneering period is no guarantee of future results, therefore, election in November is anticipated to have some impact on the global economy, business environment, and geopolitics in general.

## 4.0 Domestic Market Developments

### 4.1 UFAA begins transfer of unclaimed shares to a central depository account

In August 2020, the Unclaimed Financial Assets Authority (UFAA) Kenya announced a move to collect over 800 million units of unclaimed shares that remained uncollected by owners and beneficiaries to the Unclaimed Assets Trust Central Depository Account. Reported unclaimed shares have been in the custody of reporting institutions on instructions from the Authority[30].

The Unclaimed Assets Authority has since obtained a non-trading central depository agent license making it possible to now hold all unclaimed shares in one account. The Authority has encouraged owners and beneficiaries to continue checking with their holders and (or) registrars if their assets have been deemed unclaimed.

Currently, UFAA is in custody of Kshs.16.7 billion in cash, 1,592 safe deposit boxes and assorted unit trusts. The Authority requires holders of the assets to surrender unclaimed assets including cash in a bank, dividends, shares, insurance policies, money order, Court refunds, assets held in a fiduciary capacity, unpaid wages, safe deposit boxes, cheques, drafts or similar instruments. They also include deposits for utility services including mobile money or matured retirement benefits. Reporting and surrender unclaimed financial assets by all holders is mandatory and is due on or before November 1 every year.

### 4.2 Setting up of Warehouse Receipt Council

In July 2020, the Cabinet Secretary unveiled the Warehouse Receipt Council to oversee the operations of the Warehouse Receipt System in Kenya. This followed the ascent of the Warehouse Receipt System (WRS) Act assented in June 2019 by the President[31], setting the stage for Kenya to adopt a WRS for agricultural commodities that have been successfully used in jurisdictions such as Ethiopia and South Africa. As guided by the Act, members of the Council are drawn from various sectors and players in the commodities value chain as well as representation from both the National and County governments. Key members include the Chairperson to be appointed by the President, a nominee from the Council of Governors, a representative of the body representing warehouse operators alongside nominees from the Eastern Africa Grain Council and Kenya Bankers association[31]. The Act provides the role of the Council to include ;

i. Facilitating the establishment, maintenance and development of the Warehouse Receipt System for agricultural commodities produced in Kenya.
ii. The development and implementation, in conjunction with relevant Government agencies, an efficient commodity grading and weighing system that ensures quantity and quality assurance and facilitate the enforcement of commodity standards necessary for the warehouse receipting system.
iii. Overseeing the functioning of the Warehouse Receipt System to ensure the efficiency, effectiveness and integrity of the system.

30 https://portal.ufaa.go.ke/frontend/web/index.php/page/press

31 http://kenyalaw.org/kl/fileadmin/pdfdownloads/Acts/2019/TheWarehouseReceiptSystemAct_No._8of2019.pdf

iv. Establishing and maintaining a central registry for the management of warehouse receipt transactions under the Act.

v. Monitoring and overseeing the issuance, suspension or revocation of registration or licenses issued under the Act

**Fig 13: Warehouse Receipt System Model**


*Source: Zimbabwean Herald*

With the formation of the Council, the implementation and operationalization of the Warehouse Receipt System can now be started.

The Warehouse Receipt System (WRS) is defined as "*part of the whole of the process of depositing commodities in a licensed warehouse, the issuance of a warehouse receipt reflecting the quantity and quality of the deposited commodity, the management of the transfer of the receipts as a document of title and includes the regulation of warehouses and actors associated in the processes*"[32]

**Management Review:**

- *The WRS provides a platform for farmers to access financing from credit providers with the Warehouse Receipt, a legal document of title, acting as Security. The agricultural sector in Kenya contributes well above 25% of the GDP. Access to credit would further cement the role of Agriculture in the economy. In addition to this the Movable Property Security Rights Act No. 13 of 2017, which prescribes the use of movable property to be used as collateral for credit facilities further sets out how a creditor (in this case, a bank) can exercise their rights in case of default by the debtors (small scale farmers)*[33]
- *The Warehouse Receipt System also provides a chance for farmers to store their produce in the designated warehouses and sell at opportune times when the prices are favorable. This process can be re-enacted from season to season allowing farmers to make profits and at the same time ensure a steady supply of commodities to the market. As a result, stable prices for commodities are attained*[34].
- *With Warehouses using accreditation facilities of the Kenya Bureau of Standards (KEBS) as well as weight measurement certifications in accordance to the Weights and Measures Act, market participants including bulk traders and lenders are assured of the high quality of products which are standardized*[35]

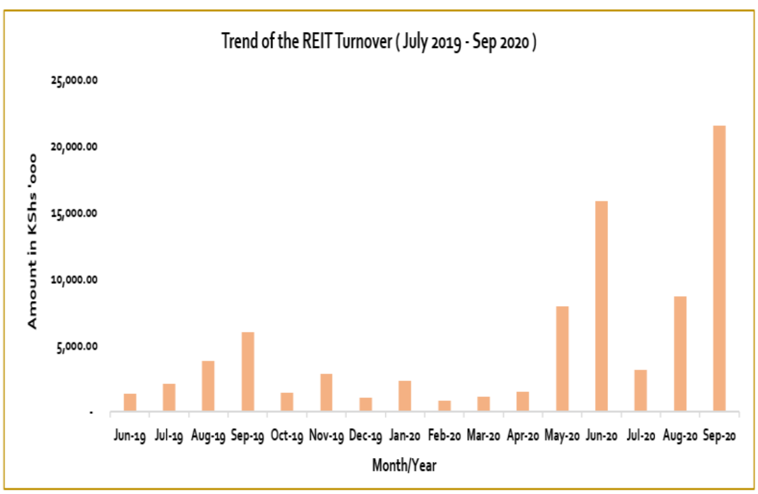
[32] http://cga.co.ke/2019/07/30/warehouse-receipt-system-kenya/
[33] https://mman.co.ke/content/warehouse-receipt-system-bill-2018-what-it-means-agribusiness-and-financing-kenya-0
[34] https://www.ifc.org/wps/wcm/connect/news_ext_content/ifc_external_corporate_site/news+and+events/news/how+warehouse+receipts+can+improve+lives
[35] https://kilimonews.co.ke/agriculture-policy/warehouse-receipt-system-council-inaugurated-by-agriculture-cs-peter-munya/

### 4.3 Favorable Performance of Alternative Asset Classes Listed at the NSE – REITs and ETFs

On the back of the current coronavirus pandemic, many investors have opted to diversify into alternative investment classes that would protect the value erosion that is currently being experienced in the plain vanilla investments such as equities. The REITs market saw increased turnover during the quarter, recording a REIT turnover value of Kshs. 33.31 Million, a 32.45% increase compared to Kshs. 25.15 Million recorded in Q2 (April – June ) 2020. The covid 19 environment called for diversification of investments amongst investors leading to increased investments in the listed REIT.

The REITs market also remains lucrative due to the exemption from income tax as stipulate in Section 20 of the Income Tax Act. In this regard, the Authority recently drafted and circulated the draft Income Tax (Real Estate Investment Trusts) Rules, 2020 and exposed the same to the public. The regulations are meant to operationalize section 20(c) and (d) of the Income Tax Act on exemption of REITs.

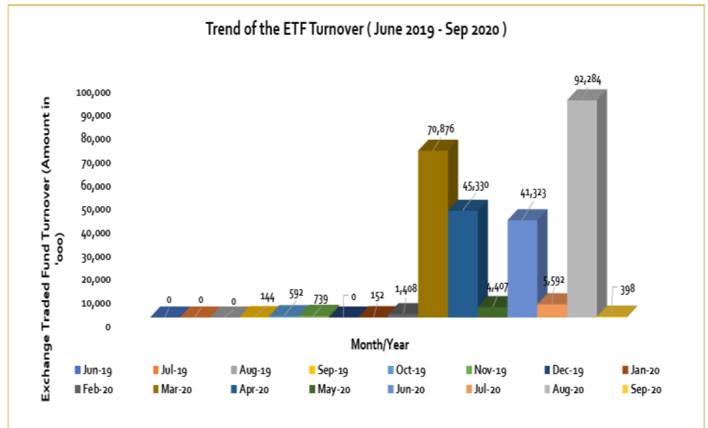
**Fig 14: Trend of Performance of Real Estate Investment Trusts in Kenya (July 2019 - Sep 2020)**




*Source: CMA/NSE*

Similarly, the listed new gold ETF recorded improved performance quarter as an ETF turnover value of Kshs. 98.27 Million was recorded in Q3(July – Sep) 2020, a 7.92% increase from Kshs. 91.06 Million recorded in the previous quarter.

**Fig 15: Trend of Performance of Exchange Traded Fund in Kenya (June 2019 - Sep 2020)**



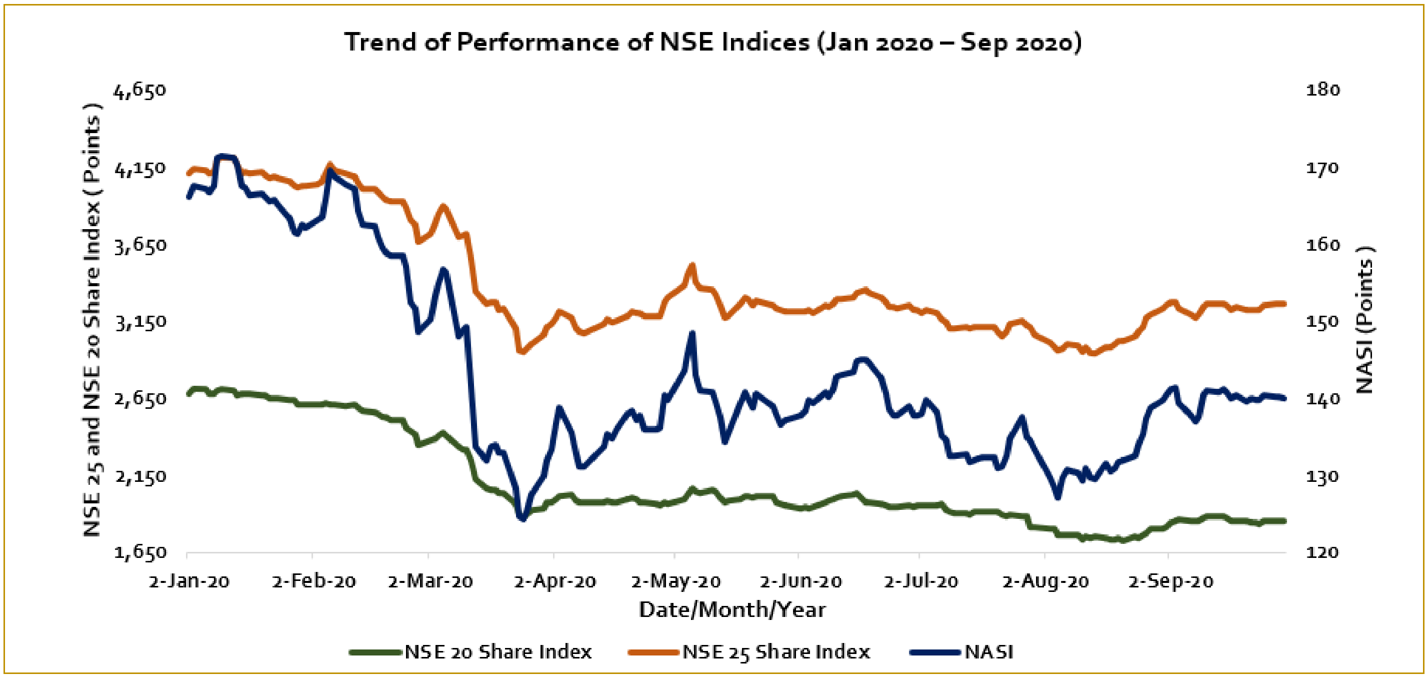

*Source: CMA/NSE*

**Management Review:**

- *Alternative asset classes such as the listed REIT and ETF at the Nairobi Securities Exchange have performed favorably in the face of Covid-19. The Listed ETF that is gold backed recorded active trading between April and July 2020 as increased cushioning from losses resulting from traditional equities is sought for by investors.*
- *Advocating of the REIT product as an alternative financing source for developers at a time when conventional lenders like banks have reduced their loan book exposure in sectors such as construction and hospitality due to the inflated risk brought about by the spread of coronavirus. Furthermore, the income tax exemption is expected to make the product more attractive for local investors.*

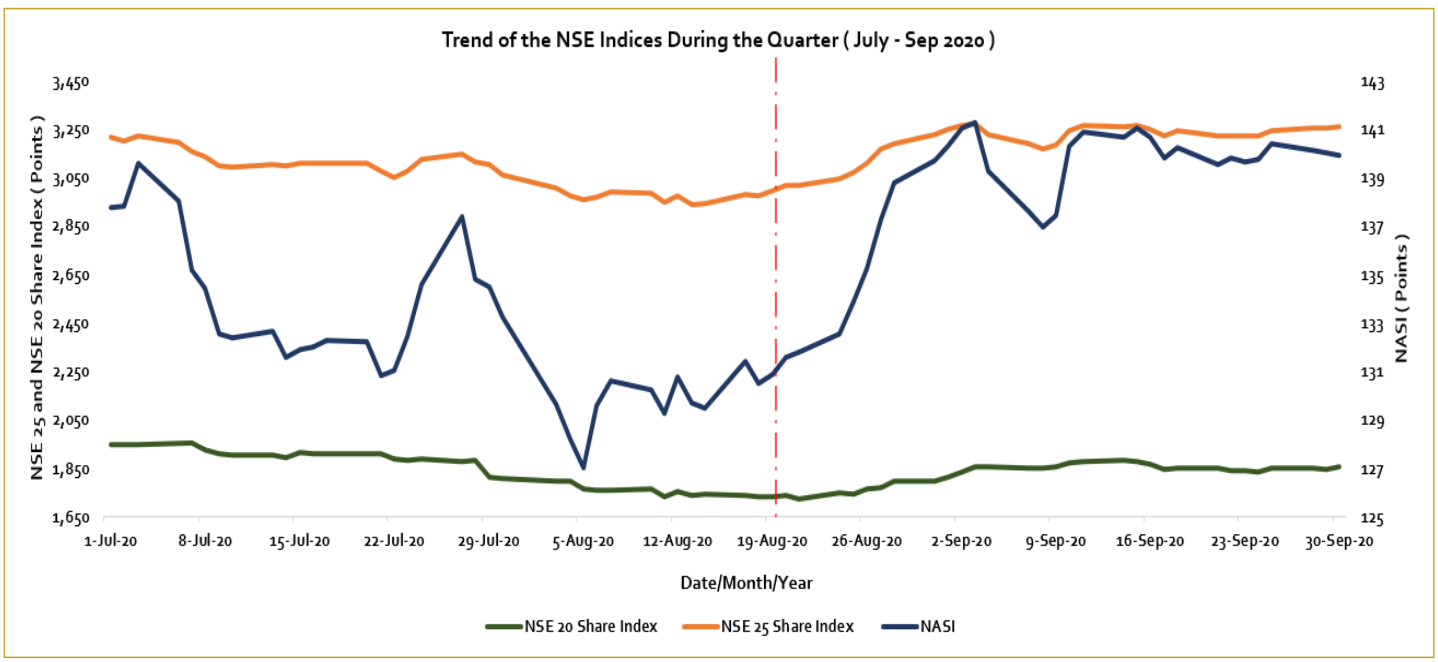
## 4.4 Summary Performance of Key Performance Metrices in the Domestic Economy

Fig 16: Trend of Performance of NSE Indices ( Jan 2020 - Sep 2020 )



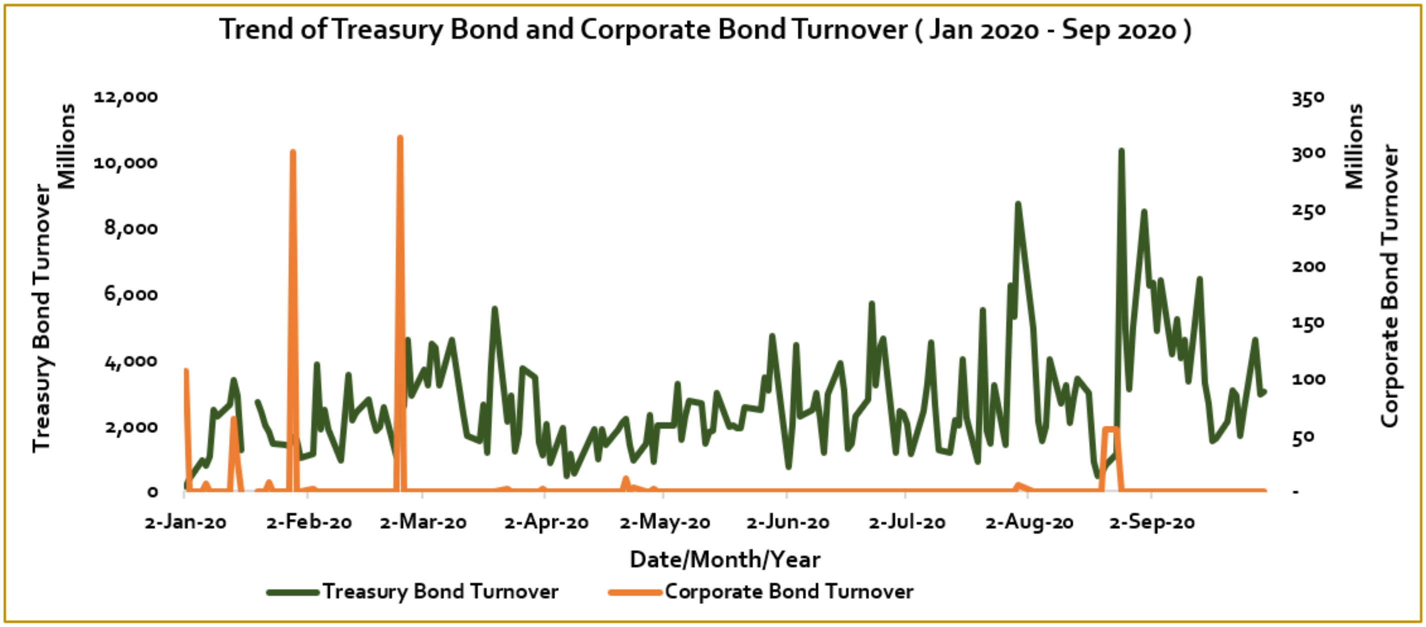

*Source: CMA/NSE*

Fig 17: Trend of Performance of NSE Indices During the Quarter (July - Sep ) 2020




*Source: NSE/CMA*

**Fig 18: Trend of Performance of Treasury Bond and Corporate Bond Turnover (Jan 2020 - Sep 2020 )**




*Source: CMA/NSE*

## 4.5 Bond Market Performance and Stability

### 4.5.1 Treasury Bond Market

In the primary treasury bonds market, a quarterly analysis indicates that during Q3. 2020, Seven (7) Treasury bonds were issued. In issuing these bonds, the government sought to raise KShs. 180 Billion but received subscriptions worth KShs. 364.92 Billion.

In the end, however, it accepted bonds worth KShs. 223.67 Billion, indicating a 61.29% acceptance rate. Further, there was a tap sale during the quarter seeking to raise Kshs 40 billion from the market. However, bids received amounted to Kshs 40.26 billion, with the government accepting Kshs 41.01 billion.

**Table 12: Treasury Bond Performance (Jan - Sep 2020)**

| | BOND | Amt Issued (Kshs. Bn) | Amt Received (Kshs. Bn) | Amt Accepted (Kshs. Bn) | % AA/AI | % AR/AI |
|---|---|---|---|---|---|---|
| Jan 2020 | FXD 1/2019/5 | 50.00 | 44.52 | 44.49 | 88.98 | 89.04 |
| | FXD 1/2019/10 | | 25.43 | 19.26 | 38.52 | 50.86 |
| | FXD 1/2020/15 | 50.00 | 18.44 | 5.19 | 10.38 | 36.88 |
| Feb 2020 | FXD 1/2018/25 | | 24.06 | 22.68 | 45.36 | 48.12 |
| Mar 2020 | FXD 1/2018/20 | 50.00 | 19.82 | 8.27 | 16.54 | 39.64 |
| | FXD 1/2018/25 | | 15.34 | 14.64 | 29.28 | 30.68 |
| April 2020 | IFB1/2020/9 | 60.00 | 68.41 | 39.01 | 65.02 | 114.02 |
| | Tap Sale | 21.00 | 37.84 | 35.39 | 168.52 | 180.19 |
| May 2020 | FXD1/2020/5 | 50.00 | 34.53 | 20.78 | 41.56 | 69.06 |
| | FXD1/2020/5 | 30.00 | 20.58 | 8.95 | 29.83 | 68.6 |
| June 2020 | IFB1/2020/6 | 25.60 | 21.16 | 19.28 | 75.31 | 82.66 |
| | FXD3/2019/5 | 40.00 | 60.89 | 16.53 | 41.33 | 152.22 |
| | FXD4/2019/10 | | 44.25 | 32.80 | 82.00 | 110.62 |
| July 2020 | FXD1/2020/05 | 60.00 | 65.34 | 9.34 | 15.57 | 108.90 |
| | FXD2/2018/10 | | 55.49 | 21.27 | 34.45 | 92.48 |
| | FXD1/2019/15 | | 60.95 | 50.24 | 83.73 | 101.58 |
| | Tap Sale | 40.00 | 40.26 | 41.01 | 102.53 | 100.65 |
| August 2020 | IFB1/2020/11 | 70.00 | 101.47 | 78.64 | 112.34 | 144.96 |
| Sep 2020 | FXD2/2010/15 | | 17.84 | 11.02 | 22.04 | 35.68 |
| | FXD1/2020/15 | 50.00 | 49.79 | 45.69 | 91.38 | 99.58 |
| | FXD1/2011/20 | | 14.04 | 7.47 | 14.94 | 28.08 |

**Table 13: Summary of Annual Treasury and Corporate Bond Turnover**

| | Treasury Bond Turnover (Kshs Bn) | Corporate Bond Turnover (Kshs Bn) | Total Bond Turnover (Kshs Bn) |
|---|---|---|---|
| **2019** | 545.83 | 2.77 | 548.78 |
| **2020** | 521.69 | 0.81 | 522.50 |

*Source: CMA/NSE*

In the secondary bonds market, during the first nine months of 2020, bond market turnover decreased by 4.79 per cent with KShs.522.50 Billion worth of bonds traded compared to Kshs.548.78 Billion traded in the same period for the year 2019. A further comparison of bonds market, treasury bond turnover accounted for 99.84 per cent.

#### 4.5.2 Corporate Bond issues

The Corporate bond market has been relatively dry. A resolution of the issues in the bonds market to address the issues of insolvency especially for bonds that have not been listed would go a long way in instilling confidence in corporate bond markets.

## 4.5 Performance of Equity Markets

**Table 14: Summary of Equity Markets Performance**

| Year | Month | Equity Turnover ( Bn) | Share Volume (Mn) | NASI | NSE 20 Index | NSE 25 Share | Market Cap ( Bn) |
|---|---|---|---|---|---|---|---|
| **Q4 2019** | Oct | 16.0 | 450.7 | 159.7 | 2,643.4 | 3,927.2 | 2,435.1 |
| | Nov | 17.0 | 482.2 | 157.9 | 2,618.6 | 3,918.5 | 2,410.3 |
| | Dec | 12.0 | 357.3 | 166.4 | 2,64.4 | 4,100.6 | 2,540.0 |
| | **Total** | **45.0** | **1,290.2** | | | | |
| **Q1 2020** | Jan | 12.3 | 336.0 | 162.1 | 2,600.4 | 4,023.4 | 2,473.9 |
| | Feb | 12.3 | 385.6 | 148.6 | 2,337.0 | 3,662.7 | 2,267.6 |
| | Mar | 19.1 | 639.3 | 131.9 | 1,966.1 | 3,109.0 | 2,016.1 |
| | **Total** | **43.7** | **1,360.9** | | | | |
| **Q2 2020** | April | 12.7 | 439.0 | 139.7 | 1,958.1 | 3,292.6 | 2,135.0 |
| | May | 14.6 | 430.3 | 137.1 | 1,948.1 | 3,203.9 | 2,095.9 |
| | June | 12.3 | 552.6 | 137.7 | 1,942.1 | 3,217.1 | 2,104.3 |
| | **Total** | **39.6** | **1,421.9** | | | | |
| **Q3 2020** | July | 13.5 | 517.1 | 133.2 | 1,804.1 | 3,059.6 | 2,036.0 |
| | Aug | 10.5 | 470.6 | 139.7 | 1,794.9 | 3,223.8 | 2,144.4 |
| | Sep | 13.9 | 524.5 | 139.9 | 1,852.3 | 3,258.8 | 2,147.7 |
| | **Total** | **37.9** | **1,512.2** | | | | |

## 4.6 Performance of Listed Companies

**Table 15: Price Gainers**

| Counter | 30th June 2020 | 30th September 2020 | % change |
|---|---|---|---|
| NATION MEDIA | 15.40 | 17.90 | **16.23%** |
| SASINI PLC | 17.80 | 20.00 | **12.36%** |
| KENYA RE INSURANCE CORPORATION | 2.14 | 2.40 | **12.15%** |
| NAIROBI SECURITIES EXCHANGE | 7.74 | 8.64 | **11.63%** |
| NAIROBI BUSINESS VENTURES | 0.60 | 0.66 | **10.00%** |
| SAMEER AFRICA PLC | 3.50 | 3.85 | **10.00%** |
| BAT | 317.75 | 348.00 | **9.52%** |
| ABSA NEW GOLD ETF | 1,810 | 1,960 | **8.29%** |
| KCB GROUP | 36.35 | 39.10 | **7.57%** |
| EQUITY GROUP | 34.70 | 36.70 | **5.76%** |

Source: NSE

### Nation Media Group

During the Quarter, the Nation Media Group announced its reorganization plans following the impact of the Covid-19 pandemic on the organization. The key pillar of the reorganization was the digitization of their operations and leveraging on innovation and mobile publications. These strategies materialized in

04th September 2020 when the Company launched its mobile content using Augmented Reality technology and whose focus group is all the African countries. This development will serve as the pillar to excellent customer services, enhance technological innovations and place the company as the top provider of information through digital platforms. These efforts by the company have served to attract and encourage investors to invest in the counter.

### Nairobi Securities Exchange

During the quarter, NSE recorded more than 100% increase on their profit after tax for the first half of 2020 compared to the profits made in the same period in 2019.In his speech on 27th August 202036 the Chief Executive Officer of NSE attributed this to the cost reduction strategy adopted by the company, whereby the staff ,system and other costs were cut down by 41.70%,5.9% and 230% respectively anchored on sustainable business plans . This together with other strategic measures taken by the NSE such as digitization of trading at the bourse through the launch of the NSE digital application and the revision of the components of the NSE 20 Share and NSE 25 Indices have played a major role in attracting investors to the counter thus the appreciation.

### ABSA New Gold ETF

During the Covid-19 pandemic the investor trends changed to safer investment options such as the ABSA New Gold ETF which saw the counter appreciate in value.

### British American Tobacco

Following the approval of a final dividend by shareholders during the Annual General Meeting [37]held on 24th June 2020 and approval of the same by the Board on 16th July 202038 ,the counter experienced high demand during the quarter as the investors sought to get this dividend hence the appreciation of the counter.

**Table 16: Price Losers**

| Counter | 30th June 2020 | 30th Sep 2020 | % change |
|---|---|---|---|
| WPP SCANGROUP | 16.50 | 6.66 | 59.64% |
| E.A. CABLES LTD | 2.08 | 1.44 | 30.77% |
| CENTUM INVESTMENT CO | 25.55 | 20.30 | 20.55% |
| FLAME TREE GROUP | 1.57 | 1.31 | 16.56% |
| BAMBURI CEMENT | 28.00 | 23.55 | 15.89% |
| DIAMOND TRUST BANK | 70.75 | 60.00 | 15.19% |
| NCBA GROUP | 26.55 | 23.00 | 13.37% |
| I& M HOLDINGS PLC | 50.00 | 44.25 | 11.50% |
| ILAM FAHARI I-REIT | 5.90 | 5.24 | 11.19% |
| HOUSING FINANCE GROUP | 4.41 | 3.97 | 9.98% |

***Source: NSE***

### WPP ScanGroup

During the quarter, WPP SCANGROUP recorded a 250 [39]million increase in its half-year profits after tax. However, a keen observation into the statements reveal that this increase was attributable to the gain on disposal of the company's shares in Millward Brown East Africa Limited, Millward Brown Nigeria Limited, Millward Brown West Africa and Research and Marketing Group Investment Limited on 30th June 2020.The company sales dropped by 21% due to the impact of Covid-19 on the business and the provision for bad debts increased due to increased non-payments by clients. This

[36] https://www.nse.co.ke/media-center/press-release.html
[37]http://www.batkenya.com/group/sites/bat_b4alxz.nsf/vwPagesWebLive/DOB4AMDW/$FILE/medMDBQXF3W.pdf?openelement
[38]http://www.batkenya.com/group/sites/BAT_B4ALXZ.nsf/vwPagesWebLive/DOBRPAZG/$FILE/HY_2020_press_release_16_Jul_2020%20.pdf?openelement
[39]https://www.wpp-scangroup.com/wp-content/uploads/2020/08/2020-FS-summary-halfpage-copy.pdf

could have lowered the demand of the counter hence the price drop.

**Bamburi Cement**

The company recorded a 13%40 decline in its half year turnover which is attributable to the impact of Covid-19 pandemic o the operations of the company following the Covid-19 containment measures put in place by the government. The turnover was mainly affected by decline of construction activities and closure of construction sites.

**Diamond Trust Bank**

The Bank recorded a 25% decrease41 in the half year profit before tax in 2020 as compared to the same period last year. This drop iis attributed to the increased in provisions made by the bank to their customers in order to help their business to stay afloat.

[40] https://www.lafarge.co.ke/bamburi-cement-group-defies-tough-economic-times-post-improved-profit

[41] https://dtbk.dtbafrica.com/news/articles/DTB-Posts-KSh4.5-Billion-in-Half-Year-Pre-Tax-Profit

## 5.0 Capital Markets Stability Soundness Indicators

**Table 17: Capital Markets Stability Indicators (July - Sep 2020 )**

| Stability Indicator | Quarter Year | Market Statistics | | | | Assessment of Risk Level | Performance Brief for the Quarter | Ongoing Intervention Measures |
|---|---|---|---|---|---|---|---|---|
| **1.0 Equity Market Depth** | | | | | | | | |
| NSE 20 Index Volatility<br><br>Base Year = 2010 | Q3.2020 | July | Aug | Sep | Q.Avg | Medium (indicative – Low < 1% Medium: >1% high; >10%) | The average NSE 20 Share Index volatility for the period 1st July to 30th Sep 2020 remained constant and was equal to the Q2.2020 average of **0.58%.** On the other hand, the NASI Index volatility for Q3.2020 | Amidst the pandemic, the index volatility for the NSE 20 Share, NSE 25 Share and the NASI recouped comparatively as calm and confidence in the management of the pandemic became evident across the globe. During the period under review, the Nairobi Securities Exchange reviewed the constituent counters of its two benchmark indices, the NSE 20 and NSE 25 Share Indices. In the review, new counters included were Stanbic Holdings PLC and Jubilee Holdings PLC in the NSE 20 and NSE 25 Share Index respectively. The two were included to replace Kenya Airways PLC previously included in the two indices. This followed the suspension of trading in KQ shares after the publication of the National Management Aviation Bill 2020. In this pandemic period, the market observed increased |
| | | 0.66% | 0.70% | 0.41% | 0.59% | | | |
| | Q2.2020 | April | May | June | Q.Avg | | | |
| | | 0.59% | 0.77% | 0.41% | 0.59% | | | |
| | Q1.2020 | Jan | Feb | Mar | Q.Avg | | | |
| | | 0.44% | 0.45% | 1.06% | 0.65% | | | |
| | Q4.2019 | Oct | Nov | Dec | Q.Avg | | | |
| | | 0.44% | 0.54% | 0.42% | 0.47% | | | |
| NASI Volatility<br><br>Base Year = 2010 | Q3.2020 | July | Aug | Sep | Q.Avg | Medium (indicative – Low < 1% Medium : | | |
| | | 0.73% | 0.73% | 0.43% | **0.63%** | | | |
| | Q2.2020 | April | May | June | Q.Avg | | | |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | 1.01% | 1.14% | 0.51% | **0.89%** | **>1% high; >10% )** | averaged is **0.63%** compared to the Q2.2020 average of **0.89%.** | performance on the ABSA ETF Gold as investors sought alternative asset classes that could retain their investment value amidst volatile prices of listed equities, a characteristic that is normally exhibited by Gold underlying Assets |
| | **Q1.2020** | **Jan** | **Feb** | **March** | **Q.Avg** | | | |
| | | 0.50% | 0.64% | 1.35% | 0.83% | | | |
| | **Q4.2019** | **Oct** | **Nov** | **Dec** | **Q. Avg** | | | |
| | | 0.50% | 0.76% | 0.32% | 0.53% | | | |
| **Turnover Ratio** | **Q3.2020** | **July** | **Aug** | **Sep** | **Q.Sum** | **Low (indicative – annual: <8%-Low; >15% High)** | Turnover ratio for the period under review summed at **1.78%** with the month of September recording highest turnover value of **0.65%.** We expect activity in the market to be influenced by counters that | Whereas turnover levels appear to fairly constant, averaging slightly below the 2% mark in the last 3 quarters, activity in the Bourse has recently seen different segments and sectors contributing significantly towards overall week on week turnover values. This, as opposed to previous trends where the telecommunication and banking sectors have largely dominated the market.<br>For example in the second week of August 2020, the ABSA New Gold ETF was the most liquid counter during the week with a turnover ratio of **9.47%.** Additionally, the ILAM Fahari I-REIT became the fourth most liquid counter in the same the week with a turnover ratio of **0.25%** |
| | | 0.64% | 0.49% | 0.65% | 1.56% | | | |
| | **Q2.2020** | **April** | **May** | **June** | **Q.Sum** | | | |
| | | 0.59% | 0.69% | 0.58% | 1.86% | | | |
| | **Q1.2020** | **Jan** | **Feb** | **March** | **Q.Sum** | | | |
| | | 0.50% | 0.54% | 0.94% | 1.98% | | | |
| | **Q4.2019** | **Oct** | **Nov** | **Dec** | **Q.Sum** | | | |
| | | 0.66% | 0.71% | 0.47% | 1.84% | | | |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | | | | | | are currently publishing their Half-year results | |
| **2.0** | **Foreign Exposure Risk** | | | | | | | |
| **Foreign Investor turnover as a % of total turnover** | **Q3.2020** | **July** | **Aug** | **Sep** | **Q.Avg** | **Medium (indicative – annual: <40%-Low; >90% High)** | Foreign investor participation in the month ended July and August 2020 was at **60.62%** and **65.14%** respectively; compared to the previous Quarter's average of **64.59%** recorded. September 2020 registered the | The net outflows and discounted prices of active Counters at the NSE experienced since the onset of the coronavirus pandemic globally has created an opportunity for local investor to take up positions in the market with a long-term view of benefiting from expected future capital gains and dividends as well as reduction in the market concentration risk. The Authority remains poised to play a role in the product uptake of capital markets products. For example, with regard to the REITS segment, through the New draft Income Tax (Real Estate Investment Trusts) Rules, 2020 recently exposed the to the public for comments, the regulations are meant to operationalize section 20(c) and (d) of the Income Tax Act on exemption of REITs. |
| | | 60.62% | 65.14% | 75.55% | **67.11%** | | | |
| | **Q2.2020** | **April** | **May** | **June** | **Q.Avg** | | | |
| | | 64.96% | 65.38% | 63.43% | **64.59%** | | | |
| | **Q1.2020** | **Jan** | **Feb** | **Mar** | **Q.Avg** | | | |
| | | 60.60% | 62.81% | 60.01% | **61.14%** | | | |
| | **Q4.2019** | **Oct** | **Nov** | **Dec** | **Q.Avg** | | | |
| | | 64.29% | 55.97% | 68.63% | **62.96%** | | | |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | | | | | | highest foreign investor turnover of **75.55%** as compared to the total turnover. This is the highest recorded rate since April 2019 which had a proportion amounting to **75.80%** | |
| **Net Foreign Portfolio Flow**<br><br>**(In KES Millions)** | **Q3.2020** | **July** | **Aug** | **Sep** | **Q.Sum** | **High**<br><br>**(indicative – annual: <Kshs (50million) - High** | Net Foreign Portfolio for the month of July amounted to an outflow of **Kshs 5,339 Mn,** compared to a total | |
| | | (5,339) | 10 | 802 | **(4529)** | | | |
| | **Q2.2020** | **April** | **May** | **June** | **Q.Sum** | | | |
| | | (4,098) | (4,462) | (1,690) | **(10,250)** | | | |
| | **Q1.2020** | **Jan** | **Feb** | **Mar** | **Q.Sum** | | | |
| | | 530 | (2,656) | (9,058) | **(11,184)** | | | |

| | **Q4.2019** | **Oct** | **Nov** | **Dec** | **Q.Sum** | **(outflow; >KShs. 50 million High inflow)** | outflow of **Kshs 1,690 Mn** in recorded in June 2020. The months of August and September recorded the first positive flows of **Ksh 10 Mn** and **Kshs 802 Mn** (net inflow) respectively since the pre-covid period i.e. January 2020. Estimates for the month of September suggest this trend is likely to continue | |
|---|---|---|---|---|---|---|---|---|
| | | (1,361) | (730) | 1,247 | **262** | | | |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **3.0** | **Market Concentration Risk** | | | | | | | |
| **Market Concentration (Top 5 companies by market cap)** | **Q3.2020** | **July** | **Aug** | **Sep** | **Q.Avg** | **High (indicative – annual: >50% High concentration)** | Since the end of Q2.2020, the top five companies by market capitalization has accounted for three quarters of the total market capitalization recording values of of **75.61%, 76.14%** and **77.03%** in July August and September respectively. | The telecommunication and banking sectors remain dominant by size in the market. Safaricom Plc, accounting for **55.79%** of the total market cap as at September 18, 2020. The company announced a First & Final Dividend of Kes.1.40 on 29-Apr-2020, a book Closure 31-Jul-2020 and payment was on 31-Aug-2020. Notwithstanding, the market has also seen some counters enter into top 5 weekly equity turnover showing investors' interest outside the common counters. For example in the week ended August 21 2020, the Investment Services section contributed upto 2.60% of the market activity |
| | | 75.61% | 76.14% | 77.03 | **76.24%** | | | |
| | **Q2.2020** | **April** | **May** | **June** | **Q.Avg** | | | |
| | | 74.36% | 75.53% | 76.39% | **75.43%** | | | |
| | **Q1.2020** | **Jan** | **Feb** | **Mar** | **Q.Avg** | | | |
| | | 74.36% | 74.43% | 73.66% | **74.15%** | | | |
| | **Q4.2019** | **Oct** | **Nov** | **Dec** | **Q.Avg** | | | |
| | | 73.25% | 73.34% | 73.46% | **73.35%** | | | |
| **4.0** | **Derivatives Trading Statistics** | | | | | | | |

| | | Jul | Aug | Sept | Q. Low | | |
|---|---|---|---|---|---|---|---|
| Total Volume<br><br>**(No. of contracts)** | 25-Share Index | - | - | 1 | 1 | In the month of July the total number of contracts traded were **103** compared to **92** in August and **180** in September.<br><br>The Safaricom SSF remained dominant accounting for **70.9%, 64.1%** and **58.4%** of the contracts traded in the July, August and September respectively. In the spot market, the book closure for Safaricom | The derivatives market continued to show considerable activity as the third quarter of the year began with over 100 contracts being traded, similar to the end of June 2020 figures. With this trend the total number of contracts traded by end of Q3.2020 is expected to equal or topple the total of 209 contracts traded in Q2.2020 |
| | SCOM SSF | 73 | 59 | 87 | 219 | | |
| | EQTY SSF | 17 | 6 | 27 | 50 | | |
| | KCBG SSF | 1 | 16 | 33 | 50 | | |
| | EABL SSF | 12 | 5 | 24 | 41 | | |
| | BATK SSF | - | 1 | 2 | 3 | | |
| | ABSA SSF | - | 5 | 6 | 11 | | |
| | **Total** | **103** | **92** | **180** | **375** | | |

<table>
<tr><td></td><td></td><td></td><td>happened on July 31, 2020, perhaps explaining the corresponding increased activity in the futures market as well during the same period.</td></tr>
<tr><td>Gross Notional Exposure (GNE)[42]</td><td>
<table>
<tr><th></th><th>Jul</th><th>Aug</th><th>Sept</th><th></th><th>Q.Su Low</th></tr>
<tr><td>25-Share Index</td><td>-</td><td>-</td><td>320,000</td><td></td><td>3</td></tr>
<tr><td>SCOM SSF</td><td>2,026,890</td><td>1,623,860</td><td>2,609,150</td><td></td><td>6,259,900</td></tr>
<tr><td>EQTY SSF</td><td>557,250</td><td>202,040</td><td>974,600</td><td></td><td>1,733,890</td></tr>
<tr><td>KCBG SSF</td><td>34,550</td><td>562,400</td><td>1,236,630</td><td></td><td>1,833,580</td></tr>
<tr><td>EABL SSF</td><td>189,500</td><td>76,890</td><td>384,975</td><td></td><td>651,365</td></tr>
<tr><td>BATK SSF</td><td>-</td><td>33,300</td><td>66,500</td><td></td><td>99,800</td></tr>
<tr><td>ABSA SSF</td><td>-</td><td>46,850</td><td>59,400</td><td></td><td>106,250</td></tr>
<tr><td>Total</td><td>2,808,190</td><td>2,545,340</td><td>5,651,255</td><td></td><td>11,004,785</td></tr>
</table>
</td><td></td><td>The total value (Gross Notional Exposure) of contracts traded in the Quarter ended September 2020 totaled Kshs. 11.00 Mn. With the month of September accounting for</td></tr>
</table>

[42] Gross Notional Exposure = no. of Contracts * notional contract size * market price of underlying equity share or index. The GNE is the value amount. It is the exact conversion of the derivative into the market value of an equivalent position in the underlying asset of that derivative.

<table>
<tr><td></td><td></td><td></td><td>that Exposure by upto 51.35% .</td></tr>
<tr><td>Total Open Interest[43](No. of Contracts)</td><td>
<table>
<tr><th></th><th>Jul</th><th>Aug</th><th>Sep</th></tr>
<tr><td>25-Share Index</td><td>-</td><td>-</td><td>1</td></tr>
<tr><td>SCOM SSF</td><td>32</td><td>37</td><td>30</td></tr>
<tr><td>EQTY SSF</td><td>18</td><td>15</td><td>10</td></tr>
<tr><td>KCBG SSF</td><td>29</td><td>28</td><td>9</td></tr>
<tr><td>EABL SSF</td><td>17</td><td>22</td><td>3</td></tr>
<tr><td>BATK SSF</td><td>1</td><td>-</td><td>-</td></tr>
<tr><td>ABSA</td><td>10</td><td>7</td><td>1</td></tr>
<tr><td>Total</td><td>107</td><td>109</td><td>54</td></tr>
</table>
</td><td>Low</td><td>There was a significant increase in open interest contracts in July and August compared to the Q2.2020 average figures recorded. Safaricom and KCB SSF recorded 32 and 29 open contracts respectively in July. In keeping with the trend experienced in Q2.2020, . the</td></tr>
</table>

[43] Open interest is the total number of outstanding derivative contracts that have not been settled or closed. It is a measure of market interest.

| | | | | |
|---|---|---|---|---|
| | | | NSE 25 Share SSF recorded close to nil trades during the quarter, even as the market is envisaged to recover from the erosion attributed to the spread of the coronavirus. | |
| Settlement Guarantee Fund (SGF) Coverage[44] for Derivatives | <table><tr><th></th><th>Jul</th><th>Aug</th></tr><tr><td>SGF</td><td>184,040,389</td><td>85,142,316</td></tr><tr><td>Average Market Value</td><td>190,477.00</td><td>169,689</td></tr><tr><td>**SGF Coverage**</td><td>**966 times**</td><td>**1,091 times**</td></tr></table> | **Low** | The SGF coverage ratio for the derivatives market as at end of July 2020 was **966 times** compared to | To maximize value from the SGF fund balances, there is deliberate effort by NSE to encourage increased activity by market intermediaries in this market for increased volumes of trade. |

[44] An indicator of the level of coverage the SGF provides for the derivatives market. It is the total SGF amount divided by the average value of all positions in the derivatives market.

August and September 2020 recorded coverage of **1091 times** and **495 times** respectively, showing increased sufficiency in coverage.

SGF Coverage of Clearing Member 1 and Clearing Member 2[45]

| | Jul | Aug | Sept |
|---|---|---|---|
| SGF | 184,040,389 | 185,142,316 | 186,3[illegible]3,473 **Low** |
| Avg Value CM1 | 150,922.00 | 135,681 | 299,268 |
| Avg Value CM2 | 39,555.00 | 28,400 | 77,481 |
| SGF Coverage CM1 | **1,219 times** | **1,365 times** | **(** |
| SGF Coverage CM2 | **4,653 times** | **6,519 times** | **2,404 times** |

**5.0** **Government Bond Market Exposure**

[45] Total SGF Amount/Average value of the positions of CM1 and CM2.

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **Treasury Bond market turnover Concentration** | **Q3.2020** | **July** | **Aug** | **Sep** | **Q.Avg** | **High (indicative – annual: >50% High concentration)** | During the second quarter, Treasury bond turnover averaged at **99.98%** compared to the current Q3.2020 average of **99.94%** . Corporate bond trading activity remains negligible with only the NCBA and EABL Fixed Medium Term Notes being traded in the months of | The Kenyan market continues to be highly exposed to Government bond market with auctions often characterized by oversubscription to the government short term debt instruments with the 90-day T-bills providing yields of up to **6.27%** ,that of the 182-day T-bills stood at **6.72%**, while yield on the 364-day T-bill stood at **7.57%** as at September, 2020.<br>During the month the Central Bank of Kenya (CBK), hit its target issuance amount of Kshs.70 billion in the August 11-year amortized infrastructure bond issue number IFB1/2020/11 at an average rate of 11.302 per cent. CBK, accepted Kshs.78.64 Billion against bids received worth Kshs. 101.47 Billion against a target of Kshs.70 Billion |
| | | 99.99% | 99.84% | 100% | **99.94%** | | | |
| | **Q2.2020** | **April** | **May** | **June** | **Q.Avg** | | | |
| | | 99.95% | 100.00% | 100% | **99.98%** | | | |
| | **Q1.2020** | **Jan** | **Feb** | **Mar** | **Q.Avg** | | | |
| | | 95.99% | 99.99% | 99.996 % | **98.66%** | | | |
| | **Q4.2019** | **Oct** | **Nov** | **Dec** | **Q.Avg** | | | |
| | | 99.86% | 98.29% | 99.98% | **99.38%** | | | |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | | | | | | July and August | |
| **Corporate Bond Market ownership** | | | | | | **High (indicative – annual: >50% High concentration)** | Local Corporate bond investors were the leading investors in corporate bonds at **95.91%** compared to **98.74%** in Q1.2020of amounts outstanding, while foreign bond investors held **3.79%** during the quarter, up from **1.15%** recorded in Q1.2020 as the | |

| Category | No of Investors | Amount Outstanding (Millions) | % of total share quantity |
|---|---|---|---|
| **Local Investors** | 1,667 | 23,844.35 | **95.91%** |
| **East African Investors** | 7 | 73.80 | **0.30%** |
| **Foreign Investors** | 32 | 942.15 | **3.79%** |

**Source: CDSC Data as at September 2020**

<table>
<tr><td></td><td></td><td></td><td>total corporate bond holdings.</td><td></td></tr>
<tr><td>6.0</td><td colspan="4">Investor Profiles - Equity Market</td></tr>
<tr><td>Equity Market</td><td>
<table>
<tr><th>Type of Investor</th><th>No. of Investors</th><th>Share Quantity (Millions)</th><th>% to Share Quan</th></tr>
<tr><td>Local Investors</td><td>2,011,938</td><td>79,046.82</td><td>8</td></tr>
<tr><td>EA Investors</td><td>9,067</td><td>1,089.92</td><td>1.</td></tr>
<tr><td>Foreign Investors</td><td>15,038</td><td>17,233.56</td><td>1</td></tr>
<tr><td>BR</td><td>23</td><td>12.20</td><td>0.</td></tr>
<tr><td>JR</td><td>273</td><td>0.96</td><td>0.</td></tr>
</table>
Source: CMA- *Data as at September 2020</td><td>Medium<br>(indicative – annual: >50% High concentration)</td><td>Local investors accounted for 81.17% of total shares held in the equity market with 17.70% being held by foreign investors.</td><td>Noting that local investors hold the greatest number shares, more targeted market deepening and investor education initiatives will be undertaken to increase participation of local investors with the aim increasing the competitiveness of our market.<br>Promotion of regional trading and access to the Kenyan market by other investors within the region also remains a strategy for increasing participation at the Nairobi Securities Exchange through increased partnerships with respective country regulators.</td></tr>
<tr><td>7.0</td><td colspan="4">Settlement Compensation Coverage</td></tr>
<tr><td>Settlement Guarantee Fund</td><td>
<table>
<tr><th>Q3.2020</th><th>July</th><th>Aug</th><th>Sep</th><th>Q.Avg</th></tr>
<tr><td></td><td>1.66</td><td>2.08</td><td>1.64</td><td>1.79</td></tr>
<tr><td>Q2.2020</td><td>April</td><td>May</td><td>June</td><td>Q.Avg</td></tr>
<tr><td></td><td>1.59</td><td>1.32</td><td>1.75</td><td>1.55</td></tr>
</table></td><td>Medium<br>(indicative – annual: > 1 times,</td><td>SGF Ratio for the month ended July 2020 was at 1.66 compared</td><td>Through Risk-based supervision, the Authority has been monitoring the SGF figures and the financial position of the firms to ensure that they are in good standing and that investors are protected.</td></tr>
</table>

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **(SGF) Coverage Ratio**[46] | **Q1.2020** | **Jan** | **Feb** | **Mar** | **Q.Avg** | **implies full coverage)** | to **2.08** and **1.64** recorded in August and September respectively. The change is attributed to Average Equity daily turnovers for the month of August decreasing by upto **KShs 123.41 Million** with a less than par increase in SGF balances of **Kshs 5.54 Million** from July 2020 to August 2020. Between | |
| | | 1.77 | 1.55 | 1.17 | 1.50 | | | |
| | **Q4.2019** | **Oct** | **Nov** | **Dec** | **Q.Avg** | | | |
| | | 1.27 | 1.21 | 1.56 | 1.35 | | | |
| | **Q3.2019** | **July** | **Aug** | **Sep** | **Q.Avg** | | | |
| | | 2.01 | 2.33 | 1.92 | 2.09 | | | |

[46] ***Source: CDSC***

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | | | | | | August and September, the average daily equity turnover increased from **Kshs 497.26 Mn** to **Kshs 631.90 Mn** recorded in September 2020. The Guarantee Fund balances remain sufficient to cover liabilities that would arise following default by securities brokers | |
| **8.0** | **Asset Base of Fund Managers, Stockbrokers, Investment Banks** | | | | | | | |

<table>
<tr>
<td>Assets Under Management</td>
<td>As at 31st August 2020 (Amount in KShs Millions)
<table>
<tr><th>CMA Licensee</th><th>Total Assets</th><th>Total Liability</th><th>Net Ass</th></tr>
<tr><td>Fund Manager</td><td>6,225.86</td><td>1,555.91</td><td>4,669</td></tr>
<tr><td>Stockbrokers</td><td>1,697.92</td><td>757.02</td><td>940</td></tr>
<tr><td>Investment Banks</td><td>12,265.52</td><td>4,065.09</td><td>8,200</td></tr>
<tr><td>Investment Advisors</td><td>2,129.44</td><td>169.35</td><td>1,960</td></tr>
<tr><td>Online Forex Brokers (Non-Dealing)</td><td>1,031.30</td><td>794.24</td><td>237.0</td></tr>
<tr><td>Total</td><td>23,350.04</td><td>7,341.62</td><td>16,008.</td></tr>
</table>
</td>
<td>Medium<br><br>(Indicative – the higher the figure, the more stable is the market)</td>
<td>The net assets base of Fund Managers, Stockbrokers, Investment Banks, Investment advisors and online forex brokers as at 31st August 2020 was Kshs 4,669.95 Mn, Kshs 940.90 Mn, Kshs.8,200.43 Mn, Kshs 1,960.09 Mn and Kshs 237.06 Mn respectively.</td>
<td>On the back of regulatory interventions aimed at improving the business environment of its licensees during this period of the pandemic as implemented in the first and second quarters of 2020, the balances recorded for the different CMA Licensee category show minimal change, providing assurance of the effectiveness of the measures enacted so as to maintain a sound market infrastructure.<br>Whereas the pandemic is far from over, the Authority remains vigilant in monitoring the market with market participants being encouraged to have up to date business continuity plans.</td>
</tr>
</table>