CAPITAL MARKETS AUTHORITY

Promoting the Integrity and Growth of the Capital Markets

The Capital Markets Soundness Report

Volume XI

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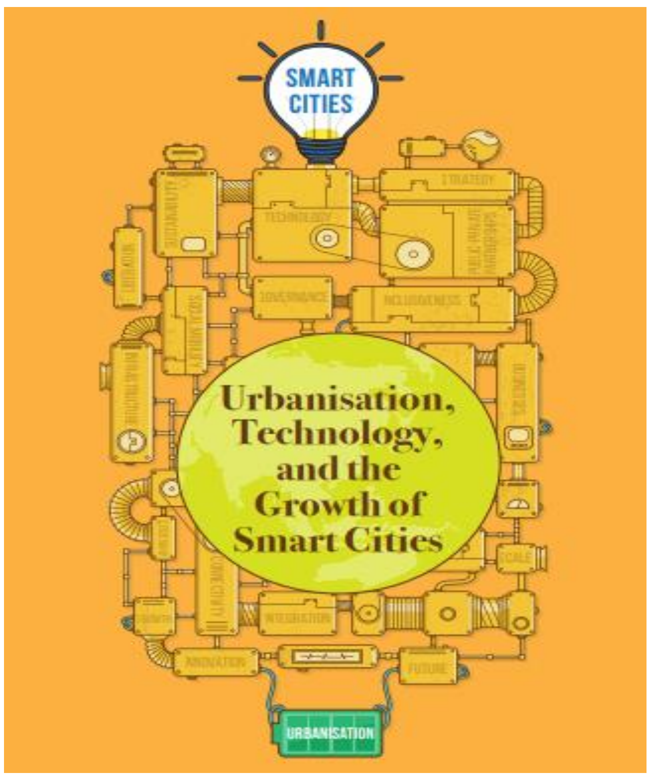

"Business Unusual: A Call for change in investment strategies and the increasing role of technology in the face of rapid urbanization and rise of smart cities."

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SPECIAL MESSAGE FROM THE CHIEF EXECUTIVE OFFICER

Mr. Paul Murithi Muthaura,
CEO, Capital Markets Authority, Kenya

On behalf of the Authority, I am happy to present this 11th edition of the Capital Markets Soundness Report (CMSR) for the quarter ended June 2019 (Q2.2019). Since the inaugural report that was published in 2016, the CMSR has undergone continual improvement both in depth and scope.

We are delighted to include in this edition a special contributory piece forwarded by the Kenya Bankers Association (KBA), titled "*Trade Wars and Global Financial Flows*." This contribution underpins the growing attention to and reliance of stakeholders on this quarterly publication. We remain confident that this platform shall continue to stimulate collaborative efforts, convergence of opinions and responsive solutions to inform multi-sectoral strategies to drive the Kenyan financial and capital markets to greater heights.

Globally, the capital markets are going through a myriad of challenges that present as much opportunity as they do risks. It is therefore upon us, as industry practitioners, to leverage the presented opportunities to propel capital markets transformation in Kenya. I wish to reiterate the Authority's commitment towards providing the necessary facilitation and support required in exploiting such benefits.

Lastly, I wish to acknowledge the immense value of stakeholder involvement in executing our policy advisory mandate. This constructive engagement culminated in the adoption of a number of policy proposals submitted to the National Treasury in the last financial year through pronouncements by the Cabinet Secretary, National Treasury and Planning in his delivery of the Budget Statement on June 13th, 2019.The proposals have been evaluated in this report for your information and analysis.

My sincere gratitude to you as a key contributor to the attainment of the success of the Capital Markets in Kenya.

Enjoy the read.

Mr. Paul Murithi Muthaura, MBS
CHIEF EXECUTIVE OFFICER

EDITORIAL

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

The 11th issue of the Capital Markets Soundness Report (CMSR) rolls out on the dawn of a new Financial Year , setting pace for the industry to align its efforts towards supporting the Government in the attainment of its global vision of transforming Kenya into a middle-income economy by the year 2030, as well as achievement of its third Medium Term Plan (MTPIII) and the "Big 4" Agenda.

The theme of this edition ***"Business Unusual: A call for change in investment strategies and the increasing role of technology in the face of rapid urbanization and rise of smart cities"***, is inspired by the ever-increasing need for capital to fund infrastructural projects to support growth of the domestic economy. We present a special feature on the dynamics accessible to countries through urbanization and the development of smart cities globally, while emphasizing the opportunity to the Capital Markets to mobilize capital to financing requisite infrastructure through innovative financing mechanisms.

Cities such as Hongkong, London and New York amongst others, did not become International Finance Centers by design- infrastructure played a pivotal role in charting their sustainability levels. As we angle towards making Nairobi the Heart of the African Capital Markets, the industry needs to anchor its stake as the primary provider of capital to fund the development of the required infrastructure in Nairobi and other Cities and emerging urban areas.

Cyber Risk is now widely recognized as one the top threats to financial markets with a prevalence of Cyber Incidents from financial data breaches at large multinational public companies to high profile incidents on Central Banks and Government systems in the face of increased use of Financial Technology (FinTech). The potential economic costs of such events can be immense and damaging to public trust. Confidence is significant as cyber incidents could potentially undermine the integrity of the global financial markets. In this edition we explore domestic and international initiatives, especially by national authorities, standard setting bodies and the private sector to address Cyber Risk and increase the Cyber Resilience of the financial markets and industry.

In the quarter under review, the Authority granted an approval to the Nairobi Securities Exchange (NSE) to run a derivatives market in Kenya, the first within the East African Region and great expectations abound for the market as we begin to realize the fruits of several years of preparations to establish the only second such market in Sub-Saharan Africa.

May we relentlessly affirm our value to the overall prosperity of the Kenyan economy by making the Capital Markets the source of choice for all, in capital mobilization.

Happy reading!
Mr. Luke E. Ombara
DIRECTOR, REGULATORY POLICY & STRATEGY

1. Special Feature - Rise of Urbanization and Smart Cities – Opportunity for a Technological Enhancement Role of the Capital Markets

It is common knowledge that cities are what keep the global economic machine humming with evidence presented by the extent of growth and activity observed in the world's top cities as illustrated below.

Fig 1: Most Populated Cities in the World – 2019

	City	Population	Country	Continent
1	Tokyo	37,435,191	Japan	Asia
2	Delhi	29,399,141	India	Asia
3	Shanghai	26,317,104	China	Asia
4	Sao Paolo	21,846,507	Brazil	South America
5	Mexico City	21,671,908	Mexico	North America
6	Cairo	20,484,965	Egypt	Africa
7	Dhaka	20,283,552	Bangladesh	Asia
8	Mumbai	20,185,064	India	Asia
9	Beijing	20,035,455	China	Asia
10	Osaka	19,222,665	Japan	Asia

Source: World City Populations by World Population Review

It is estimated that over 80% of the world's economic output is derived from activities in citiesand more specifically, an estimated 60% of GDP growth occurs in just the top 600 urban centers. Given the above, it is fair to say that the destiny of humankind is directly linked to what happens in major cities. Further, how urbanization plays out over time could end up having a significant ripple effect on the wider economy.

A Breakdown of Population Statistics over time and Projections

Between 1950 and 2018, the world's population of people living in cities moved from 30% to 55%. This has been attributed to the growth of cities in middle- and high-income economies in places like North America, South America, Europe, and Japan.

It is further estimated that over the coming decades, the large-scale role of cities will become even more amplified as rapid urbanization spills over to the rest of the world. More people, particularly in Asia and Africa will be seeking opportunities in cities over the coming decades. Between 2018 and 2050, the global urban population will increase from 55% to 68%, adding another 2.5 billion people to cities around the world.

The world is constantly changing and many of these shifts have the potential to alter the investment landscape – Jeff Desjardins

It is estimated that three countries will combine for 35% of all urban population growth; namely India, China and Nigeria[1 2].

Figure 2: Top 3 Countries Contributing to Urban Population Growth

Rank	Country	Growth in Urban Population (2018-2050)	% of Global Urban Growth
	Total	860 million people	35%
#1	India	416 million people	17%
#2	China	255 million people	10%
#3	Nigeria	189 million people	8%

Source: Visual capitalist

1.1 Linking Urbanization, Population and Contribution to Global Growth

So, what is the resultant impact of urbanization to global growth? Statistics by the United Nations indicate that in the last 40 years, developing Asia has increased its share of the global economy (in PPP[3] terms) from 8.9% in the 1980's to an estimated 34.1% in 2019.

This dominant region includes China, India, and other fast-growing economies. The European Union and the United States combined for 51.5% of global productivity in 1980, but now account for 31% of the total economic mix.

Similarly, the Latin America and Middle East and Northern Africa (MENA) regions are seeing similar decreases in their share of the economic pie[4].

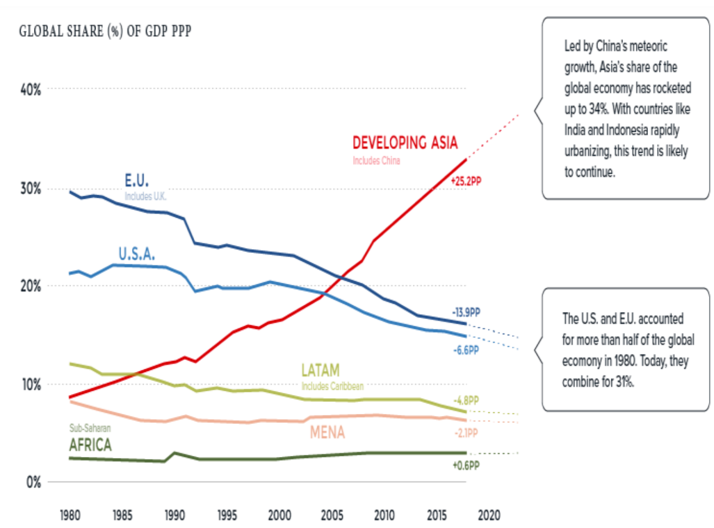
[1] https://www.visualcapitalist.com/investing-megatrend-rapid-urbanisation/

[2] https://www.visualcapitalist.com/stats-amazon-dominance-cloud/

[3] PPP – Purchasing Power Parity is a theory that establishes the idea that the ratio of price level and exchange rate between two countries must be equivalent.

[4]

Fig 3: Trend of Global Share (%) of GDP PPP Across Regions



Source: Visual capitalist

Asia as a whole is forecasted to account for 63% of all global GDP growth (PPP) in 2019, with the lion's share going to China. Countries like India and Indonesia contribute to the "Other Asia" share, and Japan will only contribute 1% to the global growth total.

Fig 4: Share of Global GDP Per Region – 1980 Vs 2019

Country or Region	Share of GDP (PPP, 1980)	Share of GDP (PPP, 2019F)	Change
Developing Asia	8.9%	34.1%	+25.2 pp
European Union	29.9%	16.0%	-13.9 pp
United States	21.6%	15.0%	-6.6 pp
Latin America & Caribbean	12.2%	7.4%	-4.8 pp
Middle East & North Africa	8.6%	6.5%	-2.1 pp
Sub-Saharan Africa	2.4%	3.0%	+0.6 pp

Source: Visual capitalist

Smart Cities, Role of Technology and Innovative Financing

Rapid urbanization over the past two decades has led to the mushrooming of megacities (accepted as those with a population in excess of ten million) around the world. The sheer size and scale of these cities place huge pressure on infrastructure development, public services provision, and environmental sustainability. If we add economic, social and ethnic stratification, as well as health, safety and security risks to the list of challenges, the task facing the leader of any megacity seems overwhelming and is certainly one that cannot be solved by technology alone. A smart city is one that can effectively leverage technology, infrastructure, public policy and citizen engagement to create an urban environment that fosters economic growth and productivity, innovation, social mobility, inclusiveness, and sustainability.

Case Study: An Urban Archipelago in the Pearl River Delta – China

Some city clusters or urban archipelagos are so extensive that they transcend multiple municipal jurisdictions. The Pearl River Delta in China is an outstanding example of how cities under separate political jurisdictions have come together to create an integrated urban cluster with full connectivity and free movement of labor.

Hong Kong is the region's financial hub and offers an open and liberal environment, Shenzhen is more state-directed, Dongguan is heavily industrial, Guangzhou has transformed itself from an industrial center to a major financial hub, and Macau, with its free-wheeling spirit, is known for gaming and entertainment.

These potentially diverse geographies come together to enjoy benefits of scale—this was witnessed during and after the 2008 financial crisis, when this cluster proved to be far more resilient compared to many other cities in the region and around the world.

Source: Parag Khanna, Future Trends in the Century of Cities, New Cities Summit 2014, Dallas, Texas

1.2 Kenya's Urbanization Challenges and the Capital Markets

Kenya Vision 2030 highlights rapid urbanization as one of the four key challenges facing the country. Within the over-arching framework of Vision 2030, the urbanization component of the Second Medium Term Plan (MTP2) 2013–17, and more recently Third Medium Term Plan that has identified housing and urbanization as a key social sector to be invested in under the social pillar. Through the MTP, the Government aims to facilitate a sustainable urbanization process through an integrated urban and regional planning management framework of Kenyan urban centers and towns. Aligned to that goal, the MTP identifies a series of investment programs to enhance infrastructure, connectivity and accessibility, safety and security.

In attaining this, the Vision 2030 has recognized institutions as a critical input to the delivery of such investments and for urbanization to contribute to sustainable growth in Kenya – both at the national and county level. It is therefore of no surprise that both levels of Government are actively involved in the development of solutions to address urbanization challenges through investments in infrastructure across different sectors. Management of Nairobi County for example has been under discussions since 2016, with the presentation of a Bill seeking to omit Nairobi as a County and instead be considered as a separate entity under management by a Cabinet Secretary. In 2017 the Nairobi Metropolitan Area Transport Authority Bill" was developed proposing that the Authority be established to oversee the establishment of an integrated, efficient, effective and sustainable public transport system within the Metropolitan Area. More recently, the Head of State appointed a taskforce responsible for managing execution of projects within Nairobi City.

While different approaches are sought by different entities in the management of such urban areas, the central drive is the need to address the challenges and complexities forwarded by the rapid urbanization witnessed in major cities and urban areas in the country that has resulted in spillover effects of overcrowded and impoverished informal settlements coupled with an increasing population.

Thus, as different players establish their roles in solving the challenges presented through urbanization, the Capital Markets as a capital mobilizer needs to take its rightful place in facilitating both Government and the private sector in capital raising drives to finance infrastructure expansion projects as enlisted through the Medium Term Plan III at the National Government level and County Integrated Development Plans at the County level in partnership with key stakeholders.

Observation;

- The role of Capital Markets in supporting the development of the domestic economy, particularly in Kenya cannot be emphasized enough as we reference other established markets like Hong Kong that have managed to develop their cities through organized capital markets.
- While the Government has historically sourced for concessional and lately commercial loans -both local and international to finance its infrastructure development agenda, the Capital Markets has not been optimally used over the years. The size of the Kenyan Capital Markets remains comparatively small in relation to its peers in the continent such as South Africa, Morocco, Egypt and Nigeria, most of whom have a much bigger role to play in mobilizing capital for the development of domestic infrastructure projects.

Key considerations should be undertaken in using existing Capital Markets instruments as channels for capital raising such as the Green Bonds, Real Estate Investment Trusts (REITs), Securitization amongst others to ensure that domestic capital is re-directed to the development and growth of productive sectors of the economy. Securitization presents an opportunity for potential issuers to raise finance by selling assets or income streams into a special purpose vehicle (SPV). Securitization focuses on ringfencing an asset/collection of assets that demonstrate regular and consistent cashflow and can be bundled together and sold to a special purpose vehicle for non-recourse purposes.

Lessons Learnt:

Aligned to the Government of Kenya's economic blue print Vision 2030 and the "Big 4" Agenda, the Capital Markets is positioning itself as the financing choice for the development of infrastructure in the country, directly and indirectly.

i. ***Directly:*** *By offering capital markets products such as infrastructure bonds, green bonds, social impact investment bonds and blue bonds as channels through which Government entities and private sector participants can* leverage long term market-based financing.

   Indirectly: *By providing a platform through which Kenyans can increase their saving levels by purchasing securities that retain and grow the value of their investments, further creating a repository of capital* *supply that can be invested in capital markets products and services.*

ii. *It may be of significant benefit for both the National and County Governments of Kenya to consider the capital markets as a cheaper long-term financing option for integrated urbanization initiatives including the development of smart cities to bolster ongoing domestic and regional integration initiatives. The Coastal Counties Economic Block "Jumuiya ya Kaunti za Pwani" is a good of example of where the Capital Markets may be used to finance the integration of cities in Kenya*

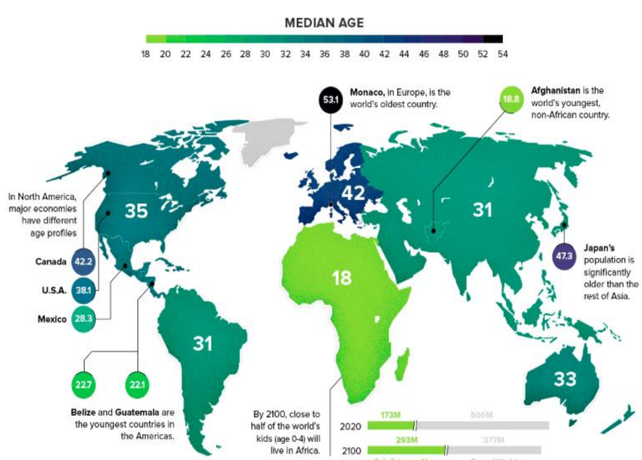
2. Global Population Dynamics and link with the G20 Summit Fukuoka Policy Priorities on Aging and Financial Inclusion (GPFI) – June 2019

Urbanization and the Age Distribution Factor

While the population dynamics continue to change shape globally, age distribution challenges are equally experienced across jurisdictions. The age distributions in large cities within developed nations is forecasted to begin to skew towards the old as evidenced by global statistics.

The biggest impact here may be felt on dependency ratios in the workforce. With a smaller pipeline of new workforce entrants and a burgeoning population of seniors, this changing ratio is one of the most significant stories impacting urban demographics.

Fig 5: The Median Age of Continents



Source: Visual capitalist

Fig 6: World's Youngest Vs Oldest Countries

Rank	Country	Median Age (Youngest)	Rank	Country	Median Age (Oldest)
#1	Niger	15.4 years	#1	Monaco	53.1 years
#2	Mali	15.8 years	#2	Japan	47.3 years
#3	Uganda	15.8 years	#3	Germany	47.1 years
#4	Angola	15.9 years	#4	Italy	45.5 years
#5	Zambia	16.8 years	#5	Slovenia	44.5 years

Source: Visual Capitalist

2.1 The G20 Resolution – June 2019

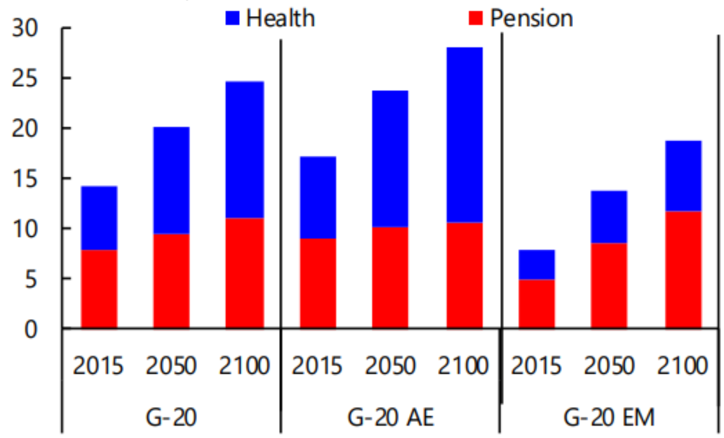
Between 28th and 29th June 2019, leaders of the G20 met in Japan for their 14th meeting, in an effort to address major global economic challenges. A key resolution from the June meeting was the endorsement of the G20 Fukuoka Policy Priorities on Aging and Financial Inclusion (GPFI) aimed at strengthening financial inclusion in the aging society. GPFI has identified eight (8) priorities (G20 Fukuoka Policy Priorities). The priorities are expected to help policy makers, financial service providers, consumers and other actors in the real economy to identify and address the challenges associated with aging populations. The 8 priorities include:

i. Use of data as evidence;
ii. Strengthening digital and financial literacy;
iii. Supporting lifetime financial planning;
iv. Addressing the diverse needs of older people;
v. Innovation to harness inclusive technologies;
vi. Tackling financial abuse and fraud of older people;
vii. Adopt a multi sectoral approach towards financial inclusion; and
viii. Targeting key audiences to address vulnerabilities.

Current data suggests that for all the advanced and a few emerging G-20 countries (Brazil, China, and Russia), fertility rates are below the replacement rate (that is, the fertility rate at which a population exactly replaces itself from one generation to the next) and are steadily declining (Figure 6). By 2050, all G-20 economies are expected to have fertility below replacement which would imply smaller cohorts joining the labor force. At the same time, life expectancy is projected to increase by 5 years from 74 to 79 years. The combination of these developments would lead to large increases in old-age dependency ratios.

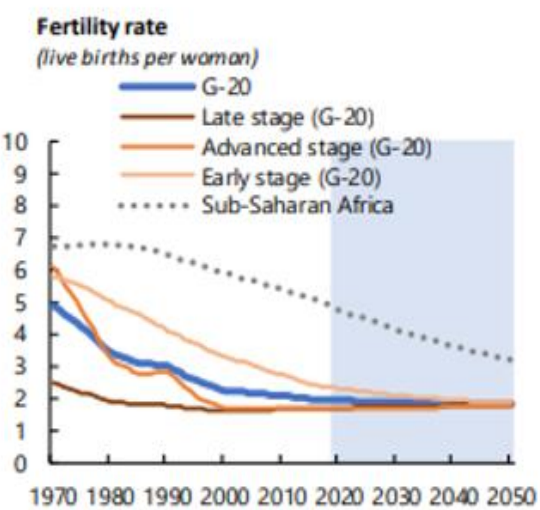
With a growing aged population, costs related to health and servicing of pension is projected to rise as indicated in fig 7 below with advanced economies within the G20 bearing the greatest costs on both fronts.

Fig 6: Daunting Costs on Age-Related Spending (Percent of GDP, nominal GDP weighted)



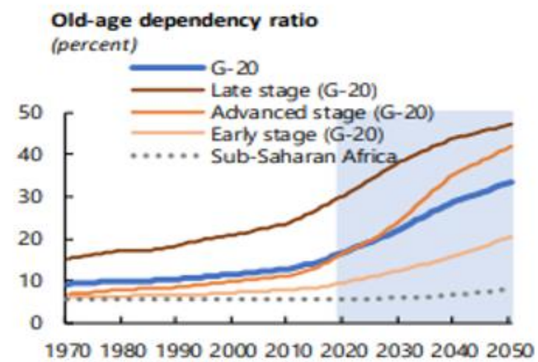
Sources: United Nation (2017); and IMF staff calculations.
Note: Age-related spending is composed of public expenditures for pensions and health.

Fig 7: Fertility Rate Trends



Source: United Nations (2017).
Note: Population weights are used to sum across country groups.

Fig 8: Trend of Old-age Dependency Ratio



Source: United Nations (2017).
Note: The old-age dependency ratio is the number of people ages 65 and older divided by the population ages 15 to 64. Population weights are used to sum across country groups.

Classification of aging Groups – G20 Countries Versus Sub Saharan African Countries

G-20 countries are aging but at different speeds. The aging levels can be broadly grouped into stages of demographic transition according to fertility and mortality rates.

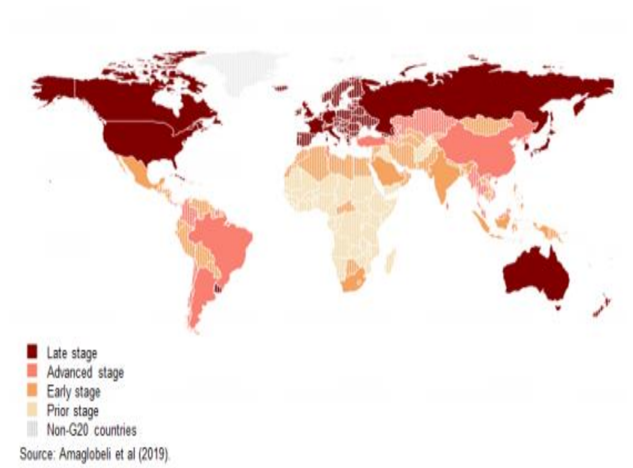
Table 1: Classification of Aging Populations

	Classification	Narrative
1	Late stage demographic transition group	Aging process well under way and the working age population about to decline or already declining (***Australia, Canada, France, Germany, Italy, Japan, Korea, Russia, Spain, UK, and United States***)
2	Advanced stage demographic transition group	A period during which the working age population expands relative to the young and the old. ***(Argentina, Brazil, China, and Turkey)***
3	Early stage demographic transition	fertility rates are declining but remain relatively high with the share of working age population expected to peak in the coming decades. ***(India, Indonesia, Mexico, Saudi Arabia, and South Africa)***
4	Prior transition demographic stage	Both fertility and mortality rates are high – Prevalent in most non-G20 countries including Sub Saharan African Countries

Source: Macroeconomics of Aging and Policy Implications, IMF

Globally, a number of non-G-20 countries especially in Sub-Saharan Africa are in the prior transition demographic stage in which both fertility and mortality rates are high.

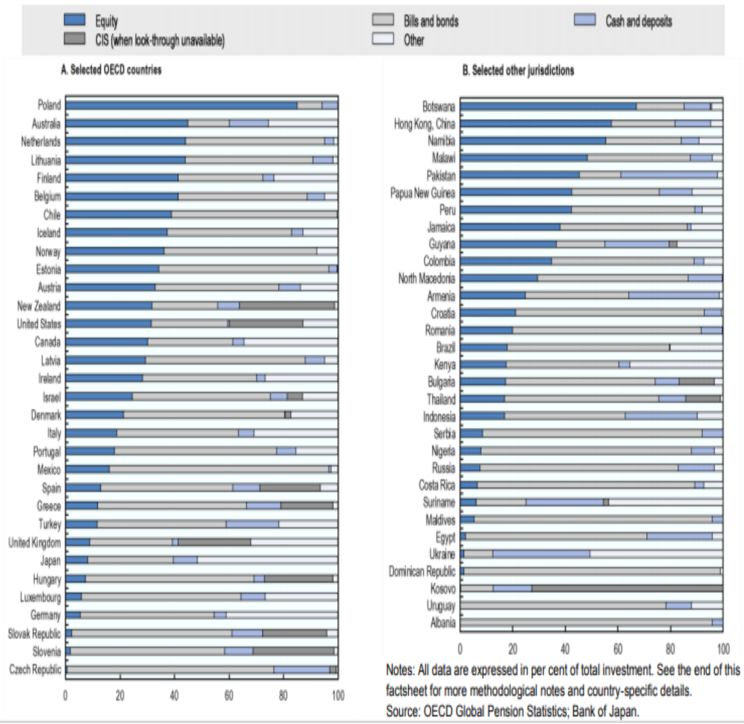
Fig 9: Global Depiction of aging population levels



2.2 Linking Capital Market Performance Trends in Developed Countries to Pension Assets

Pension funds, like many other funds are professionally managed with fund managers seeking investment in asset classes that generate highest return for the pensioners. For example, preliminary data on the performance of pension assets in OECD countries in 2018 indicates that assets in pension funds for the year amounted to USD 27.6 trillion in the OECD area, close to 4% lower than in 2017. Calculated in national currencies, pension fund assets declined in 12 out of 34 reporting OECD countries, including some of the largest pension markets: Japan (-1.1%), the Netherlands (-1.2%), Switzerland (-0.7%), the United Kingdom (-0.3%) and the United States (-5.0%)[5]. Poland experienced the most significant decline at -12.3%. Korea and Australia fared better with a 12.9% and a 9.2% increase respectively, although for the period from June 2017 to June 2018 for Australia.

Fig 10: Asset allocation of pension funds in selected investment categories in 2018



As expected, pension fund assets remained mostly invested in bills, bonds and equities in most jurisdictions. In 2018, these instruments accounted for more than 75% of pension fund investments in 36 out of 63 reporting jurisdictions thus, any developments in equity and bond markets therefore affect investment returns of pension funds[6].

2.2.1 Performance of International Equities – Q2. 2019

At the start of the quarter, global stocks came under heavy pressure as they reacted to the U.S. - China trade tensions and news of plans to add tariffs on goods from Mexico. Specifically, in early May 2019 (Table 2 below), the breakdown in trade talks with China set-off a shift towards safe haven assets, sending U.S. stocks to their worst May performance in nine years[7].

[5] http://www.oecd.org/daf/fin/private-pensions/Pension-Funds-in-Figures-2019.pdf

[6] OECD Report on Pension Fund Assets Performance 2018

[7] http://www.mrminv.com/commentary/index.html

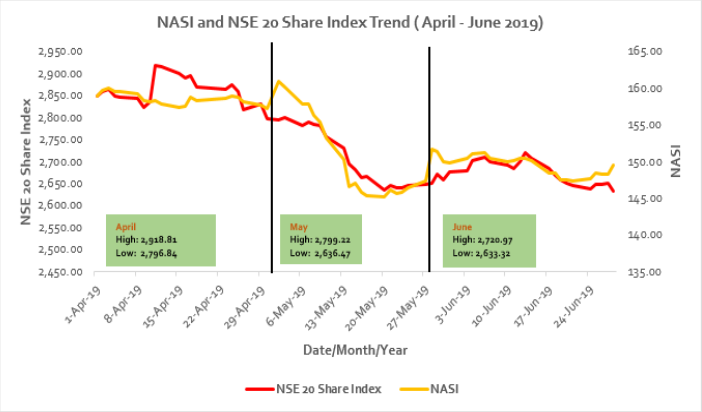
Table 2: Performance of International Equity Markets[8]

Stock Market Indices 2019				
Index	**Country**	**May**	**June**	**YTD**
S&P 500	US	-6.6%	6.9%	17.3%
Dow Jones Ind Ave	US	-6.7%	7.2%	14.0%
NASDAQ	US	-7.9%	7.4%	20.7%
FTSE100	UK	-3.5%	3.7%	10.4%
FTSE250	UK	-4.3%	2.6%	11.2%
DAX	Germany	-5.0%	5.7%	17.4%
CAC40	France	-6.8%	6.4%	17.1%
Nikkei 225	Japan	-7.4%	3.3%	6.3%
Hang Seng	Hong Kong	-9.4%	6.1%	10.4%
Shanghai Composite	China	-5.8%	2.8%	19.4%
Sensex	India	1.7%	-0.8%	9.2%
Ibovespa	Brazil	0.7%	4.1%	14.9%
RTSI	Russia	3.1%	7.3%	29.2%

Data source :Morningstar

The negative sentiment across global markets manifested itself with developed and emerging market equities ending lower for the month of May 2019.

Fig 11: Trend of the NASI and NSE 20 Share Index (April – June) 2019



Source: NSE/CMA

An assessment on the trend of the NASI and NSE 20 Share Index (*fig 11 above*) shows a general decline in the index during the quarter under review, depicting a possible correlation between movements in foreign indices, particularly the US, noting that the Kenyan securities market is mainly driven by foreign participation with the average foreign investor participation between January and May 2019 surmounting to 73 percent.

2.2.2 *Performance of International Bonds – Q2.2019*

Carrying forward their downward trend, global bond yields fell further in June 2019 including in markets like Japan, Germany and Switzerland. There is an anticipation that the Federal Reserve could cut rates in July, on the strength that the U.S. and global economy have never been stronger (record employment and best economic/GDP growth since the financial crisis) and on the other hand that cheap money/lower interest rates are required to stimulate the economy.

Table 3: Bond yields in selected countries

Country	10-year yield	June 2019 Change	1-year Change
United States	2.00%	-0.23%	-0.84%
United Kingdom	0.83%	-0.06%	-0.47%
Japan	-0.16%	-0.07%	-0.19%
Germany	-0.32%	-0.15%	-0.63%
Switzerland	-0.64%	-0.08%	-0.54%
France	0.01%	-0.24%	-0.68%
Italy	2.09%	-0.56%	-0.56%
The Netherlands	-0.16%	-0.18%	-0.62%
Canada	1.47%	-0.11%	-0.67%
India	6.88%	-0.25%	-1.02%
Mexico	7.57%	-0.39%	-0.18%
Brazil	7.47%	-1.03%	-4.14%

Source: TTID[9]

Fig 12: Trend of the German 10-Year Bond Yield (Q3. 2016 – Q2.2019)

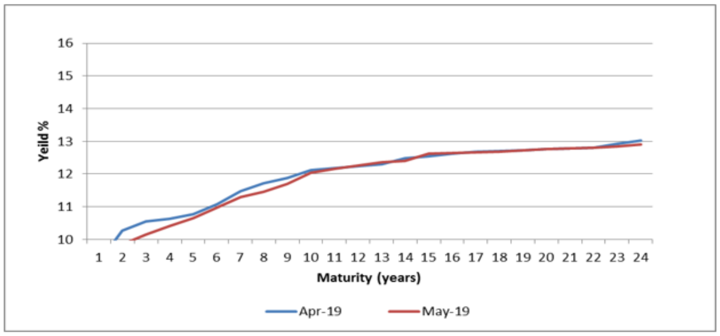
[8] https://www.ii.co.uk/analysis-commentary/fund-ive-bought-capitalise-us-boom-ii508570

[9] https://thistimeitisdifferent.com/highlights-from-june-2019

2.2.3 Opportunity for Global Pension Funds to invest in Emerging Markets and Kenya

While the yield in bonds in major international markets recorded lowest levels during the quarter, Kenya's bond yield was on an upward trajectory in April and May 2019 as shown in figure 21 below.

Fig 21: Bond Yield Trend in Kenya – April and May 2019



Source: NSE

The same can be said of most emerging markets that have ended up attracting foreign capital linked to the relatively high yield offered in these markets.

Observation;

- Unlike the positive correlation depicted in the equities market, Kenya's bond yields are more favorable and continuously present an alternative destination for foreign capital. This was confirmed in May 2019 when Kenya's $2.1 Billion Eurobond was admitted on Euronext Dublin, Ireland's main stock exchange effective 22nd May 2019.The bond, which was oversubscribed by 4.5 times, was split into two tranches of 7-year and 12-year tenors; the 1st issue was a $900 million paying a coupon of 7% while the second $1.2 Billion was priced at 8%. It was the country's third issue in the European capital Markets[10].

Lesson Learnt;

i. *With the German Treasury Yield curve delivering negative yield for the first time in its history and with similar trends across the globe, there is an opportunity for international capital to flow into Kenya in search for yield. It is therefore incumbent on the Kenyan industry to avail the products and promote the confidence in governance, infrastructure and liquidity to facilitate this type of investment.*

ii. *Global pension funds should therefore consider investing in the region to take advantage of the opportunities presented by the Capital Markets in emerging markets. To tap into this opportunity, the Authority, in collaboration with other financial sector players is considering modalities of engaging foreign pension funds to explore Kenya as an investment choice destination.*

2.2.4 Brief Analysis of the Kenyan Population and the Pension Sector and opportunities presented through the G20 Fukuoka Principles

According to the third Medium Term Plan, Kenya's population is projected to increase to 50.8 million by 2022 from 45.9 million in 2017. The population of those less than 15 years is estimated at 20.3 million in 2018 and is expected to increase to 21.5 million in 2022 while youthful population is expected to increase to 19.3 million in 2022 from 17.5 million in 2018. The population of elderly (65+ years) is estimated at 1.4 million in 2018 and projected to increase to 1.6 million by 2022[11]

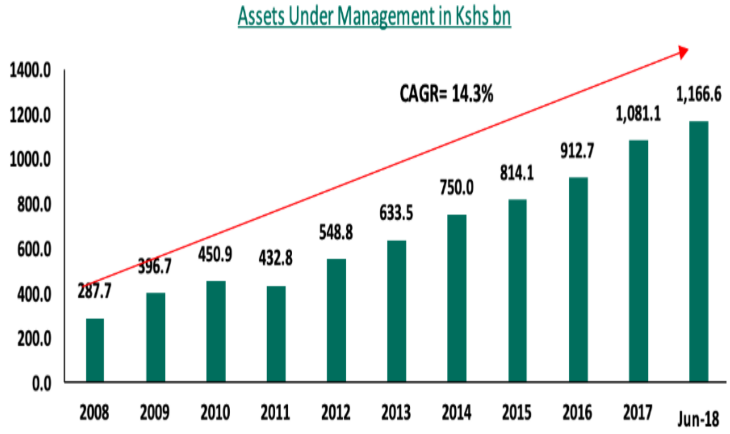
Guided by these statistics Kenya can incorporate some of the G20 Fukuoka Principles in its engagements with the pension sector. The Kenyan pension industry has made significant strides in developing the Kenyan pension sector as evidenced by significant growth from both member contributions and good performances leading to the assets under management growing to Ksh 1,166.6 bn in 2018, from Ksh 287.7 bn 10-years

[10] https://kenyanwallstreet.com/irish-stock-exchange-admits-kenyas-third-eurobond/

[11] Kenya Medium Term Plan III

ago, which is a compound annual growth rate of 14.3% over the 10-years.

Fig 13: Asset allocation by Retirement Benefit Schemes in Kenya



Changes in the Asset Allocation by Retirement Benefits Schemes in Kenya

However, despite the immense growth, the penetration rate of the Retirement Benefits Schemes remains low at 15.0% of the adult population, indicating that most Kenyans are yet to subscribe to a formal Retirement Benefits Scheme. More recently in July 2019, the Government of Kenya, in conjunction with the Retirement Benefits Authority stated that plans are underway to work on forming a partnership with pension funds in the United States of America, South Africa and the United Kingdom to facilitate Sh25bn in investments in infrastructure, real state and affordable housing over the next four years[12].

Observations;

Over the years, the Authority has conducted capital markets investor, behavioral and situational analysis studies that have informed decision making and strategy setting to inform targeted investor education activities for existing and potential investors.

- Noting Kenya's greatest population is the youth, the Authority has made targeted efforts towards engaging youth to consider the capital markets as a savings and investment destination. This was evidenced in the FY 2018/19 where the Authority conducted a country wide University challenge targeting universities across Kenya. Through such engagements, the Authority continues to create awareness on Capital Markets products such as Collective Investment Schemes as saving instruments for the retail market.

Lessons Learnt:

i. *Despite Kenya's rich youthful population, the Government of Kenya is also facing significant pension related costs following the retirement of staff from the public service. This presents an opportunity for the financial sector to develop products through which the Government of Kenya can be able to sufficiently and sustainably process pension requirements of retirees within reasonable time.*
ii. *Further, the asset base of Kenya's pension industry has significantly grown over the years. Trustees should be educated to consider mobilizing capital to finance the domestic economy. This can be done through investments in Capital Markets instruments and other emerging securities/instruments for maximum returns for the pensioners.*
iii. *The non-bank financial services sectors in Kenya are well placed to adopt some of the forwarded priorities by Fukuoka to expand the scope of financial literacy across the different demography of investors in the country for increased uptake and overall contribution to Kenya's GDP.*

3. Rising Concerns on Cybersecurity – Statistics, Risk Management Mechanisms and solutions for the Capital Markets

Cybersecurity issues are becoming a day-to-day struggle for businesses. Trends show a huge increase in hacked and breached data from sources that are increasingly common in the workplace, like mobile and Internet of Things devices. Additionally, recent research suggests that most companies have unprotected data and poor cybersecurity practices in place, making them vulnerable to data loss.[13]

[12] https://www.capitalfm.co.ke/business/2019/07/kenyas-pension-funds-urged-to-invest-in-infrastructure/

[13] https://www.varonis.com/blog/cybersecurity-statistics/

Average expenditures on cybercrime are reported to be increasing dramatically, with costs associated with such crimes crippling to companies who have not made cybersecurity part of their regular budget.

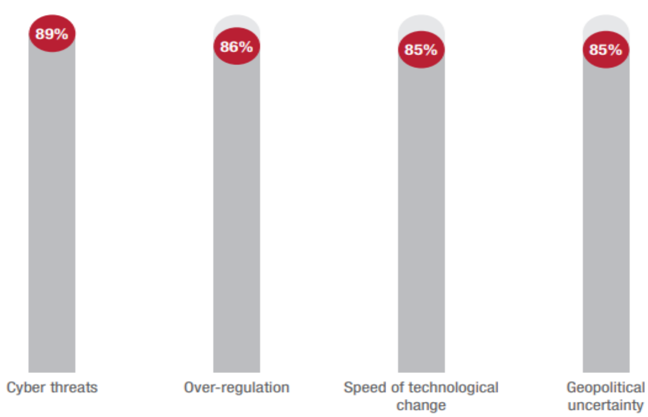
3.1 Impact of Cyber Threats on capital markets

According to a study published by the International Organization of Securities Commissions (IOSCO) research department and the World Federation of Exchanges office in June 2019, around half of the world's securities exchanges were the subject of cyber-attacks in 2018.

Cyber threats in capital markets are seen to lead to manipulation of order management systems leading to incorrect feeds, false orders/ non-submissions, and corruption of trade surveillance systems thus enabling manipulative, illegal and abusive trade practices. All this can result in triggering automated rogue trading strategies, thereby increasing the chance of flash crashes.

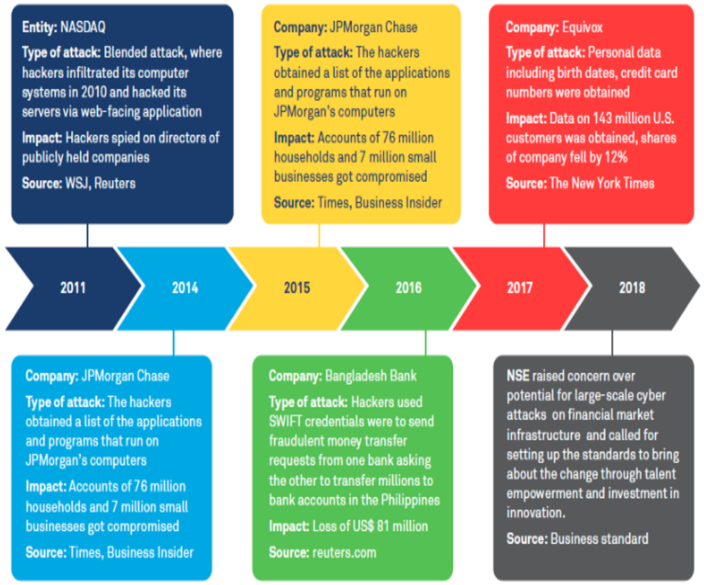
The cybersecurity landscape for asset and wealth management firms is also fraught with an array of threats aimed at stealing or compromising clients' investment or personal data. With the growing adoption of wealth management applications on mobile and via cloud-based services, attacks like Distributed Denial of Service (DDOS), ransomware and phishing are equally gaining popularity[14].

Fig 14: What's keeping banking and capital markets CEOs up at night?



Source: PwC's 2019 21st CEO Survey: Key findings from the banking and capital markets industry

Fig 15: Impact of cyber threats on capital markets



Globally, regulatory members of IOSCO have been kept abreast with developments in cybercrime in order to set sound risk management frameworks. In 2016, the Committee on Payments and Market Infrastructure (CPMI) developed and disseminated guidance on cyber resilience for financial market infrastructures to its members.

The guide provided supplemental detail related to the preparations and measures that FMIs should undertake to enhance their cyber resilience capabilities with the objective of limiting the escalating risks that cyber threats pose to financial stability[15].

Further in October 2017, IOSCO Board established a Cyber Task Force (CTF) whose mandate was to raise awareness of existing international Cyber guidance and encourage the adoption of good practices among the IOSCO regulatory community. This feature purposes to present the identified good practices to practitioners in the industry as a guide towards enhancing internal cyber risk exposure.

[14] https://www.wipro.com/securities-and-capital-markets/cybersecurity-essentials-for-capital-markets-firms-in-the-digital-age/

[15] https://www.bis.org/cpmi/publ/d146.pdf

Fig 16: Core Standards used by the Market in Cyber Risk Management

Comparison of the Key Characteristics of the Core Standards

	NIST	CPMI-IOSCO	ISO
Developed by	U.S. non-regulatory agency	International standard setting bodies	Independent, non-governmental, worldwide federation of national standards bodies
Designed for	Originally aimed at operators of critical infrastructure	Financial market infrastructure	All sectors, public and private
Cost	Free	Free	Charges apply to most standards
Approach	Framework	Principles/Guidance	Framework, Menu of Controls, and Guidance
Updates	Updated April 2018	Not currently planned	Periodic updates
Single or Multiple Standards	Framework referencing variety of standards	Single set of guidance supplementing PFMI	Framework and Set of standards

Source: IOSCO

- i. *NIST Standard – National Institute of Standards and Technology;*
- ii. *CPMI-IOSCO Standard – Committee on Payments and Market Infrastructure of IOSCO*
- iii. *ISO and IEC Standard – International Organization for Standardization and International Electrotechnical Commission*

In 2018, WFE published a set of best practice guidelines on the behavioral aspects and preventative methods for encouraging employees to comply with Cyber protocols.

The financial securities sector is interconnected, and therefore Cyber Security practices in one jurisdiction are likely to have potential consequences for the capital markets sector in other jurisdictions[16].

Through a survey conducted on member jurisdictions earlier in the year, common cyber risk management policies were forwarded as solutions in managing the risk and challenges posed by cybersecurity attacks. The elements are well summarized in fig 15.

Fig 17: Cyber Risk Management Enabling Frameworks

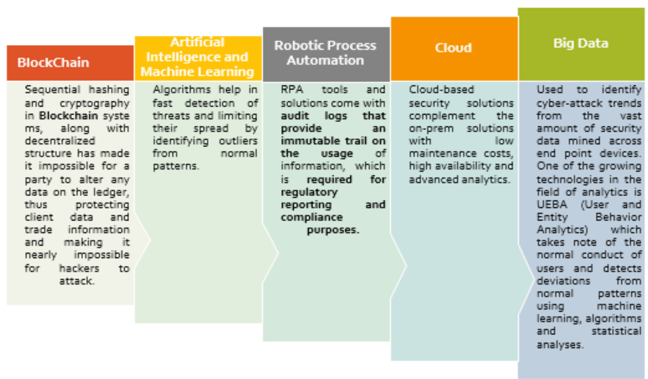
Source: IOSCO

3.2 Kenya's Experience with Cyber Security and Risk

The latest report by cybersecurity firm Serianu shows the cost of cybercrime in Kenya in 2018 was Sh30 billion, while anticipating that organizations could lose more in the coming years.

The report indicates that only 1700 cyber security skilled professionals are certified in Kenya with 60 per cent of companies set to experience a shortage of cybersecurity professionals this year especially at senior and mid-management levels.[17]

Fig 18: Technology based Solutions to Cyber Threat



[16] https://www.iosco.org/library/pubdocs/pdf/IOSCOPD633.pdf

[17]

Observations;

- While we note that complete prevention of cybersecurity is utopia, there is need for substantial investment in the prevention of cybersecurity attacks both at a firm level and at a National Level.
- Great strides have been made by the Government of Kenya in the last financial year towards establishing cybersecurity and data protection regulations. Specifically, in 2018, the Government developed two bills namely;
  i. ***The Computer Misuse and Cybercrime Act through which a National Computer and Cybercrimes Co-ordination is established.***
  ii. ***Data protection bill 2018 that establishes the Office of a Data Protection Commissioner***
- While there are commendable steps towards attaining security of systems, hardware and data, concerns have been raised by practitioners in the industry on certain clauses that seem to breach data security rights of the citizenry. This saw the freezing of some sections of the Computer Misuse and Cybercrime Act by the courts.

Lessons Learnt:

i. *Evolved, innovative and sophisticated cybercrimes involving crimeware, resources, and implicit help can only be curbs with surveillance, hands-on defense mechanism, regulation, and awareness.*

ii. *Seasonal brainstorming drills, awareness generation roundtables, regular surveying, powerful regulations, promotion of preventive measures, more cyber-crime insurances, and active measures like ethical hacking, storage encryption, firewalling, intrusion prevention, anti-ransomware & anti-malware programs, will help to vanguard capital markets from such attacks.*

4. America's Long-Term Exchange – The Newest Stock Exchange in Town Promoting Long-term Investments

On May 10th, 2019, American based Long-Term Stock Exchange (LTSE), received approval from the Securities and Exchange Commission to operate a U.S. national securities exchange.

Forwarded literature shows that the process towards the establishment of LTSE started in 2016 when a startup backed by prominent Silicon Valley companies initiated the process of creating a new US stock exchange, one with additional rules for companies and investors designed to reward long-term shareholding and business strategies to generate long-term results.

The launch of the exchange is a culmination of discussions among US tech startups that have long wanted to overhaul the process for firms to list their shares and to find ways to minimize pressures on public companies from high-frequency trading, cynical activism, and any distorting incentives of quarterly results.

This stems from historical attempts by tech firms to limit public shareholding in their companies. In 2004, Google tried an unusual Dutch auction for allocating some shares in its initial public offering. In 2012, Facebook tried to reduce the control of investment bankers in its IPO.

Silicon Valley founders have used separate share classes to retain control of their companies once listed, which they argue is critical for piloting a business amid harmful short-term pressures [18] - a key disadvantage forwarded by the firms with regard to going public.

The newly launched LTSE prescribed that the exchange and listed companies would have to satisfy all of the normal SEC requirements that would allow shares to trade on other regulated US stock markets. However, companies that list on the LTSE would agree to additional requirements that the SEC would enforce.

LTSE intends to use its regulatory powers to try and create incentives for long-term thinking by both managers and investors with the aim of stakeholders agreeing to the idea that companies are managed in a more long-term way.

LTSE is established to have a number of differences from a traditional stock exchange including;

[18] https://qz.com/704657/eric-ries-ltse-long-term-stock-exchange/

i. **Tenured shareholder voting power**, meaning that a shareholder's votes would be proportionately weighted by the length of time the shares have been held.

ii. **Mandated ties at listed companies** between executive pay and long-term business performance.

iii. **Additional disclosure requirements** that allow companies to know who their long-term shareholders are and investors to know what investments the company is making.

Further, to promote initial listings and trading, the LTSE will allow companies to have dual listings, with their shares also trading on any other US regulated market, such as the NYSE or Nasdaq.

4.1 The Argument Against Current Initial Public Offering Set up in the United States

Proponents of LTSE argue that when companies go public, people stop thinking about them as companies, and start thinking about them as stocks; with propositions that this is the equivalent of judging people only by looking at their reflection in one specific mirror, while at the same time having no idea how distorting that mirror actually is.

The argument forwarded is that many traders, especially in the high-frequency and algorithmic spaces, don't take time to think about what the company might actually do from a long-term perspective as they buy and sell ticker symbols, and help to drive correlations up to unhelpful levels.

The resulting impact is that CEOs get judged in large part by what the stock market in general is doing, rather than what they are doing in promoting the long-term sustainability of the firm. As a result, CEOs of public companies have to spend an enormous amount of time on outward-facing issues, dealing with investors, analysts and journalists while generally being accountable to their shareholders[19].

4.2 Interim Tested Solutions towards Capital Raising other than Initial Public Offerings

It is for this reason that the business of raising capital, particularly by some tech firms has evolved, aided by technological developments – **blockchain platforms**. One of the most significant introductions that blockchain has made available in recent years is adding new tools through which companies can raise capital.

The technology has made it possible to raise funds for a project from investors of just about any pocket size through initial coin offerings (ICOs) as well as security token offerings (STOs).

Typically, investors put in their money not just in return for a big payday, but they're usually believers in the project as well. As a result, a community of investors is created upon which new projects are built. This is usually not the case in the traditional investment sphere.

Another argument given is that initial public offerings target already established companies with huge profit margins, hence the craze for mark up prices amongst traders. As a result, early stage and middle-sized companies seeking capital for expansion growth are left in the periphery as investors place their bets on company size and short-term value.

4.3 Business Proposition by LTSE

Bottomline, LTSE is looking towards attracting the sort of committed, in-for-the-long-haul investors that have been witnessed within the crypto space but through widely acceptable investment tools.

This could well prove to be a revelation for the crypto industry, since many companies operating in the space possess the characteristics that LTSE is after: early stage, sizeable long-term growth potential.

LTSE is said to be building a structure that would encourage growing companies to attract and reward long-term, patient capital in the public market with the stock exchange. It believes its own approach will help build more sustainable companies. Critics have however raised two key concerns;

i. That the exchange is likely to be targeting US based companies only based on its requirements – presenting

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[19] http://blogs.reuters.com/felix-salmon/2012/07/17/why-going-public-sucks-its-not-governance-issues/

a myopic vision for the larger securities market in the United States.

ii. That listing at the exchange is likely to be costly noting the additional new requirements that come along with it.

Observations

- Most analysts seem to find the concept forwarded by LTSE as absurd and unlikely to be implemented in the long run. However, concerns raised by the tech firms could be valid and need a second thought.
- In a number of jurisdictions, save for countries like India, Australia, Indonesia, China, Korea, Japan, Philippines, Thailand, Malaysia and New Zealand – there has been a slowdown in IPO activity with Sub Saharan Africa being the most affected destination.
- Instead, alternative capital raising options have grown in the recent past to include private equity, venture capitalist firms and more recently online crowdfunding platforms that are perceived to facilitate easier access to capital for companies under limited or no regulation.

Lesson Learnt;

- *While the rise of activity in these industries is considered complimentary, it is time the Capital Markets considers restructuring and re-evaluating the benefits its offers both investors and issuers to ensure that the interests of both are at the core of its activities, particularly initial public offerings.*
- *At the local level, the Capital Markets Authority Kenya has in the last year assessed the latent demand for capital markets products through research and stakeholder engagement with the aim of improving uptake of capital markets products and services.. Noting the urgency of the matter, the Authority has re-structured its functions, with a key component being the creation of a dedicated team of staff charged with the mandate of spearheading the market deepening agenda. This is expected to yield results as the team focuses on finding missing gaps within the market, identifying appropriate solutions and implementing the same for the prosperity of the Kenyan capital markets.*

5. Key Global Economic and Financial Markets Stability issues

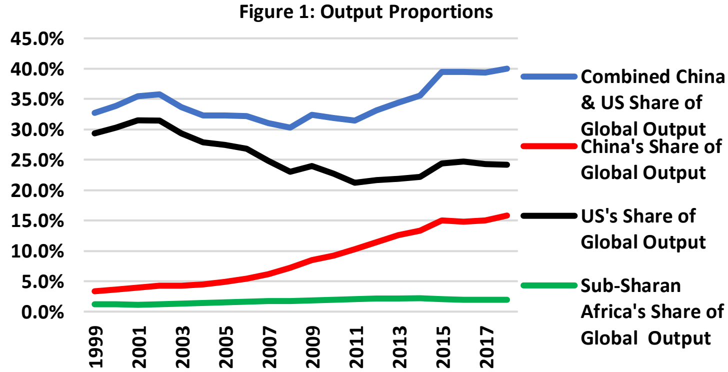
5.1 Guest Column - By Jared Osoro, Director of Research and Policy, Kenya Bankers Association (KBA)

The Trade Wars and Global Financial Flows

It was obvious that when the United States (US) Government launched a trade war with China the ramifications were going to be far reaching. This isn't a bilateral affair, cognizant that the combined output of these two economies as at the end of 2018 is estimated at 40 percent (Figure 1). Two decades ago the US was arguably the only systemically important global economy such that if it were to be embroiled in financial or economic volatility, there would be negative spillover effects to the rest of the world.

Not any longer. China has steadily grown in stature, its share of global output rising from 3.3 percent in 1999 to about 16 percent as at the end of 2018 while that the share of the US was 29 percent and then declined to 24 percent for the corresponding period. This therefore means that the adverse economic cost of the trade war will be felt by both economies, reverberating across the global economy with a potentially higher adverse effect.

Figure 1: Output Proportions



Source: IMF World Economic Outlook, April 2019; Output at Current Prices (USD)

The trade war begun in 2018 when US imposed tariffs on three "lists" of goods from China. The sequential tariff increases first targeted USD 34 billion of annual imports, then USD 16 billion more, and eventually an additional USD 200 billion. As a result, US imports from China have declined quite sharply in all three groups of the goods on which tariffs were imposed. The lag between announcement of the tariffs and their implementation or when the tariffs are phased have seen imports increase ahead of the effective dates as importers stocked up in advance. Subsequently, there have been sharper declines in imports.

As was widely anticipated, China imposed retaliatory tariffs, with the attendant consequence of US exports to China declining. Unlike the case for US that has been characterized by front-loading dynamic that eventually ended up in import declines, US export growth to China has been generally weaker since the trade tensions began.

With no sign that the trade tension between the two dominant economies will abate soon, the question that is in the mind of watchers of the global economy is: ***how quick will the negative effects filter to the global economy, and especially to economies that see themselves as peripheral and therefore way from the trade war frontline? What does it mean for global financial flows?***

At the global level, the verdict of the IMF World Economic Outlook (April 2019)20 is that the trade war has had a substantial contributory effect to the reversal of the good fortunes of the world output growth.

The global economy expanded by almost 4 percent in 2017 and is estimated to have slowed down to a 3.6 percent growth in 2018 and projected to grow at 3.3 percent in 2019. The escalation of the US - China trade tensions has compounded the already fragile environment as reflected by macroeconomic stress in Argentina and Turkey, disruptions to the auto sector in Germany, tighter credit policies in China, and financial tightening alongside the normalization of monetary policy in the larger advanced economies.

The Frontline and Beyond

The first order effects of the trade war are already evident. Consumers in the US and China have started bearing the blunt. In the case of the US, a recent study (Amiti, Redding and Weinstein, 2019)21 indicates that US tariffs were almost completely passed through to US domestic prices, implying that the entire incidence of the tariffs fell on domestic consumers and importers up to now, with no impact so far on the prices received by foreign exporters. The study further finds that:

a. US producers have responded to reduced import competition by raising their prices, and
b. There has been a reduction in US real income of USD 1.4 billion per month by the end of 2018, accompanied by similar patterns for foreign countries who have retaliated against the US, which indicates that the trade war also reduced real income for other countries.

Central to the effect of the trade tension on other countries beyond the frontline, the second order effects, is the so-called "trade in tasks". Over the period that China has been gaining ground on the US in terms of share of global output, the shape of globalization has evolved beyond the expansion of international trade and finance. It's common place now to see geographical fragmentation of the production processes within networks of firms associated through contractual arrangements or belonging to a transnational corporation. That means specific industrial operations – from conception to final products' assembly – are no longer undertaken by a single establishment but increasingly outsourced within these global value chains -hence "trade in tasks".

The implication of the "trade in tasks' is that a substantial portion of the world trade in merchandise (excluding oil and other primary produce) is attributed to intermediate goods. The underlying linkages have taken prominence in the so-called "new economy", characterized by a rapid pace of technological change, and a closer integration of capital, labor and product markets.

Therefore, beyond the price and welfare effect as outlined, the production effect is the channel through which the trade tension will propagate itself to the rest of the world. As some

[20] IMF (2019) *World Economic Outlook*, April. https://www.imf.org/en/Publications/WEO/Issues/2019/03/28/world-economic-outlook-april-2019

[21] Amiti, M., Redding, S. J and Weinstein D. (2019), "The Impact of the 2018 Trade War on US Prices and Welfare", *NBER Working Paper Series*, Working Paper 25672, March https://www.nber.org/papers/w25672.pdf

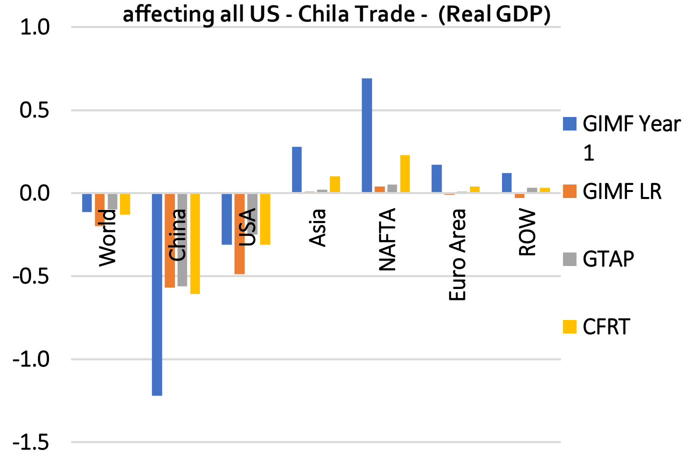
have argued (Cerutti, Gopinath and Mohommad, 2019)[22], the effect on producers is mixed, with some winners and many losers. For those US and Chinese producers of goods competing in domestic markets with imports affected by tariffs, as well as competing third country exporters, the tariffs are a boon; but for those US and Chinese producers of the goods affected by the tariffs as well as producers that use those goods as intermediate inputs, the tariffs are a bane.

Even as winners and losers can be picked, the channels through which tariff wars affect production gives a better context on which direction the loses – gains tradeoffs lean. The two prominent channels are:

a. Trade diversion channel. Here, the decline in imports from China could have been offset by an increase in imports from other countries, and a similar offsetting effect on the part of China's exports from the US. It remains to be seen whether this will be sustained for as long as the tariff war persists.
b. Market segmentation channel. The segmentation happens in price of traded goods. Take the case of a country (China) importing a similar product (soybeans) from two countries (US and Brazil). If soybeans the product is targeted in the tariff war, then the price of the produce in the exporting economy will collapse and remain either constant or even rise in the other exporting economy. This is how Brazilian farmers have gained out of the trade war and the US farmers have lost, even when prices are converging.

Overall, the welfare and production effects of trade wars and the uncertainties over how long they may persist are at the core of the negative growth outlook as earlier noted. As the IMF shows (Figure 2), even with some winners, the net effect is largely negative with the impact being large in the systemically important economies. The negative effects in China and the US more than offsets the positive effects in in NAFA, Euro Zone and the Rest of the World in a simulating where there is a 25 percent tariff increase for all US and China trade; this is reflected in the World macro effect.

Figure 2: Macro Effects of a 25% Tariff Incresee affecting all US - Chila Trade - (Real GDP)



Source: IMF

IMF's GIMF = Global Integrated Monetary and Fiscal model; GTAP = Global Trade Analysis Project; CFRT = Caliendo, Feenstra, Romalis, and Taylor model23; LR = long run; NAFTA = North American Free Trade Agreement; ROW = Rest of the World

From the Real Economy to Financial Flows

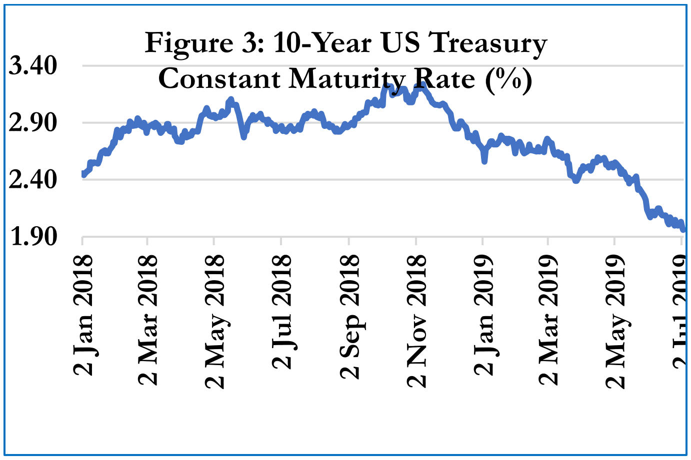
The initial filtering of the trade war into the financial markets is by way of how markets perceive US producers with significant exposure to Chinese markets and the reflect that in stock market valuations. As Cerutti et. al., (2019) observe, the equity price performance of US companies with high sales to China underperformed relative to US businesses exposed to other international markets, after tariffs linked to the USD 34 billion retaliation list by China were implemented. They note that the performance gap narrowed at the beginning of 2019 with a potential trade truce but reopened again after the US tariff increase to 25 percent on the USD 200 billion list was announced.

Arguably, the biggest influence of the trade war on financial flows is hinged on the likely policy response to market behavior. The Federal Reserve has clearly changed course from the anticipated rate hikes in 2019, instead holding the rates in March and June 2019. The reason for that is the gloomy global

[22]Cerutti, E., Gopinath, G. and Mohommad, A., (2019), "The Impact of US-China Trade Tensions" https://blogs.imf.org/2019/05/23/the-impact-of-us-china-trade-tensions/

[23]Caliendo, L., Feenstra, R. C., Romalis, J. and Taylor. A., (2017). "Tariff Reductions, Entry, and Welfare: Theory and Evidence for the Last Two Decades." *NBER Working Paper 21768*, April https://www.nber.org/papers/w21768.pdf

economic outlook pinned on the inability of the US and China to strike a deal regarding the ongoing trade war. Beyond the equities market the of pain the trade war could be inferred from the decline in the 10-year US Treasury yields as investors anticipate a rate cut and flee for safety (Figure 3).

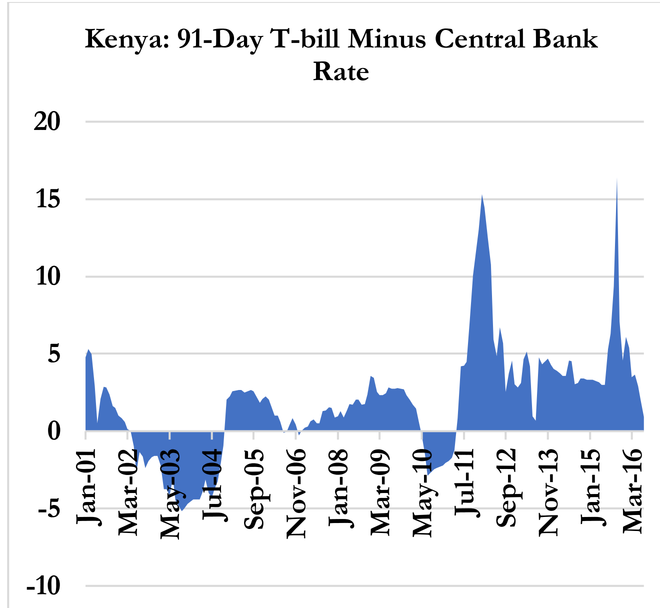


Source: Federal Reserve

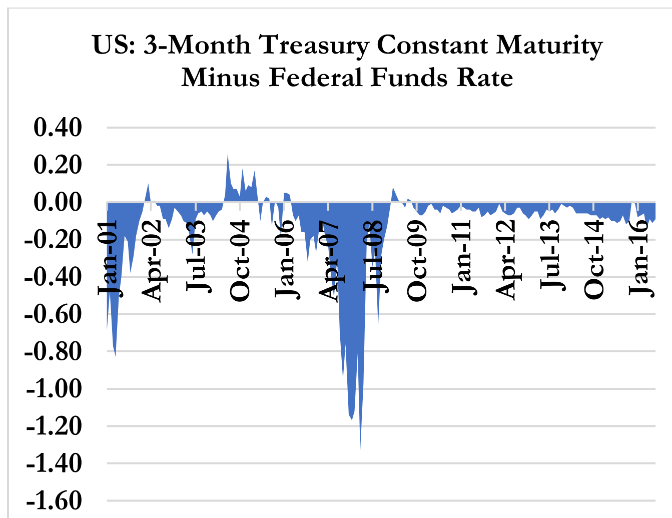
The response of the Fed is to be seen in the context of the debate as to whether it responds in a manner that gives that its monetary policy stance is influenced by traders – and politicians too seeking a rate cut – or it should stick to a policy direction as would be informed only by the backward-looking economic date that moves slowly. If the Fed listen to the markets even as it looks at the hard data on growth and inflation, then we are seeking a possibility of a lower interest rates regime – which prevails too at the Eurozone as signaled by the European Central Bank (ECB) in the face of economic challenges in Europe as well as the Bank of England (BOE) in the face of uncertainty over Brexit.

Does this then imply that the trade-war triggered low interest rates regime will lead to portfolio flows to emerging as well as frontier markets as was the case during the 2007 – 2008 global financial crisis and the subsequent period? Superficially, if you take the largely positive short-term spreads between market rates and policy rates in the case of a frontier market such as Kenya compared to the spreads for the same tenor of market rates versus policy rates that are largely negative (Figure 4), then you could expect resource flows to the former from the latter.

Figure 4: Interest Rate Spreads



Source: Central Bank of Kenya; Federal Reserve



However, the clearer picture is seen by looking beyond the superficial implication of positive interest rates differential in favor of emerging and frontier markets. In particular, the role that China will play in the global financial markets going forward is important to appreciate. Just as China is stamping its authority in its influence on the global output, its stature in the global financial space is now noticeable. Effective October 1, 2016, the Chinese renminbi (RMB) met the criteria for inclusion in the IMF's Special Drawing Rights (SDR) basket – joining the USD, the euro, the Japanese yen, and the British pound sterling. The SDR basket is reviewed every five years, or earlier if necessary, to ensure that it reflects the relative importance of currencies in the world's trading and financial systems.

Most notably, China is systematically embedding itself into the global financial markets in a manner that will influence overseas investment, improved liquidity, better governance, and a lead to broader range of instruments. There is a deliberate endeavor to include Chinese stocks and bonds in several global financial-market indices. As Chinese securities are added, investors seeking to match or surpass the returns of the indices will adjust their portfolios to include Chinese stocks and bonds. Thanks to these benchmark-driven asset managers, China's portfolio flows are being globalized.

Over the past half a decade, foreign ownership of Chinese government bonds has quadrupled (Chen, Drakopoulos and Goel, 2019)24. Ownership of onshore equities has also increased but remains low compared with other emerging markets. As Chen, et.al (2019) argue, this trend of rising foreign ownership is likely to accelerate further. Evidence to that effect is in the move in April 2019, to include two types of Chinese bonds in the Bloomberg Barclays Global Aggregate Index—local currency-denominated bonds issued by the central government and by state-owned policy banks such as China Development Bank. It is also anticipated that there will be an inclusion of Chinese bonds and equities into FTSE and JP Morgan indexes, a move that will substantially boost portfolio inflows into the economy.

These developments have the real possibility of seeing investors reducing the purchases of other emerging-market assets as they undertake portfolio rebalancing to reflect China's inclusion. This will be especially so in cases where benchmark-driven holdings constitute a significant amount of their foreign debt. Cognizant that benchmark-driven investors tend to be more sensitive to changes in global financial conditions than other investors, their greater role in international finance may mean that external shocks propagate to medium-sized emerging and frontier market economies faster than in the past.

Ultimately…

Ultimately, trade, production and finance are intertwined and therefore the disruption of one affects the others. The logic that is grounded in the linkages between the three is expected to prevail even as the politics of trade take center stage. The interaction between trade and capital on the back of an increasingly integrated global economy will be such that in less financially developed economies, trade and capital mobility are complements.

Trade integration increases the return to capital and thus the incentives for capital to flow to the less developed markets in the event of returns being low in developed markets. By implication, deepening trade integration raises net capital inflows or reduces net capital outflows). It also implies that, at the global level, protectionism may backfire if the goal is to rebalance capital flows to the disadvantage of the country targeted by the trade war.

5.2 Global Growth seen weakening to 2.7% in 2019

Latest figures on the global economy indicate that the world economy will decelerate in 2019 due to among others, sustained trade tensions between the major global economies, Brexit uncertainty, geopolitical tensions, domestic political uncertainties in some of the major global economy players and weather-related shocks such as the recent cyclone Idai[25].

The fiscal stimulus measures in the United States also appear to have come full-circle, with disruptions to the automobile sector in Europe[26]; as well as other economy disruptions like power shortages in South Africa and oil production cuts by Organization of the Petroleum Exporting Countries (OPEC) and

[24] Chen, S., Drakopoulos, D., and Goel R (2019), *"China Deepens Global Finance Links as It Joins Benchmark Indexes"*. https://blogs.imf.org/2019/06/19/china-deepens-global-finance-links-as-it-joins-benchmark-indexes/

[25] This was an intense Tropical Cyclone that affected parts of Southern Africa and the Southern Hemisphere. The storm caused catastrophic damage in Mozambique, Zimbabwe, and Malawi, leaving more than 1,200 people dead and thousands more missing.

[26] Two tests Worldwide harmonized Light vehicles Test Procedure (WLTP) and Real Driving Emissions (RDE) test that replaced the New European Driving Cycle (NEDC) required all vehicle models to undergo the testing effective Sept. 1st, 2017. This requirement forced car manufactures in EU to reduce build-up of inventory, pull out cars from the market and/or stall production as they figure out ways of complying with this EU requirement.

other oil producers contributing to the anticipated global economy's deceleration.

Fig 19: Global Growth Projections

Source: World Economic Update 2019

According to IMFs World Economic update, the global l GDP growth is expected to be 3.3% in 2019 compared to 3.6% in 2018. The GDP growth is projected to be 3.6% e in 2020, an increase in 0.3% from 2019.

5.3 U.S. Economy likely to contract in Q2.2019

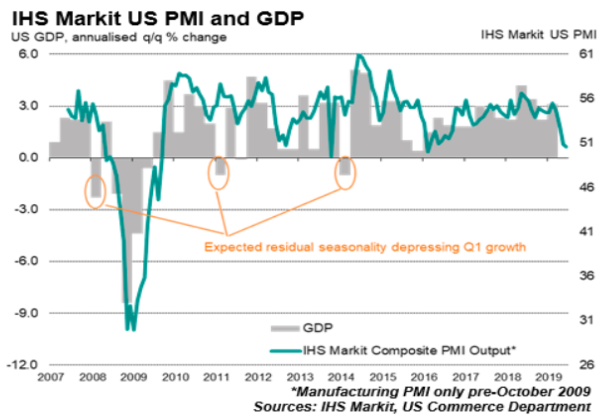
Although the U.S. is marking the 10th year of economic expansion that began in June 2009, the risk of a downturn may be on the horizon, amplified by heightened trade tensions with China and Mexico. Among the reasons for a likely drop in GDP include those highlighted below:

i. On June 3rd, 2019 the yield on the U.S. 3-month Treasury bills exceeded that on 10-year Treasury notes by the highest margin since 2007, a strong indicator that a recession might be on the horizon;

ii. The U.S. GDP growth has been modest despite stimulative fiscal policy. It is noteworthy that the federal budget deficit had shrunk to just over 2% of GDP at the end of 2015, but has now widened to about 4.5% , this is largely attributable to the big tax cut at the end of 2017 and more spending, particularly on defense[27];

iii. US Business activity edged closer to stagnation in June, according to flash PMI survey data from IHS[28] Markit. Output across the manufacturing and services economies expanded at the slowest rate since February 2016.The composite PMI output index fell from 50.9 in May to 50.6 in June 2019.The June reading rounds off a second quarter in which the PMI survey data point to the pace of economic expansion slipping to 1.4%.

Fig 20: HIS Markit US PMI and GDP – Q2.2019



Source: IHS Markit Research

iv. The yield on 10-year Treasury Inflation-Protected Securities [29]fell from 4% during the dot-com boom at the end of 1999 to below zero in 2012 and 2013. It rebounded to just over 1% late 2018 but has receded to 0.4%. When money is this cheap, it indicates weak demand for credit or an overabundance of savings—or both.

Observation;

- The risk of a downturn of the U.S. economy is on the rise, with JPMorgan Chase & Co. indicating that the probability of one beginning in the second half of 2019 has risen to 40% from 25% in early May 2019.As of 2018, Kenya was the 98th largest goods trading partner, with $1.0 billion in total (two way) goods traded during 2018. Goods

[27] https://www.bloomberg.com/news/articles/2019-06-06/u-s-economy-celebrates-10-years-of-growth-but-no-one-s-partying

[28] Information Handling Services (HIS) Markit is a global information provider that was formed in 2016.

[29] Treasury Inflation-Protected Securities (TIPS) are a form of U.S. Treasury bond designed to help investors protect against inflation. These bonds are indexed to inflation, have U.S. government backing, and pay investors a fixed interest rate as the bond's par value adjusts with the inflation rate

exports totaled $365 million; goods imports totaled $644 million. The U.S. goods trade deficit with Kenya was $279 million in 2018[30].

Lessons Learnt;

i. *Given the improving trade relations between U.S. and Kenya, where possible, CMA advocates for closer trade partnership between Kenya and the U.S., specifically in Kenya's capital markets, as a way of fostering capital markets deepening and growth for the country.*

5.4 China focusses on Stimulus to Boost Consumers, Ease Trade Risk

In April 2019, China's National Bureau of Statistics reported that the country's Gross Domestic Product (GDP) had expanded by 6.4 per cent in the first quarter of 2019, compared to a year earlier. The country's growth target range is 6.0 to 6.5 per cent for this year[31]. In January 2019, China effected fiscal and monetary policy measures including fast-tracking infrastructure projects and cutting taxes and banks' reserve requirements. Additionally, in April 2019, it was reported that China is planning to effect another fiscal stimulus by allowing local authorities to use some of the proceeds from 'special bond' sales as part of the capital for qualified major projects and encourage banks to offer loans to projects funded by the instruments. The bonds will allow local authorities to invest outside of their regular budgets and shall be repaid using the proceeds of the projects. Insurers shall also be encouraged to provide funds for qualified mid to long-term special bond projects.

The decision aims to expedite infrastructure construction by expanding the proportion of projects that can be paid for with money from the special local debt. China raised the annual special bond quota for local authorities to a record of 2.15 trillion yuan ($311 billion) in 2019.

Given China's and Kenya Government's focus on infrastructure as a key enabler of investment and growth, management will continue to engage relevant stakeholders so that they can prioritize the use of capital markets through such instruments as Asset-Backed Securities as the primary avenue of raising capital for investment in infrastructure.

6. Regional developments

6.1 AfCFTA officially comes into force

On May 30th, 2019, the African Continental Free Trade Agreement (AfCFTA) officially came into force, clearing a key procedural hurdle and being ratified by the parliaments of 24 countries. The unified market is scheduled to be launched on July 7, 2019. Under a successfully implemented AfCFTA, Africa will have a combined consumer and business spending capacity of $6.7 trillion in 2030. Africa is now home to the world's largest free trade area since the establishment of the World Trade Organization (WTO), with nearly every country on the continent joining. The remaining countries that have not joined the free trade Area are Nigeria, Eritrea and Benin.

Fig 21: HIS Markit US PMI and GDP – Q2.2019

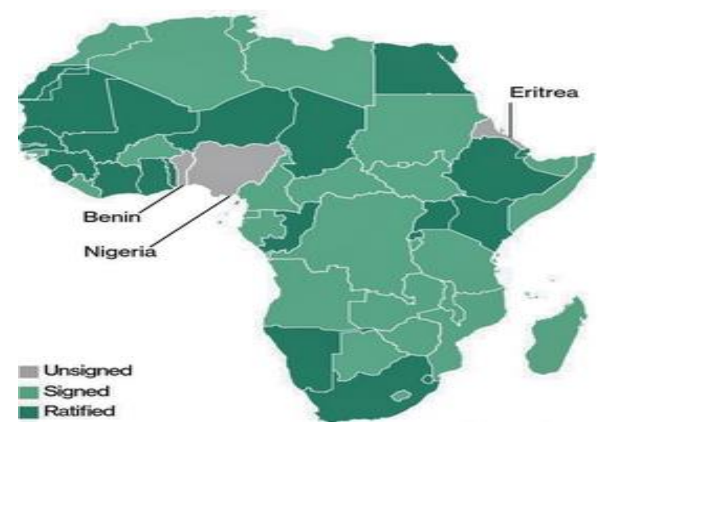
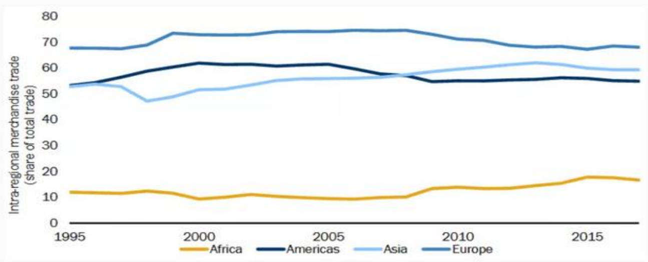


Fig 22: Level of Intra-Regional Free

[30] https://ustr.gov/countries-regions/africa/east-africa/kenya

[31] https://www.bloomberg.com/markets/fixed-income



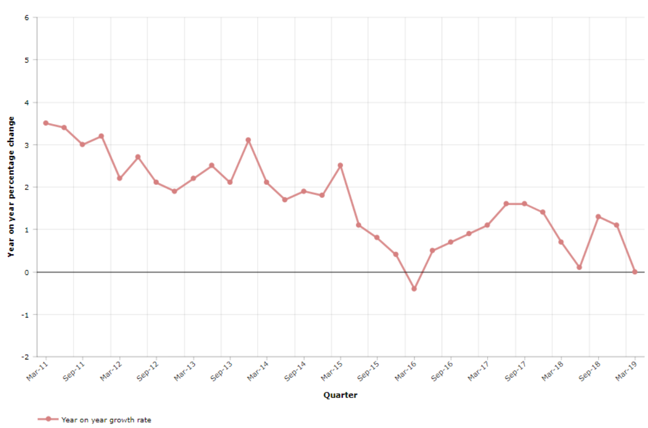
Source: Landry Signé and Colette van der Ven, Brookings Institution, "Keys to success for the AfCFTA negotiations," 2019.

Source: Gramha[32]

6.2 South Africa - Political and policy uncertainty affect growth

Statistics released in May 2019 indicate that South Africa's economy shrank by 3.2% in Q1.2019, largest contraction since the global financial crisis 10 years ago. This coupled with the ruling ANC party's mixed messaging about the mandate of the South African Reserve Bank[33], piled pressure on the Rand during the quarter, making it peak at R15.17 to the dollar on June 7th, 2019, from R14.47 on June 3rd, 2019. This also led to Moody's, the last major sovereign rating agency to hold South Africa's debt at investment grade, lowering the country's growth projections for 2019 to 1 percent from 1.3 percent.

Fig 23: Year on Year Growth in SA GDP



Source: https://www.southafricanmi.com/south-africas-gdp.html

The depressed economic performance in South Africa can be attributed to a myriad of factors including an obstructive regulatory environment as reflected by its declining position in the ease of doing business reports.

Fig 24: Trend in the Price of Crude Oil in SA

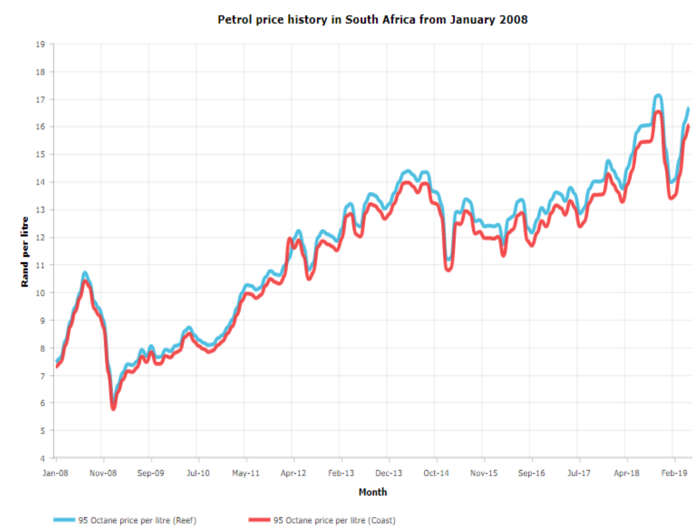
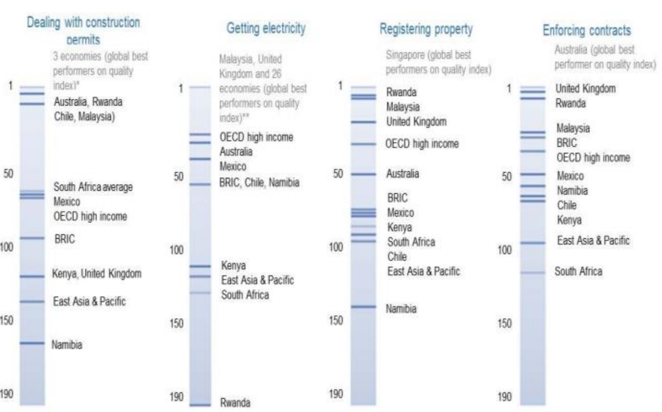


Fig 25: Quality of South Africa's Regulations – Based on Ease of Doing Business Report



Source: Investec – The Higher the Rating, the worse off the ranking

In April 2019, the South Africa Government, increased fuel levy and the road accident fund levy resulting in a general increase in cost of running both enterprises and households in the country. The IMF recently concluded that for South Africa

[32] https://gramha.net/media/2055823352866413127

[33] On June 4th, 2019 ANC Secretary General announced that ANC leaders had "agreed to expand the mandate of the South African Reserve Bank beyond price stability to include growth and employment". He also said the party wanted the Government to consider quantitative easing, a policy widely used by developed economies after the global financial crisis to stimulate growth by pumping cash back into the economy. However, the ANC issued a statement on June 6, in the name of Ramaphosa, indicating that its policy on the role of the central bank had not changed.

to see positive change in its subdued economic growth, it needs to reignite the pace of structural reform implementation, adopt policies that strengthen governance, encourage competition, increase labor market flexibility, and, more generally, reduce the cost of doing business[34]."

The country's equity market however rose 4.8% in the month of June 2019, recovering the losses experienced in May. Despite the worrying economic outturn in SA, On April 29, the Johannesburg Stock Exchange (JSE) successfully went live with a new real-time clearing platform for the JSE's Equity Derivatives and Currency Derivatives market. The launch was reported to be part of a multi-year project known as ITaC focusing on migrating all the JSE's markets to the new clearing solution, bringing a host of benefits to the market including more efficient collateral utilization, intra-day risk monitoring and improved margin transparency. The project is delivered in phases with the first asset classes to be migrated being Equity and Currency Derivative markets[35]

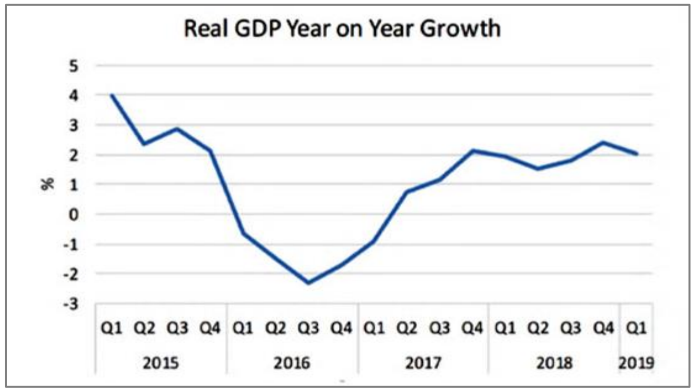
6.3 Rwanda launches the EAC Passport

During the period, Rwanda rolled out the East African Community (EAC) electronic passport as a step towards boosting faster cross-border clearance and a strategy to enhance regional integration. The country joins other EAC states—Uganda, Kenya and Tanzania that have already issued the electronic passport to their citizens. This follows a directive by EAC heads of state in March 2016 to adopt the new generation passports and phase out national documents. The launch of the new East Africa electronic passport is in adherence to specifications of the International Civil Aviation Organization. The new e-passport replaces the existing national document set to be phased out by June 2021.

6.4 Nigeria's economic growth slows in Q1 as oil sector shrinks

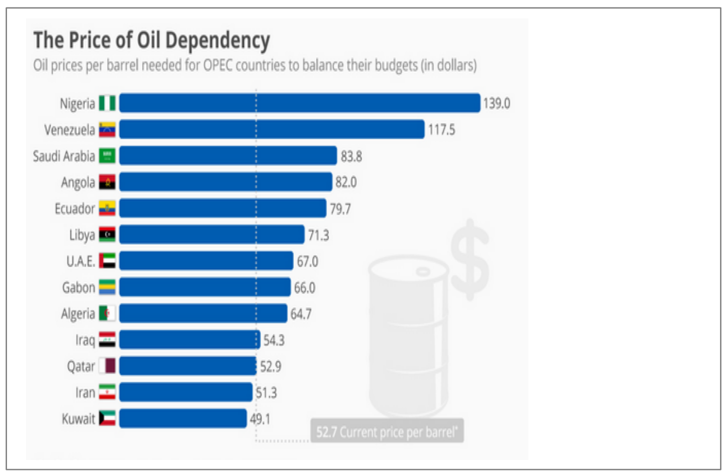
According to Nigeria's National Bureau of Statistics, in the first quarter of 2019, the country's economy grew by2.01 percent, lower than the Central Bank of Nigeria's targeted 3 percent[36]. The country's non-oil sector grew by 2.47% while the oil sector shrank 2.40%. Growth in the first quarter of 2018 was 1.89%. The country's economy is largely dependent on revenue from crude oil exports which make up over 90 percent of its earnings. The country's crude production rose to 1.96 million barrels per day from 1.91 million in the fourth quarter of 2018.

Fig 26: Nigeria's Quarterly GDP Growth



Source: Channelstv

Fig 27: Oil Dependency in Selected Countries



The largely crude-dependent economy emerged from recession in 2017 and has been recovering mainly due to higher oil prices.

[34] https://www.investec.com/en_za/focus/economy/sa-economics.html

[35] https://www.globenewswire.com/news-release/2019/05/15/1824340/0/en/Johannesburg-Stock-Exchange-launches-new-clearing-platform-from-Nasdaq.html

[36] https://www.channelstv.com/2019/05/20/nigerias-gdp-records-slow-growth-in-2019-first-quarter/

Fig 28: Nigeria Stock Exchange Index Performance

	Q1 2019 (Mar-2019)	52-Week Change (Apr-2018 to Mar-2019)
Total Market Capitalization**	N22.33 tn $61.91 bn	-10.21%
Equities Market Capitalization††	N11.65 tn $32.30 bn	-22.34%
ETF Market Capitalization	N5.66 bn $15.70 mn	-26.55%
Bonds Market Capitalization	N10.64 tn $29.50 bn	7.93%
NSE-30 Index	1,392.65	-25.70%
All Share Index	31,041.42	-25.21%
NSE Premium Board Index	2,203.76	-25.30%
NSE Main Board Index	1,420.06	-20.86%
NSE ASEM Index	807.22	-18.34%
NSE Pension Index	1,188.02	-25.03%
NSE Banking Index	403.96	-22.40%
NSE Consumer Goods Index	711.29	-27.28%
NSE Insurance Index	125.98	-16.62%
NSE Oil/Gas Index	290.52	-16.25%
NSE Lotus Islamic Index	2,267.64	-15.98%
NSE Industrial Index	1,239.73	-43.45%
NSE Corporate Governance Index	1,227.72	-26.01%
NSE-Afrinvest Banking Value Index	1,019.33	
NSE-Afrinvest High Dividend Yield Index	1,410.33	
NSE Meristem Growth Index	1,544.15	
NSE Meristem Value Index	1,388.68	
Total Volume (Q1)	20,704,972,473	-52.76%
Total Value Traded (Q1)	208,887,875,401.67	-52.50%
Avg. Daily Volume (Q1)	323,515,194.89	-53.49%
Avg. Daily Value Traded (Q1)	3,263,873,053.15	-53.24%
Avg. Daily Transactions (Q1)	3,769.72	-38.25%

Source: Nigeria Stock Exchange

Despite the above, Nigeria's main stock market index has returned -5.93 percent year to date (January 1st – April 12, 2019) and -23.9 percent in the past year (between April 2018 and April 2019), one of the worst performances globally for frontier/emerging market equities[37]. In Nigeria, statistics indicate that stocks are not a perfect proxy for the wider economy as total market capitalization of N11 Trillion represents only 8.5 percent of nominal GDP of N129 Trillion (IMF Estimates) as at the end of 2018.

6.5 Tanzania - Kenya and Tanzania to hold trade discussions in Mombasa in July 2019

Kenya and Tanzania are set to hold consultative meetings in July 2019 to resolve bilateral trade differences between them. The two countries have been at odds over economic and logistical issues. Instructively, in 2018, Tanzania introduced a 25 per cent import duty on confectionary imports from Kenya. Also, Tanzania currently has a ban on tour operators from Kenya accessing the Serengeti National Park. Similarly, Kenya has barred Tanzanian tour vans from visiting Maasai Mara National Park. To resolve these differences, officials from the two countries have been meeting, with the fourth session of the consultations happening in Arusha in April 2019 to resolve the disagreements. The next forum is expected to be held in Mombasa in July 2019. Already, Kenya and Tanzania have resolved 19 Non-Tariff Barriers and expect to reach an amicable agreement for the remaining 18 Non-Tariff Barriers.

Table 4: Trade Balance of EAC Countries – 2011 to 2018

Value in US$ million		2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18
Kenya	Exports	214.50	226.52	268.86	348.41	374.75	414.73	475.06	628.47
	Imports	535.07	680.82	591.25	602.60	608.69	582.66	516.45	505.70
	Trade Balance	**-320.56**	**-454.30**	**-322.39**	**-254.19**	**-233.94**	**-167.93**	**-41.39**	**122.78**
Tanzania	Exports	38.98	45.39	54.02	50.08	56.47	61.97	71.14	46.72
	Imports	32.47	54.82	47.48	55.12	55.11	76.34	169.22	210.08
	Trade Balance	**6.51**	**-9.43**	**6.54**	**-5.04**	**1.37**	**-14.37**	**-98.09**	**-163.36**
Rwanda	Exports	175.25	208.41	217.43	224.92	253.54	206.90	188.37	197.44
	Imports	6.12	8.94	7.48	12.09	9.52	11.79	10.60	20.25
	Trade Balance	**169.13**	**199.47**	**209.95**	**212.83**	**244.02**	**195.12**	**177.77**	**177.20**

Annual EAC Performance Report – 31st October 2018
Source: The Independent[38]

The longstanding trade disputes have resulted in low Intra-regional trade with business transactions among EAC member countries standing at 20 per cent compared to the South African Development Community at 58 per cent and the European Union at 68 per cent[39].

7. Domestic Economy updates

7.1 M-Akiba MAB2/2017/03 Re-opened

Following the relatively successful uptake of M-Akiba Retail Infrastructure Bond in March 2019 which attracted 79%

[37] https://businessday.ng/columnist/article/nigerian-stocks-flash-warning-signalsis-anyone-paying-attention/

[38] https://www.independent.co.ug/uganda-for-the-first-time-exports-more-to-kenya-than-it-imports/

[39] https://kenyanwallstreet.com/kenya-and-tanzania-to-hold-trade-discussions-in-mombasa-in-july/

subscription rate, the issuer re-opened the M-Akiba Retail Infrastructure Bond Issue to offer Kenyans another opportunity to invest and also improve financial inclusion. The bond which sought to raise Sh250 million ran from Monday, May 27, to Friday June 7, 2019. The value date was Monday, June 10, with trading at the NSE starting Tuesday, June 11, 2019. The tenor for the bond will be one year and three months, with a redemption date of September 7, 2020. The bond raised Ksh 187.5 million, implying a 75 percent subscription level. In the issuance, there has been a persistent problem of investors getting a time-out error when they attempt to purchase the M-Akiba bond. As a result, in the February 2019 re-open of the bond, approximately 4,000 investors were affected and therefore failed to buy the bond with a total of about Kshs.50M in lost opportunity. In the May 2019 re-open, 694 clients were affected resulting in a lost opportunity of about Ksh. 5.5M. It should also be noted that previous challenges of delayed settlement of the pilot retail bond issue post-listing due to reconciliation hitches may have discouraged previous investors from participating in the re-open.

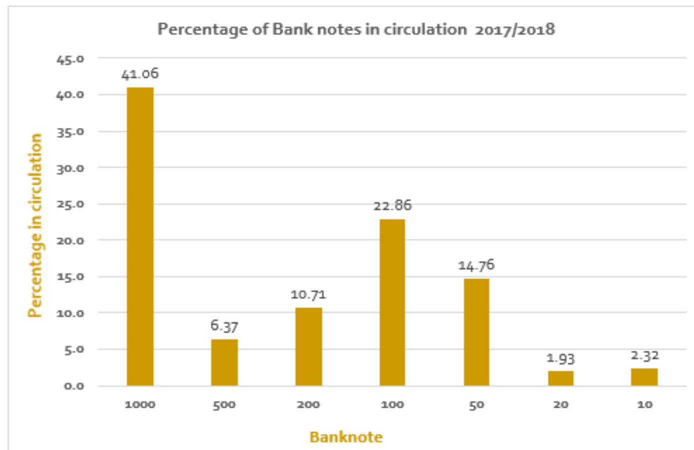
Lessons Learnt;

i. *Management has noted that as per the M-Akiba Post-Issuance Survey done by FSDA, some of the key challenges faced included poor timing, lack of reminders, Agents-focused registration, weak customer care practices and very late and impactful marketing.*
ii. *To this end, management has already written to the National Treasury, pointing out the key concerns, even as more issuances/re-openings are effected by Government. Management shall to continue to engage with the key stakeholders such as the NSE, CDSC, KASIB and the National Treasury and Planning to push for full resolution of the identified concerns in subsequent issues.*

7.2 New Kenyan currency Notes issued

On 1st June 2019, the Kenya Government unveiled new generation banknotes as part measures to curb fraud and money laundering. These new notes will be in KSh50, KSh200, KSh500 and KSh1000. In addition, it was announced that the old KSh1000-note will be withdrawn effective October 2019, from which time, the note ceases to be legal tender. Those who do not have a bank account were notified to contact the central bank. Those with more 5 million shillings in cash will also have to contact the CBK. Subsequently, on the request of the Central Bank of Kenya, on June 10th, 2019 and June 11th, 2019 Bank of Tanzania and Bank of Uganda, suspended Kenya's current account respectively, implying that no Kenyan currency should move across the borders to the two countries.

Fig 29: Percentage of Bank Notes in Circulation in Kenya – FY 2017/18



Source: CBK

Lessons Learnt;

i. *Management notes that in the rush to meet the deadline for use of the old notes, the Capital Markets could be susceptible to laundering and will continue to engage with market intermediaries such as stockbrokers, investment banks and fund managers to step up their Know Your Client (KYC) process during onboarding.*
ii. *The surveillance teams both at the NSE and CMA will heighten their monitoring of transactions to pick up any alerts that require further analysis and/or investigations*

7.3 National Budget for 2018/19 – key capital market-related pronouncements

On 13th June 2019, the Government of Kenya through the Ministry of Finance & Planning made budget policy pronouncements which will among others:

i. Measures to enhance transparency and predictability in the issuance and trading process for Treasury Bills and Treasury Bonds.

ii. Exemption from the Capital Gains Tax the transfer of property that is necessitated by restructuring of corporate entities.
iii. Introduction of an amnesty on the tax penalties and interest, on any outstanding tax for two years prior to the listing, for SME's that list under the GEMS program to encourage them to list and clean their tax records. The principal taxes shall however be paid in full.
iv. Empowerment of the Authority to enforce penalties and sanctions on market players who violate laid down rules and procedures.
v. Tax neutrality treatment of Special purpose Vehicles used for the issuance of REITs

7.4 Takeover of National Bank by KCB approved

During the quarter, the key relevant regulators (CBK and CMA) approved the takeover agreement between KCB Group and the National Bank of Kenya. KCB offered to acquire in a National Bank a share swap agreement, with Shareholders of two institutions endorsing the transaction in which NBK investors will gain one share in KCB group for every ten shares they hold in NBK. This, despite an independent fairness opinion conducted by Standard Investment Bank that pegged the valuation at 1 KCB share for 7 NBK ordinary shares. However, noting the lack of an alternative best offer for NBK, the two parties agreed to proceed with the transaction based on KCB offer. It is also noteworthy that two petitioners have moved to court to stop it from going through, alleging that the takeover will result in job losses. They also demand that the auditor general conducts an audit on National Bank to establish the bank's financial status and value before the acquisition.

7.5 Domestic Economy indicators

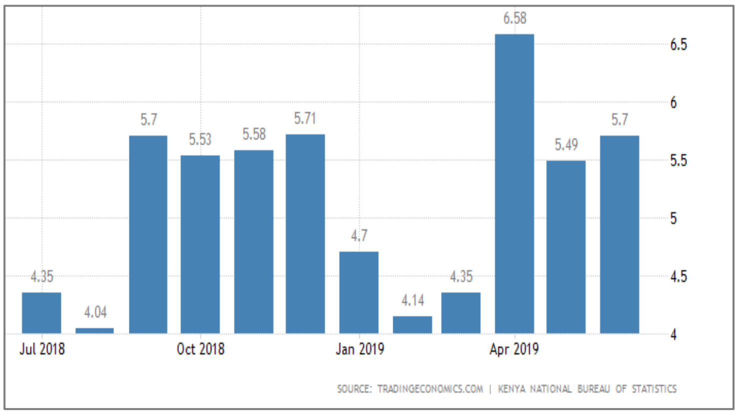
7.5.1 GDP - Kenya economy expands by 5.6 percent in Q1.2019

Kenya's economy expanded by 5.6 per cent in the first quarter of 2019, compared to 6.5 per cent performance recorded in the same quarter of 2018. According to the Kenya National Bureau of Statistics, the slowdown was due to a deceleration in agricultural activities following delay in the onset of long rains. The agriculture, forestry and fishing sector grew by 5.3 per cent compared to a growth of 7.5 per cent of similar quarter in 2018. The manufacturing sector grew by 3.2 per cent over the period, compared to a growth of 3.8 per cent in 2018. The construction sector grew by 5.6 per cent in the review quarter compared to a growth of 6.6 per cent in the corresponding quarter. The transportation and storage sector also recorded a slower growth of 6.7 per cent, compared to 8.5 per cent registered over same period in 2018. KNBS also indicated that other sectors experienced a contraction amid the continued monetary tightening instigated by high borrowing rates.

7.5.2 Inflation

According to the latest inflation figures released by the Kenya National Bureau of Statistics, Kenya's inflation rose marginally to 5.7 per cent in June 2019 from 5.49 per cent in May 2019. KNBS attributed the increase in June to higher fuel prices which led to an increase in the cost of transport.

Fig 30: Kenya's Monthly Inflation Figures



The Food and non- alcoholic drinks index decreased by 1.60 per cent in June compared to a 0.37 decline in May 2019. During the period, basic needs in housing, water and other fuels recorded a 0.05 per cent increase due to higher rates in rental outweighing drops in electricity and Kerosene cost.

Further, the transport index increased by 0.26 per cent on account of an increase in pump rates of petrol and diesel.

7.5.3 Exchange Rates - Kenyan shilling steady against the dollar

The Kenya shilling exchange rate has been relatively stable, with the rate to the US Dollar averaging Ksh 102.00 in recent times. The highest exchange rate in recent times is 106.15

recorded in September 2015, while the lowest is Ksh 36.23 in January of 1993.

Fig 31: Trend of Exchange rate between the Kenya Shilling and the U.S

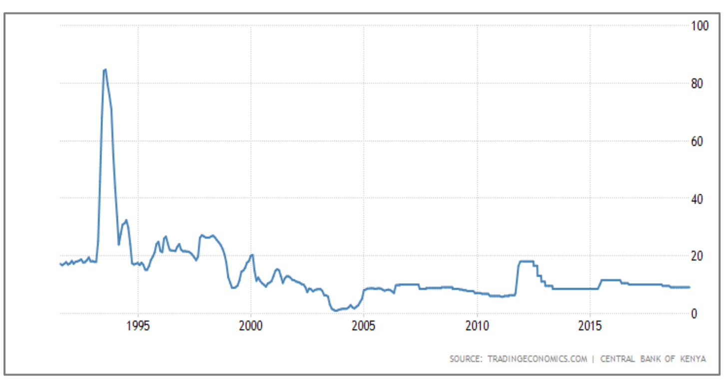
Source: Trading Economics

7.5.4 *Interest Rates*

In the latest policy action on May 27th, 2019, the Central Bank of Kenya left its benchmark interest rate (CBR) unchanged at 9 percent. This was against a backdrop of domestic stability, optimistic growth prospects, improving weather conditions in most parts of the country and increased uncertainties in the global financial markets. The bank noted the rise in headline inflation to a 19-month high of 6.58% in April 2019 from 4.35% in March, mainly driven by food cost as a result of the prolonged drought.

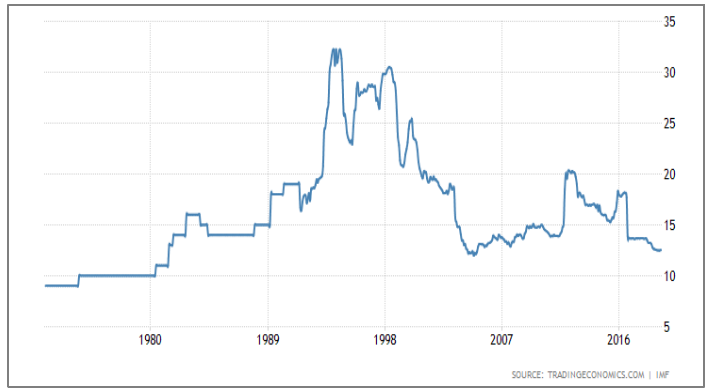
Interest Rate in Kenya averaged 13.77 percent from 1991 until 2019, reaching an all-time high of 84.67 percent in July of 1993 and a record low of 0.83 percent in September of 2003.

Fig 32: Trend of CBR Movement in Kenya



Bank Lending Rate in Kenya remained unchanged at 12.51 percent in April from 12.51 percent in March of 2019. Bank Lending Rate in Kenya averaged 16.22 percent from 1971 until 2019, reaching an all-time high of 32.28 percent in April of 1994 and a record low of 9 percent in January of 1972.

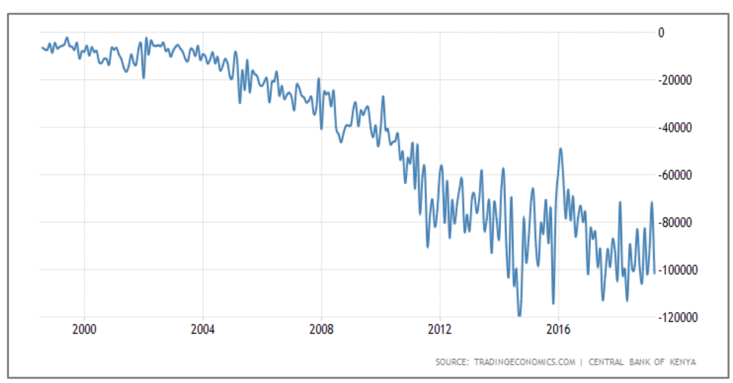
Fig 33: Trend of Bank Lending Movement in Kenya



7.5.5 *Balance of trade*

Kenya's trade deficit rose to KES 101.6 billion in April 2019 from KES 100 billion in the same month a year ago. Exports advanced only 0.5 percent to KES 43.4 million, as higher sales of chemicals (6.4 percent), fish (54.9 percent) and petroleum (87 percent) were offset by declines in those of vegetables (-0.2 percent); tea (-12.2 percent); coffee (-13.4 percent) and cement (-83.5 percent). The country's overall crop output has been hit by prolonged drought conditions, causing substantial delays in planting operations. Imports increased 0.2 percent to KES 150.4 billion, boosted by food & live animals (9.3 percent); mineral fuels (18.2 percent); crude materials (38 percent) and beverages & tobacco (18.3 percent).

Fig 34: Kenya's Balance of Trade Position



In contrast, purchases fell for chemicals (-14.2 percent); machinery & transport equipment (-9.9 percent) and manufactured goods (-0.4 percent). Balance of Trade in Kenya averaged -44,492.18 Million KES from 1998 until 2019, reaching an all-time high of -2175 Million KES in June of 1999 and a record low of -119,463 Million KES in September of 2014.

8. Capital Markets performance

8.1 Equity Market Performance

In the secondary equities market;

i. Equity turnover for Q2. 2019 dropped to KSHs. 32.897 Billion from the turnover for Q1.2019 which stood at Ksh. 45.25 Billion; indicating a 27.3% decrease.
ii. End month market capitalization for Q2. 2019 was KSHs. 2278.899 Billion compared to KSHs. 2360.52 Billion recorded in the previous quarter, indicating a 3.46% decrease.
iii. Volume traded decreased over the period by 16.54% to 1396.67 million shares compared to 1673.55 Million in Q4. 2018.
iv. Other composite indicators such as the NSE All Share and NSE 20-Shares index similarly recorded decreases of 5.11% and 7.48% closing the quarter at 149.61 points and 2633.32 points respectively.

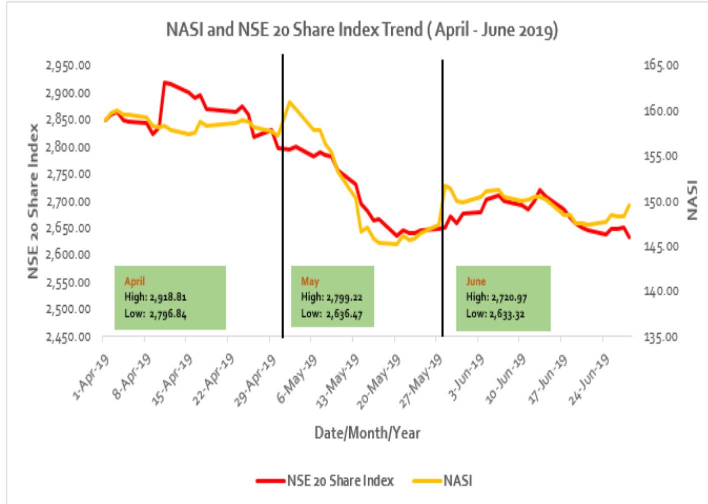
Table 7: Gross Securities Market Statistics – Q1.2019 and Q4.2018

	Q4. 2018	Q1. 2019	Q2. 2019	% change
NSE 20 Share Index	2833.84	2846.35	2633.32	-7.48
NASI	140.43	157.66	149.61	-5.11
Shares Volume traded	1570.02	1673.55	1396.67	-16.54
Equity Turnover (Ksh. Bn)	35.43	45.25	32.897	-27.30
Bonds Turnover (Ksh. Bn)	109.32	161.63	201.71	24.80
End month market cap (Ksh. Bn)	2102.02	2360.52	2278.899	-3.46

Source: CMA/NSE

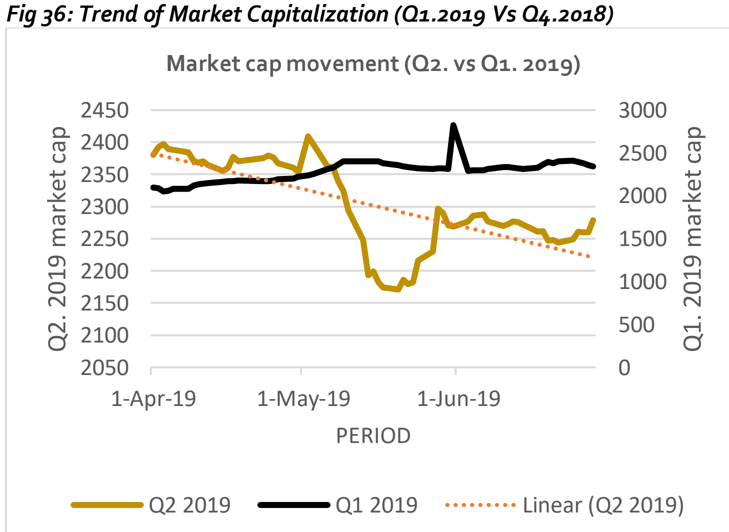
In the secondary Bond Market, Ksh 201.71 Billion worth of bonds were traded in Q2. 2019 compared to Ksh 161.63 Billion traded in Q1. 2019, indicating a 24.8% increase.

Fig 35: Trend of the NASI and NSE 20 Share Index (April – June 2019)



Source: CMA

Fig 36: Trend of Market Capitalization (Q1.2019 Vs Q4.2018)



Source: CMA/NSE

8.2 Performance of Listed Companies

8.2.1 Price Gainers

During the quarter ended June 2019, the top price gainers during were Sameer, Longhorn, Home Afrika, Kapchorua and Liberty as shown in the table below.

Counter	Q1. 2019	Q2. 2019	% change
Sameer Africa	1.83	3.07	**67.76%**
Longhorn	6.34	7.80	**23.03%**
Home Afrika	0.57	0.62	**8.77%**
Kapchorua	69.25	75.25	**8.66%**

Liberty	9.78	10.45	**6.85%**

Source: NSE

8.2.2 Price Losers

Counter	Q1. 2019	Q2. 2019	% change
Kenya Re	11.00	3.76	**65.82%**
I & M	113.50	55.00	**51.54%**
Mumias	0.51	0.34	**33.33%**
HF Group	5.00	4.01	**19.80%**
Co-op	14.95	12.00	**19.73%**

8.3 Bond Market Performance and Stability

Primary Market

8.3.1 Treasury bond Market

In the primary treasury bonds market, a quarterly analysis indicates that during Q2. 2019, six (6) Treasury bonds were issued. In issuing these bonds, the government sought to raise KShs. 140 Billion but received subscriptions worth KShs. 242.07 Billion. In the end, however, it accepted to issue bonds worth KShs. 157.82 Billion, indicating a 65.20% acceptance rate.

In the secondary equities market, Equity turnover for Q2.2019 stood at KShs. 32.89 Billion, compared to KShs. 45.25 Billion registered in Q1.2019; a 27.31% decrease confirming a decline in trading activity at the bourse during the quarter. End month market capitalization recorded a 3.46% decrease to KShs. 2,278.90 Billion registered in Q2. 2019 from KShs. 2,360.52 Billion in Q1. 2019. Volumes traded.

Table 5: Treasury bond Performance April - June 2019

Month /Year	BOND	Amt Issued (Ksh. Bn)	Amt Received (Ksh. Bn)	Amt Accepted (Ksh. Bn)	% AA /AI	% AR /AI
Apr 2019	**FXD2/2019/10**	50.00	70.93	51.33	120.70	171.22
	FXD1/2019/20		14.68	9.02	36.80	62.68
May 2019	**FXD 2/2019/5**	50.00	49.30	39.21	117.06	141.68
	FXD 2/2019/15		21.54	19.32		
June 2019	**FXD 1/2018/15**	50.00	-	-	-	-
	FXD 1/2012/15		-	-	-	-

Source: CMA/NSE

8.3.2 Corporate Bond issues

There were no corporate bond issuances during the quarter under review.

Secondary bond market

Table 6: Summary of Bond Turnover Q1.2019 – Q2.2019

Month	Government Bond Turnover (KShs. Bn)	Corporate Bond Turnover (KShs. Bn)	Total Bond Turnover (KShs. Bn)
Jan.	50.98	0.05	50.98
Feb.	48.26	0.06	48.26
Mar.	62.38	0.07	62.37
Apr	70.456	0.05	70.461
May	57.35	0	57.35
June	73.61	0.112	73.72

Source: CMA/NSE

9. New Developments and Key Updates

9.1 *Derivatives Market*

In February 2019, the Authority granted the Nairobi Securities Exchange a final approval to operationalize a Derivatives Market in Kenya. The NSE Derivatives Exchange- NEXT- is the first Derivatives Market in East Africa and the Second Derivatives Exchange in Africa. This development will position Kenya and its capital markets as a key investments gateway for East and Central Africa as well as enhance Nairobi's status a regional financial hub. The Market went live on July 4th, 2019.

The Journey began in earnest 8 years ago when the then Deputy Prime Minister and Minister of Finance, in his June 10th, 2010 Budget speech, through a policy pronouncement, announced that steps would be made towards developing institutional and legal frameworks to introduce a commodities and futures exchange in Kenya. Subsequently, the Futures Exchange Project (FEP) was initiated by the Office of the Deputy Prime Minister and Minister of Finance, resulting in the development of a policy framework for the establishment of futures market in Kenya which was adopted by the Authority in 2013. This formed the rationale for the development of the Capital Markets (Derivative Markets) Regulations 2015 that were gazetted in March 2016.

Consequently, the last two years have been focused on putting in place an institutional, product and operational framework and culminated in undertaking extensive pilot tests between July 2018 and March 2019 to perform end-to-end tests of the derivatives systems and processes in a live environment so as to evaluate the robustness of the systems, procedures and guidelines in place before market 'Go-Live'. It would also allow for the assessment of the viability of products on offer as well as the technical capacity of market players in derivatives trading. The result has been the deployment of world class infrastructure and products that are expected to provide for the needs of both local and foreign investors.

Market Structure

Participants

The approved participants in the Derivatives Market eco-system include the Clearing House (NEXT) as well as two (2) Clearing members i.e. Stanbic Bank and Co-operative Bank. The Clearing House is responsible for settling trading accounts, clearing trades, collecting and maintaining margin monies, regulating delivery and reporting trading data. Clearing Members have the responsibility for clearing (computation of obligations) and settlement of trades (movement of cash) from their trading members. The Exchange has also on boarded a total of six (6) Trading Members who are approved to execute derivatives contracts for their proprietary books as well as on behalf of their clients whom can either be institutional or retail, foreign or local or participate on the derivatives exchange in order to achieve a specific purpose.

In addition, the Derivatives Technical Advisory Committee (D-TAC) was established and constitutes of representatives from the CMA, CBK, NSE and the National Treasury. D-TAC's key mandate is twofold; Firstly, to enhance information sharing among the regulators; and secondly, to provide technical advice on derivatives market risk management, operational framework and market development in order to facilitate effective decision making in relation to Derivatives Market growth and soundness in Kenya.

IT Infrastructure

The Derivatives Market IT infrastructure is comprised of a range of systems used by members in order to fulfill their role in the market which comprise of Multi-Instrument Clearing & Settlement System (MICS) at the exchange level, Global Clearing Management System (GCMS) at the Clearing Member Level, Avvento, the trading system & Broker Back Office (BBO), the client and risk management systems, at the Trading Member level.

Risk Management Framework

As a self-regulating organization, the Exchange will serve as a first line defense in risk management that will be achieved through the following measures;

a) Collection and investment of the initial margin (a good-faith deposit by clients against open positions and include additional and house margins) and the reporting of aggregated margin positions, interest income generated and reports on its distribution to market participants.

b) Clearing and settlement data together with reconciliation information for any variance in the clearing and settlement reports

c) The NSE will also receive risk-based capital adequacy reports from the trading members to be used for the monitoring and risk management of open positions.

d) The Exchange has developed a Surveillance Manual and put in place a surveillance system.

e) In line with global practice in safeguarding market infrastructure and investor interests, the Exchange has also established the Settlement Guarantee Fund (SGF) and the Investor Protection Fund (IPF). The main purpose of the SGF is to settle specified claims by derivatives members arising out of transactions in derivative securities while the main purpose of the IPF is to satisfy specified claims by the investing public arising out of non-settlement of obligations owed to them by trading members or losses incurred by reason of the default of trading members.

f) In addition, the following Risk Management Policies have been operationalized by the Exchange; Liquidity Policy, Default Handling Procedure, SGF Policy, IPF Policy, Disaster Recovery Plan and Business Continuity Plan.

At the Authority level;

a) Trading members will be required to submit monthly risk-based capital adequacy (RBCA) compliance reports. The data will be used to model for the capital required by the market intermediary to ensure sustainability in the event of a sustained market trend that falls outside stress testing scenarios. The analysis would inform recommendations on revision of position and market limits well in advance of a market event with significant price impact. Also, the trading members will maintain know your client data in accordance with the guidelines issued by the CMA on Prevention of Money Laundering and Combating Financing of Terrorism in the Capital Markets.
b) The Authority has issued a Practice Guidance Note (PGN) on risk management for the derivatives market participants. The PGN is issued together with a self-assessment checklist for clearing members and trading members. The NSE has undertaken a self-assessment in relation to the Risk Management PGN. Consequently, it had been agreed, and in consultation with CMA and D-TAC, that compliance with the PGN be undertaken in a phased approach to be fully implemented within 5 years from market Go-Live.
c) The Authority is in the process of modernizing its surveillance program which will address the new products including surveillance. This initiative will culminate into the acquisition of a multi asset surveillance system covering all asset classes for effective market oversight.

Products

NEXT will commence with index futures and single stock futures on selected indices and stocks respectively. The Exchange will initially offer index futures contracts on the NSE25 Share Index and single futures on Safaricom Plc, Kenya Commercial Bank Group Plc, Equity Group Holdings Plc, KenGen Co. Plc, East African Breweries Ltd, British American Tobacco Kenya Plc and Bamburi Cement Ltd. The above single stock futures have been selected based on the following eligibility criteria:

a) The security underlying the futures contract must be a listed instrument on the Nairobi Securities Exchange;
b) The security underlying the futures contract shall be chosen from amongst the constituents of the NSE 25 Share Index;
c) The security underlying the futures contract must demonstrate a minimum average daily turnover of KES 7 million over the last six months before review; and
d) The security underlying the futures contract must have a market capitalization of at least KES 50 billion.

In addition, the criteria used in selecting the companies for the NSE 25 Index were as follows:

a) Shares must have their primary listing on the Nairobi Securities Exchange;
b) A company must have at least 20% of its shares quoted on the NSE;
c) A company must have been continuously quoted for a least 1 year;
d) A company must have a minimum market capitalization of Ksh one billion; and
e) Should ideally be a "blue chip" superior profitability and dividend record

All futures contracts listed on NEXT will have quarterly expiry dates; this will be the third Thursday of March, June, September and December of every year. All NEXT futures contracts will initially be cash settled.

Going forward, in order to ensure adequate capacity building and product uptake after the Market launch, the Exchange has rolled out the Market Demand Plan focusing on various sequenced activities to drum up support and encourage uptake of the product.

Major Licenses and Approvals

During Q2 2019, the Authority granted the following licenses and other major approvals including;

a. A Fund Manager License to Jubilee Financial Services Limited;
b. An Authorized Depository License to Credit Bank Limited;
c. An Authorized Depository and Authorized Securities Dealer Licenses to SBM Bank Kenya Limited;
d. A Non-dealing Online Foreign Exchange Broker License to SCFM Limited;
e. An Investment Adviser License to AFG Wealth Kenya Limited;
f. Approved an interim shareholder circular in respect to conversion of preference shares to ordinary shares by National Bank of Kenya Limited;
g. Approved a shareholder circular in relation to acquisition of all the ordinary shares of National Bank of Kenya by KCB Bank;
h. Approved the offer statement in relation to the acquisition of all the ordinary shares of National Bank of Kenya by KCB Bank;
i. Approved the NIC Group Plc shareholders circular in relation to the merger between NIC Group Plc and Commercial Bank of Africa Limited;
j. Approved the Noteholders circular in relation to the proposed merger between Commercial Bank of Africa Limited and NIC Group Plc;
k. Approved a shareholder circular by Express Kenya Plc for the conversion of debt to equity; and
l. Approved a bonus issue by I & M Holdings Plc of 413, 405, 369 New Fully and Paid Up Ordinary Shares to existing shareholders of I & M Holdings Plc.

10. Capital Markets Stability Indicators (CMSIs)

	1.0 Stock Market Volatility							
Equity Market Depth	**Quarter/ Year**	**Statistics**				**Assessment of Risk Level (High – Medium – Low)**	**Performance Brief for the Quarter**	**Ongoing Intervention Measures**
NSE 20 Index Volatility Base Year = 2010	**Q2. 2019**	**April**	**May**	**June**	**Q.Avg**	**Low (indicative - <10% high; >10% - low)**	• The NSE 20 Share Index volatility for the quarter ended June 2019 averaged at **0.45%**, compared to **0.42%** recorded in Q1.2019.	• Derivatives market – During the quarter, the Authority granted NSE an approval to launch and fully operationalize the derivatives exchange with initial trading limited to Equity Single Stock Futures (SSF) and Equity Index Futures (EIF).
		0.64%	0.42%	0.31%	0.45%			
	Q1.2019	**Jan**	**Feb**	**March**	**Q.Avg**			
		0.49%	0.37%	0.41%	0.42%			
	Q4.2018	**Oct**	**Nov**	**Dec**	**Q.Avg**			
		0.53%	0.28%	0.63%	0.48%			
	Q3. 2018	**July**	**Aug**	**Sep**	**Q. Avg**			
		0.35%	0.42%	0.52%	0.43%			
NASI Volatility Base Year = 2010	**Q2.2019**	**April**	**May**	**June**	**Q.Avg**	**Low (indicative - <10% high; >10% - low)**		
		0.23%	0.80%	0.30%	**0.44%**			
	Q1.2019	**Jan**	**Feb**	**March**	**Q.Avg**			
		0.40%	0.41%	0.52%	**0.44%**			
	Q4.2018	**Oct**	**Nov**	**Dec**	**Q.Avg**			
		0.50%	0.57%	0.49%	**0.52%**			
	Q3. 2018	**July**	**Aug**	**Sep**	**Q. Avg**			
		0.46%	0.54%	1.04%	**0.68%**			
Turnover Ratio	**Q2.2019**	**April**	**May**	**June**	**Q.Avg**	**Medium (indicative – annual: <8%- Low; >15% High)**	• A turnover ratio of **1.39%** was recorded in the quarter, compared to	• Kenya's equity turnover levels remain low in comparison with global peers. This has
		0.42%	0.55%	0.42%	**1.39%**			
	Q1.2019	**Jan**	**Feb**	**March**	**Q. Sum**			
		0.67%	0.50%	0.67%	**1.85%**			
	Q4.2018	**Oct**	**Nov**	**Dec**	**Q.TR**			

		0.79%	0.49%	0.37%	**1.69%**		**1.85%** in Q1.2019 indicating a fall in turnover levels during the quarter under review.	mainly been attributed to limited options of counters to trade on with major trading reflected on the top five companies at the bourse by market capitalization. • Joint market initiatives are being pursued by key stakeholders including the Authority, NSE and CDSC through such initiatives as signing MOUs with institutions relevant institutions such as the Kenya Manufacturers Association with the goal of bringing more companies to market. • The NSE through its Ibuka program has been able to admit 15 companies from
	Q3. 2018	**July**	**Aug**	**Sep**	**Q. TR**			
		0.39%	0.41%	0.54%	**1.34%**			

								different sectors, with a long-term plan to list. • The Authority has developed a regulatory framework to support securities lending and borrowing and will be facilitating a stakeholders' session to promote this trading mechanism.
	2.0 Foreign Exposure Risk							
Foreign Investor turnover as a % of total turnover	**Q2.2019**	**April**	**May**	**June**	**Q.Avg**	**Medium (indicative – annual: <40%-Low; >90% High)**	• Average Foreign investor participation for the months of April and May averaged at **69.62%,** a **7.34%** decrease from **76.96%** recorded in Q1.2019	• During the quarter, through its Investor Education and Public Awareness (IEPA) Department, the Authority engaged investors on Facebook to understand their preferences. The feedback from the sessions will be used to better serve
		75.80%	63.43%	-	**69.62%**			
	Q1.2019	**Jan**	**Feb**	**March**	**Q.Avg**			
		81.55%	72.38%	70.81%	**76.96%**			
	Q4.2018	**Oct**	**Nov**	**Dec**	**Q.Avg**			
		75.14%	76.54%	73.67%	**75.12%**			
	Q3. 2018	**July**	**Aug**	**Sep**	**Q.Avg**			
		67.69%	62.03%	64.80%	**64.84%**			
Net Foreign Portfolio Flow (In KES Millions)	**Q2.2019**	**April**	**May**	**June**	**Q.Sum**		• Net Foreign Portfolio levels for April and	
		93	2,166	-	**2,259**			
	Q1.2019	**Jan**	**Feb**	**March**	**Q.Sum**			

		(1,357)	216	1,742	**601**	**High (indicative – annual: <Ksh (50million) - High (outflow; >KShs. 50 million High inflow)**	May 2019 amounted to a total inflow of **Ksh 2,259 Mn,** an increase of **Ksh 1,658 Mn** in net foreign inflows during the quarter compared to Q1.2019.	international investors. • The Budget Policy proposal to exempt foreign investors from Personal Identification Number (PIN) requirements is also likely to attract more foreign investors in the market, increasing net inflows
	Q4.2018	**Oct**	**Nov**	**Dec**	**Q.Sum**			
		(4,287)	(599)	(1,785)	**(6,671)**			
	Q3. 2018	**July**	**Aug**	**Sep**	**Q. Sum**			
		(2,111)	(1,565)	(3,029)	**(6,705)**			
Market Concentration (Top 5 companies by market cap)	**Q2.2019**	**April**	**May**	**June**	**Q. Avg**	**High (indicative – annual: >50% High concentration)**	• During the quarter, the top five companies by market capitalization accounted for **70.80%,** the highest in the last four quarters, confirming their dominance in the Kenyan securities market.	• The Authority has been actively promoting market diversification as a way of addressing this challenge. Market deepening function has been reorganized and strategic alliances leveraged to facilitate uptake of new products and especially bringing to the market large cap entities to reduce
		70.17%	71.62%	70.62%	**70.80%**			
	Q1.2019	**Jan**	**Feb**	**March**	**Q. Avg**			
		65.34%	67.85%	69.56%	**67.58%**			
	Q4.2018	**Oct**	**Nov**	**Dec**	**Q. Avg**			
		66.74%	64.76%	65.95%	**65.82%**			
	Q3. 2018	**July**	**Aug**	**Sep**	**Q. Avg**			
		68.45%	68.31%	67.40%	**68.05%**			

							• The top five companies included SAFARICOM, EQUITY, EABL, KCB and CO-OP.	market concentration.
	3.0 Government Bond Market Exposure							
Treasury Bond market turnover Concentration	**Q2.2019**	**April**	**May**	**June**	**Q.Avg**	**High (indicative – annual: >50% High concentration)**	• During the quarter, Corporate Bond turnover amounted to **Ksh 34.76 Mn**, 0.02% of total bond turnover valued at **Ksh 190 Bn**, making Treasury bond turnover at **99.98%** compared to 99.90% in the previous quarter.	• The Authority is implementing a hybrid bond market model that will allow trading of bonds both on and off the Exchange. The recent establishment of the Kenya Mortgage Refinancing Company (KMRC) will enable bond market deepening after it leverages on capital markets to raise funds through bonds for on-lending to banks and other mortgage financing companies.
		99.99%	100%	99.96%	**99.98%**			
	Q1.2019	**Jan**	**Feb**	**March**	**Q.Avg**			
		99.96%	99.84%	99.90%	**99.90%**			
	Q4. Avg	**Oct**	**Nov**	**Dec**	**Q.Avg**			
		99.96%	99.98%	99.96%	**99.97%**			
	Q3. 2018	**July**	**Aug**	**Sep**	**Q. Avg**			
		99.78%	100.00%	100.00%	**99.93%**			
Corporate Bond Market ownership	**Category**	**No of Investors**	**Amount Outstanding (Mn)**	**% of total outstanding**		**High (indicative – annual: >50%**	• Local Corporate bond investors were the leading	

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<tr><td>Local Investors</td><td>4,721</td><td>67,539.04</td><td>99.06%</td></tr>
<tr><td>East African Investors</td><td>20</td><td>181.99</td><td>0.27%</td></tr>
<tr><td>Foreign Investors</td><td>111</td><td>457.17</td><td>0.67%</td></tr>
<tr><td colspan="4">Source: CDSC Data as at September 2018</td></tr>
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<td>High concentration</td>
<td>investors in corporate bonds at 99.33% of amounts outstanding, while foreign bond investors held 0.67% of total corporate bond holdings.</td>
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<td colspan="4">4.0 Investor Profiles - Equity Market</td>
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<td>Equity Market</td>
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<table>
<tr><td>Type of Investor</td><td>2016</td><td>2017</td><td>2018</td><td>2019*</td></tr>
<tr><td>E.A. Institutions (%)</td><td>66.38</td><td>68.36</td><td>68.50</td><td>67.51</td></tr>
<tr><td>E.A. Individuals (%)</td><td>12.49</td><td>11.47</td><td>11.54</td><td>11.59</td></tr>
<tr><td>Foreign Investors (%)</td><td>21.13</td><td>20.17</td><td>19.97</td><td>20.91</td></tr>
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Source: CMA- *Data as at June 2019
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<td>High (indicative – annual: >50% High concentration)</td>
<td>
Local investors, a sum of East African institutional and individual investors accounted for 79.1% of shares held in the equity market with 20.91% being held by foreign investors.
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In order to address low uptake issue and attract local investors and issuers the Authority undertook a study aimed at determining the underlying reasons behind the low uptake of capital markets products and services.
The Authority concluded an Investor Education Impact and Opportunities Analysis Study that

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								will be instrumental in the development of a National Consumer Financial Education Strategy as well as development of an Impact Assessment Measurement Index that the Authority can use to gauge the impact of its investor education program going forward. • This will translate to more targeted engagements to onboard and drive increased market participation within the capital markets.
	5.0 Investor Compensation Coverage							
Settlement Guarantee Fund (SGF) Coverage Ratio[40]	**Q2.2019**	**April**	**May**	**June**	**Q.Avg**	**Medium (indicative – annual: > 1 times, implies full coverage)**	• SGF Ratio for the quarter ended June 2019 averaged **1.74.** This is an	• Through Risk-based supervision, the Authority has been monitoring the SGF figures and the
		1.87	1.64	1.70	1.74			
	Q1.2019	**Jan**	**Feb**	**March**	**Q.Avg**			
		1.30	1.28	1.20	1.26			
	Q4.2018	**Oct**	**Nov**	**Dec**	**Q.Avg**			

[40] ***Source: CDSC***

		1.14	1.83	2.05	1.67		indication that the Guarantee Fund balances are sufficient to cover liabilities that would arise following default by securities brokers.	financial position of the firms to ensure that they are in good standing and that investors are protected. • The Authority has also embarked on a joint assessment of the Capital Markets stability indicators and will be reviewing the sufficiency of the SGF in determining the sufficiency of the fund in the coming financial year.
	Q3. 2018	**July**	**Aug**	**Sep**	**Q. Avg**			
		1.96	1.83	1.46	1.75			
	6.0 Asset Base of Fund Managers, Stockbrokers, Investment Banks							
Assets Under Management	**As at 31st January 2019 (Amount in KShs Millions)**					**Medium (Indicative – the higher the figure, the more stable is the market)**	• The total Asset Base of Fund Managers, Stockbrokers, Investment Banks, Investment advisors and online forex brokers as at 31st January	• The Authority continuously monitors asset levels of its licensees to ensure accurate reporting of assets and liabilities and monitoring sufficiency of liquid capital to monitor
	CMA Licensee	**Total Assets**	**Total Liability**	**Net Assets**				
	Fund Managers	7,853.96	1,532.09	6,321.86				
	Stockbrokers	2,330.41	692.06	1,638.36				
	Investment Banks	11,885.78	2,995.46	8,890.32				
	Investment Advisors	1,464.78	161.95	1,302.83				

	Online Forex Broker (Non-Dealing)	202.58	200.21	2.4			2019 was **Ksh 7,853.96 Million, 2,330.41 Billion, Kshs.11,885.78 Million, Ksh 1,464.78 Million** and **Ksh 202.58 Million** respectively.	potential bankruptcy of licensees.

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2. Nairobi Securities Exchange Monthly Bulletins
3. Kenyan Wall Street
4. Focus Economics
5. World Bank Reports
6. IMF Reports
7. Statutory reports/submissions (to CMA)

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