The Capital Markets Soundness Report (CMSR)

Volume XIII

"Socially Responsible Investing: The rising tide to Comply with Environmental, Social and Governance (ESG) Principles in investments and the increasing role of the financial sector as a critical nexus in reversing the escalating Global Climate Crisis"

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About this Report

The Capital Markets Soundness Report examines global, regional and domestic political and socio-economic events that pose risks to the performance of the capital markets and facilitate informed debate amongst industry players, policy makers and investors on market soundness.

It further links the impact of such events to Kenya's Capital Markets industry to help devise risk mitigation measures, interrogate key market risks to reduce the exposure of capital markets to identified risks as well as utilize the report as a key reference document for collaborative evidence based policy formulation and analysis.

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Mr. Luke Ombara, Director Regulatory Policy and Strategy

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SPECIAL MESSAGE FROM THE AG. CHIEF EXECUTIVE OFFICER

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

2020 marks the dawn of another opportunity to steer the Capital Markets in Kenya to greater heights in line with its role to facilitate the country's economic development and aspirations to become a middle-income country by 2030.

On behalf of the Authority, I am happy to sharewith you the 13th edition of the Capital Markets Soundness Report (CMSR) for the quarter ended December 2019. The report provides a platform for the Authority to communicate stakeholders' thoughts on cross-cutting emerging policy issues that present threats or provide opportunities towards the growth and development of the Kenyan Capital Markets industry and economy.

The Capital Markets continue to feature prominently both domestically and globally as countries and regions seek competitive advantage over others. For instance, China and the Eurozone are the most recent examples with the former unlocking bureaucracy in favor of small businesses to encourage new listings while the latter working towards establishment of the Next Capital Markets Union to position the Eurozone as an international financial center away from London, amidst Brexit, expected on 31st January 2020.

Noting such developments, the Authority continues to work towards finding the right balance between regulation and market development, to ensure that the domestic market can grow and be able to attract significant capital flows to fund the country's needs, especially the infrastructural funding requirements as outlined in the Vision 2030, Medium Term Development Plans and as envisaged under the "Big 4 Agenda".

As we begin a new year, I would urge continued participation by all capital markets stakeholders in the quarterly roundtables meetings that precede the publication of this report as well as new ideas as we position it to be the leading source of capital markets policy and stability updates in Africa.

I am confident that this report will continue to help guiding your strategic initiatives and decision making in your day to day business as you contribute towards the National Development Goals.

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

Enjoy the read.

EDITORIAL

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

The 13th edition of the Capital Markets Soundness Report (CMSR) comes at a time when attention has inevitably shifted to the escalating climate crisis, manifested in a myriad of devastating climatic conditions coupled with natural disasters that have been observed across continents. The protests witnessed at the December 2019 UNFCC Cop25 meeting in Madrid confirm the height of global concern. In 2019 alone, the world has witnessed several natural disasters that have proven costly to economies, with two of the most recent being the Brazilian and Australian wildfires. As at 7th January 2020, economists estimated the economic costs of the Australian fires to be around $2 billion and still expects the figure to rise in the coming months.

It is upon these developments that this Issue is themed "***Socially Responsible Investing: The Rising Tide to Comply with Environmental, Social and Governance Principles in investments and the increasing role of the financial sector as a critical nexus in reversing the escalating Global Climate Crisis***."

With the realization that ESG exposures could lead to large losses for firms and asset owners, financial markets players, notably large global asset managers and regulators are now pushing for integration of these factors into the entities' business models. Some market players such as investment banks and trust funds have even restricted investments in sectors and projects considered to cause adverse effects to the environment.

Further, following the call for review of the US Dodd-Frank Act by its critics and the signing into law of the Economic Growth, Regulatory Relief and the Consumer Protection Act by President Trump on May 2018, the US Securities Commission adopted new rules and amendments during the quarter under review, to relax the regulatory framework, that had been enhanced as a response to the Global Crisis.

The key message is that worldwide, the capital market regulatory environment is being scrutinized to reflect their responsiveness to global realities. Kenya has recently established a Financial Law Review Panel (FLRP) as recommended in the Capital Markets Master Plan to address such concerns.

Other global developments in the securities market space covered in the report include: recommendations by clearing members and end-users, following their assessment of the inadequacy of IOSCO Principles on Financial Market Infrastructure (PFMI) on Central Counter Party (CCP) providers relating to addressing resilience, recovery and resolutions; and top challenges for the industry in 2020, as reflected in the PWC Capital Markets Survey.

Coming closer home, we explore the Absa Africa Financial Markets Index Rankings for African countries based on six pillars, with Kenya ranking third overall in the continent in building deeper and more transparent financial markets. We also provide an analysis on how firms could position themselves to benefit from the repeal of interest rate caps through the capital markets.

The report concludes with an assessment of the stability of the capital markets as reflected in the soundness scores in indicators such as liquidity, volatility of the securities indices, market concentration, , foreign investor participation, net gross notional exposure of derivatives contracts, settlement Guarantee Fund and ownership of securities

We hope that you will be regularly kept abreast of the critical factors and events that shape the functioning and prosperity of the Kenyan Capital Markets to inform decision making at various levels; corporate, policy and implementation levels.

Happy reading!

1.0 Special Feature: - Rising Place of Socially Responsible Investing and the increasing role of Environmental, Social, and Governance (ESG) aligned factors in determining global competitiveness amongst players.

For a long time, historical decisions on where financial assets would be placed, were based on various criteria, with financial return being predominant. However, for more than a decade now, the increasing importance for consideration of other factors particularly, ESG has taken dominance, with investors increasingly applying these non-financial factors as part of their analysis process to identify material risks and growth opportunities.

Numerous institutions, such as the Sustainable Accounting Standards Board (SASB), the Global Reporting Initiative (GRI) and CDP[1] (formerly the Carbon Disclosure Project) have developed guidelines and standards to help define materiality to facilitate incorporation of these factors into the investment process[2].

Table 1: Sample of ESG Issues

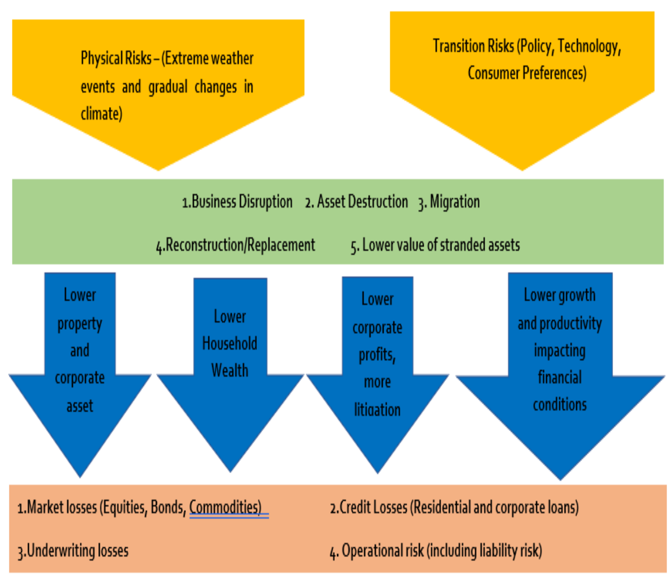
Environmental Issues	Social Issues	Governance Issues
Climate change and carbon emissions	Customer satisfaction	Board composition
Air and water pollution	Data protection and privacy	Audit committee structure
Biodiversity	Gender and diversity	Bribery and corruption
Deforestation	Employee engagement	Executive compensation
Energy efficiency	Community relations	Lobbying
Waste management	Human rights	Political contributions
Water scarcity	Labor standards	Whistleblower schemes

Source: CFA Institute

ESG issues can have a material impact on a firms' corporate performance and risk profile, and on the stability of the financial system. Governance failures at banks and corporations contributed to past financial crises, including the Asian and the global financial crises. Social risks in the form of inequality may contribute to financial instability by triggering a political response of easier credit standards to support consumption despite stagnant incomes for middle- and lower-income groups (Rajan 2010).

Environmental risk exposures can lead to large losses for firms, and climate change may entail losses for financial institutions, asset owners, and firms.

Fig 1: Linkages of Financial Stability Risks emanating from ESG related risks[3]



[1] CDP is a not-for-profit charity that runs the global disclosure system for investors, companies, cities, states and regions to manage their environmental impacts.

[2] CFA Institute

[3] Global Financial Stability Report, October 2019

The integration of ESG factors into firms' business models—prompted either by regulators or by investors—may help mitigate these risks.

1.1 The Politics in the Climate Change Agenda

Despite the glaring evidence of the fast effects of climate change to the global environment, it remains the toughest, most intractable political issue discussed today. For Governments, even environmentally friendly ones, climate change poses a massive political dilemma. While environmentalists, scientists and activists seem to have unified their resolve and consensus in advocating for a cleaner environment, different Governments and policy makers across different jurisdictions differ in opinion on the gravity and impact human activity is causing to the environment today.

So, one would ask, what makes climate change different from any other political topic? Perhaps a befitting response is the mere fact that the climate crisis cannot be solved by a single world power or a group of states. It is an inclusive agenda that requires the whole of humankind to cope with the consequences on a planetary scale. Yet, although everyone seems to be aware of the necessity of global cooperation, finding a supranational consensus has proven to be practically impossible as the political and economic interests of countries around the world interfere in finding an adequate solution. Evidence shows that;

a. In 2018, President Macron's suffered political backlash owing to two weeks of protests for a proposed policy aimed at imposing higher eco-taxes on fuel towards a cleaner environment leading to a halt in the process.

b. Germany is currently at a crossroad in introducing a policy aimed at promoting the use of electric cars in the country as analysts predict a possible shrink in its workforce by almost 1 percent by 2030, owing to the fact that the assembly of electric vehicles which contain far fewer components would become more automated and require less manpower than production of petrol or diesel models.

c. Further, the developments of transparent, corrupt free and progressive carbon credit markets remain a challenge across countries as concerns over corruption and dishonest and skewed industry lobbying efforts lead to the distortion of the price mechanism for such markets, compromises the credibility and growth of carbon markets.

1.2 The December 2019 UN Climate Change Conference (UNFCCC) COP 25 Outcomes, Increased Protests on the Urgency of Commitment to Socially Responsible Investing and Reducing Green Gas Emissions in line with the 2016 Paris Agreement

In 2015, one hundred and ninety-six (196) countries negotiated, committed to and signed to the Paris Agreement aimed at reducing the levels of emissions of greenhouse gases to curb the rapid rise in global warming and climate change effects. Under the Agreement, each signatory country was expected to develop its own national plan, setting targets for emissions reductions and specifying pathways by which it aims to meet those targets.

However, research shows that global CO2 emissions have increased by around 11% since the first UNEP emissions gap report in 2010[4]. Between 2nd and 13th December 2019, the COP25 UN Climate Change Conference was held in Chile Madrid amidst prolonged protests mainly attributed to the perceived discrepancy between the slow pace of the talks and the urgency to act towards decreasing global emissions for a cleaner and safer environment.

Table 2: Some Natural Disasters Witnessed in 2019[5]

Date	Disaster and Estimated Cost
Mar 2019	Typhoon Idai claims more than 900 lives in Africa. Idai killed 602 people in Mozambique and 299 in Zimbabwe. It destroyed almost 90% of Mozambique's second-largest port, Beira.
Jul 2019	Japan Heat wave kills more than 160. Hundreds ended up in hospitals due to sizzling temperatures that soared above 105 degrees Fahrenheit (41 degrees Celsius)
Jun 2019	9 people dead from heat wave in India. Temperatures topped 120 degrees Fahrenheit (49 degrees Celsius) in the northern part of the country
Oct 2019	At least 86 dead in Japan from Typhoon Hagibis
Aug 2019	Typhoon Lekima kills 172 in China
Aug 2019	Brazilian wildfires in the Amazon. The smoke and flames of forest fires shut down airports, increased hospitalizations, caused blackouts and cost Brazil +5 Billion [6]
Dec 2019	Australian bushfires witnessed in this quarter are estimated to have at least caused 20 deaths with thousands of homes having been destroyed and millions of animals killed. More than 5,000 insurance claims totaling $375 million have been made in relation to the Australian bushfires, including 1,600 destroyed homes, according to the Insurance Council of Australia (ICA)7

The lag in implementation has mainly been attributed to the laxity by the world's top global gas emitters (such as China, US, India, Australia) to implement policies that would largely reduce the emissions. During this year's COP25 meeting, scientists largely pointed out the increased use of fossil fuels and cement production through increased demand for coal, oil, and natural gas as a key factor that has resulted in increased Green House Gases (GHG) emissions as provided for by the International Energy Agency. Countries emitting the most CO2 are also often among the countries that control the world's oil.

Coal is the largest contributor of fossil fuel carbon dioxide emissions, making up 42% of the global total. Latest data by the World Resources Institute indicate that emissions from fossil fuels grew 1.5% in 2017, 2.1% in 2018 and was projected to grow another 0.6% in 2019. This growth is at odds with the deep cuts urgently needed to respond to the climate emergency[8].

[4] https://www.carbonbrief.org/unep-1-5c-climate-target-slipping-out-of-reach

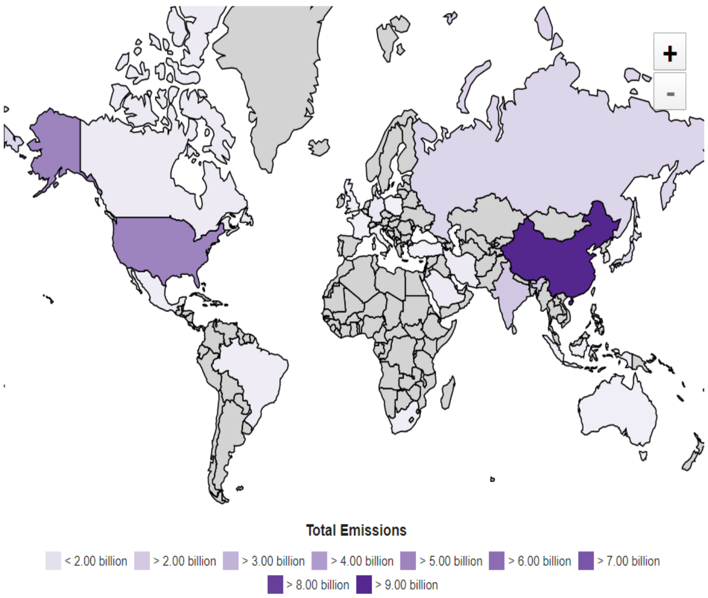
[5] https://www.usnews.com/news/best-countries/slideshows/5-of-the-deadliest-natural-disasters-in-2019

[6] https://www.theverge.com/2019/9/10/20858834/amazon-fire-brazil-forest-harm-recovery-century

[7] https://www.businessinsider.com.au/australian-bushfires-cost-economy-surplus-government-spending-2020-1

[8] https://www.wri.org/blog/2019/12/co2-emissions-climb-all-time-high-again-2019-6-takeaways-latest-climate-data

Fig 2: Total Emission Levels per country [9]



1.3 Shift of focus to Funds Investing in Fossil Fuels and calls for Financiers to halt investing in corporations linked to fossil fuels

The climate discussion has stretched to board rooms of global pension funds as the voice of "fossil free movement" increases globally. In the United States for example, the world's top three asset managers; BlackRock, Vanguard and State Street, which together oversee assets worth more than China's entire GDP are stated to have about $300bn of their assets invested in fossil fuels using money from people's private savings and pension contributions[10].

Fig 3: Investment Allocations by the world's top 3 Asset Managers

Source: InfluenceMap

The key impacts so far seen this year include the hottest month ever recorded on our planet, giant fires across the northern latitudes and a hurricane that stalled over the Bahamas producing what meteorologists called "the longest siege of violent, destructive weather ever observed" on our planet.

The climate protests on fossil fuel companies has added a further blow to the performance of companies in the oil and energy sector in the United States in addition to an observed trend of bankruptcies as many oil and gas companies have struggled to generate free cash flows, according to www.resilience.org. In 2019 for example, California and Colorado's public pension funds together lost out on over $19 billion over the past decade by investing in fossil fuel stocks.

Further, in December 2019, Goldman Sachs Group Inc stated its intent to provide $750 billion in financing, advisory services and

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10 https://www.theguardian.com/environment/2019/oct/12/top-three-asset-managers-fossil-fuel-investments

investments for initiatives that fight climate change, as well as those that foster economic opportunities for under-served people over the next decade. The Bank also updated its internal environmental policy framework to rule out providing financing to any new projects that will drill for oil in the Arctic or that create new thermal coal plants or new thermal coal mines.

1.4 Lessons from Countries that have made significant steps towards adapting renewable energy sources

a. *Morocco's largest Solar Plant in the world*

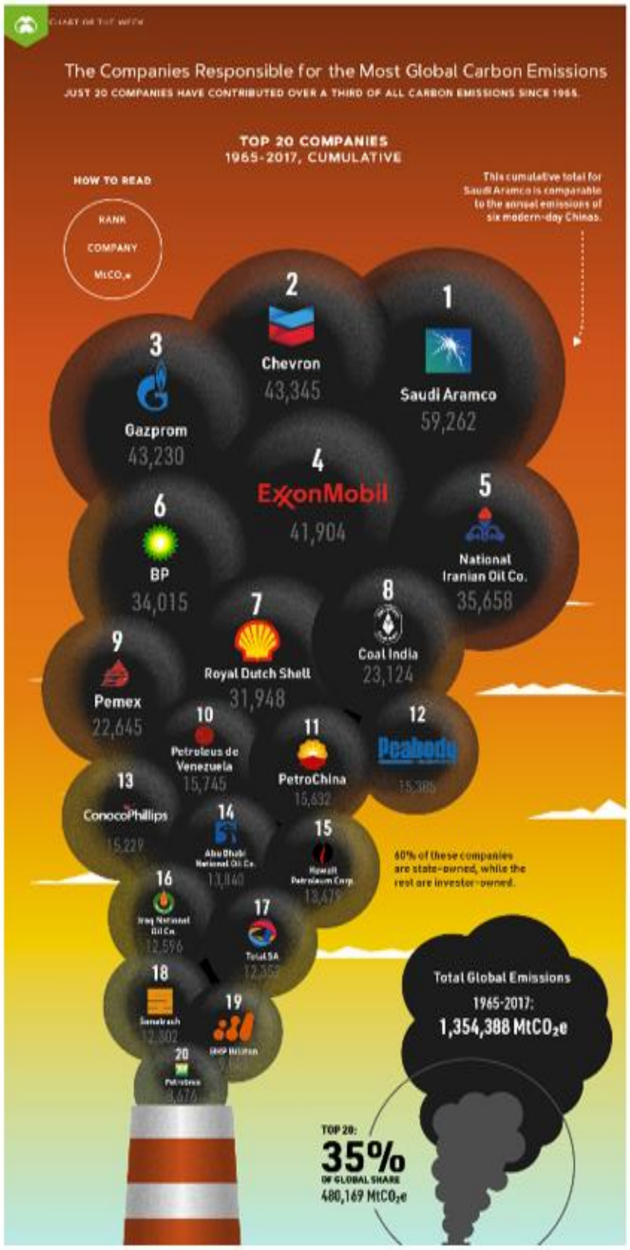
According to National Geographic's September 2019 article "*Climate Change report card*," Morocco's renewable energy model is reported to focus mainly in the development of the world's largest solar power plant, dubbed "*Noor Ouarzazate complex*" that is estimated to have the capacity to generate enough electricity to power two cities the size of Marrakesh. The plant is estimated to cover an area the size of 3,500 football fields. Morocco's National Energy Strategy calls for generating 42 percent of its electricity production from renewables by 2020, and 52 percent by 2030[11].

b. *Gambia's Alternative Renewable Energy sources*

Gambia's model is based on one of its principal pathways to reducing GHG emissions has been through the use of renewables, in the form of a program that will increase the country's electricity capacity by one-fifth partly through construction of one of the largest photovoltaic plants in West Africa. The country has also launched a large project to restore 10,000 hectares of forests, mangroves, and savannas. It is also replacing flooded rice paddies with dry upland rice fields and promoting adoption of efficient cook stoves to reduce the overuse of forest resources.

[11] https://www.nationalgeographic.com/environment/2019/09/climate-change-report-card-co2-emissions/

Fig 4: Top 20 Companies Responsible for the Most Global Carbon Emissions between 1965 and 2017[12]



Rank	Company	Emissions(MtCo2) (1965 – 2017)	Country
1	Saudi Aramco	59,262	Saudi Arabia
2	Chevron	43,345	USA
3	Gazprom	43,230	Russia
4	ExxonMobil	41,904	USA
5	National Iranian Oil Co	35,658	Iran
6	BP	34,015	UK
7	Royal Dutch Shell	31,948	Netherlands
8	Coal India	23,124	India
9	Pemex	22,645	Mexico
10	Petroleus de Venezuela	15,745	Venezuela
11	PetroChina	15,632	China
12	Peabody Energy	15,385	USA
13	Conoco Phillips	15,229	USA
14	Abu Dhabi National Oil Co.	13,840	Abu Dhabi
15	Kuwait Petroleum Corp	13,479	Kuwait
16	Iraq National Oil Co.	12,596	Iraq
17	Total SA	12,352	France
18	Sonatrach	12,302	Algeria
19	BHP Billiton	9,802	Australia
20	Petrobas	8,676	Brazil

"60 percent of the companies are state-owned, while the rest are investor owned"

Source: Visualcapitalist

[12] https://www.visualcapitalist.com/companies-carbon-emissions/

1.5 Costa Rica's Renewable Energy Alternatives and a Moratorium on Oil extraction and exploitation from 2021 to end of 2050

Costa Rica on the other hand is reported to aim for its electricity production to be 100 percent renewable by 2021. It's already extremely close: in 2018 it generated 98 percent of its electricity from renewable sources—primarily hydropower—for the fourth consecutive year. Two-thirds of its greenhouse gas emissions are from transportation, and the country has made it a national priority to use renewable energy across its roads and rails. The country's National Plan for Electric Transportation calls for at least five percent of the bus fleet to be replaced by electric buses every two years, and for at least 10 percent of new taxi concessions to be given to electric vehicles. Additionally, in February 2019 Costa Rica extended a moratorium on oil extraction and exploitation from 2021 until the end of 2050.

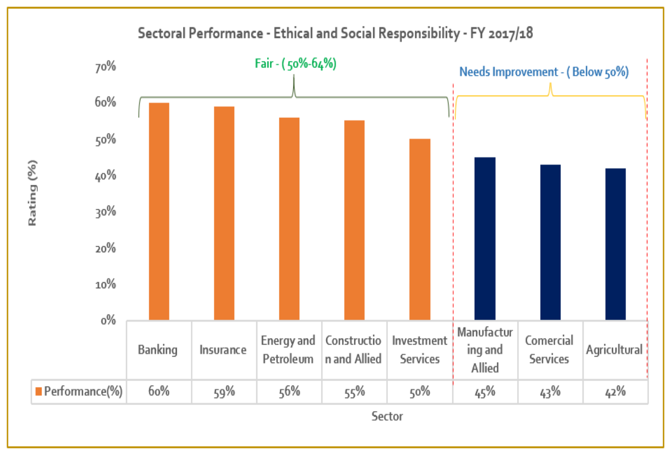
c. Norway

Norway has set an ambitious target of reducing emissions by 40 percent by 2030; and it has adopted legislation committing the country to reducing emissions by 80-95 percent relative to 1990 levels by 2050. The Norwegian Parliament is reported to have agreed in June 2019 to (mostly) disinvest its $1 trillion Sovereign Wealth Fund from oil, gas, and coal, dumping $13 billion in stocks related to fossil fuels (though sparing those belonging to ExxonMobil and Royal Dutch Shell) and diverting resources to renewable energy projects. The Nation also leads the world in its embrace of electric cars; almost 60 percent of new cars sold in the country in March were electric. Its forest cover is also increasing, and electricity production is almost entirely from renewables: 96 percent from hydropower and 2 percent from wind farms[13].

1.6 Linking Global Developments to Kenya's Corporate Governance Framework and compliance with ESG Requirements

In its debut report on the status of corporate governance covering FY 2017/18, the Authority made an assessment on the compliance of listed companies to ethical and social responsibility as one of the seven anchors[14] on the code of corporate governance.

Fig 5: Performance of Listed Companies by Sector with respect to ESG Compliance Assessment



Source: CMA State of Corporate Governance for Publicly Listed Companies Report, 2019

Out of the 56 listed companies that were assessed, on ethics and social responsibility, the assessment reveals the following rating for issuers; 2 - leadership, 7 - good, 24 - fair and 23 - needs improvement[15].At the sectoral level, the listed company's adherence to the Ethical and Social

[13] https://www.nationalgeographic.com/environment/2019/09/climate-change-report-card-co2-emissions/

[14] Other Scorecard components within the Corporate Governance framework include; i. Commitment to good governance ii. Board operations and Control iii. Rights of shareholders iv. Stakeholder Relations v. Accountability, risk management and internal control and vi. Transparency and disclosure

[15] A leadership score is a 75% and above rating; Good is between 65% and 74%; Fair is between 50% and 64%; and Needs Improvement is below 50%.

Responsibility is represented in Fig. 5 below, with the banking sector leading in embedding ESG principles in their business processes.

- *Kenya has made significant progress in facilitating financing climate change initiatives through the capital market, following its commitment as a signatory to the Paris Agreement towards reduction of greenhouse gas emissions. The development of a Policy Guidance Note for Green Bond Issuance and Nairobi Securities Exchange (NSE) Green Bond Trading Rules in February 2019 are cases in point. Consequently, in August 2019 the first unlisted Green Bond in East Africa, structured as a restricted public offer for sophisticated investors was issued by Acorn Project (Two) Limited Liability Partnership backed by a 50% guarantee from GuarantCo Ltd., a Mauritius-based private infrastructure development company.*
- *Noting the supporting legal and regulatory instruments available to facilitate Green Bond issuances, there is great opportunity for development of an effective ecosystem that supports the establishment of green capital markets in Kenya in line with the Marrakech Pledge 2016 with both private and public sector participants. We further welcome the amendment of the Income Tax Act (ITA)through the Finance Act 2019, to exempt from withholding tax, interest income payable to investors in Green bonds.*
- *We note that the Kenyan Government is projecting to issue its first Sovereign Green Bond in March 2020 and the Authority will provide the necessary facilitation to make this a success.*
- *Further, to jump-start the overall primary debt capital markets the Government needs to reconsider providing or endorsing Guarantees for similar products. However, going forward, more care should be undertaken in properly screening and identifying the pipeline of projects to be financed if the country seeks to attract foreign capital from some of the world's largest pension funds and asset managers.*
- *Based on CMA's first report on the state of corporate governance, it is evident that the banking sector in Kenya is keen on aligning its functions to ESG factors and it is becoming increasingly likely that they could redirect a good deal of funding from fossil fuel based companies to those focused on clean energy, as most are signatories to the Principles of Responsible Investing(PRI)*[16] *signed in November 2019.*
- *It is projected that investment banks, fund managers and other non-bank financial institutions will follow suit, a strategic decision which will hugely deepen the capital markets going by recent decisions by top global asset managers.*
- *To realize the benefits that accrue to the capital markets, Pension funds, trustees and asset managers will need to be urged to re-evaluate their funds allocation to different asset classes as well as nature of projects being funded by their assets to avoid fiscal losses that could accrue from global developments along disinvestments in non-clean energy investments.*
- *As presented in fig 4 above, about 60 percent of the top 20 companies responsible for most GHG emissions are from the oil sector. With Kenya's recent discovery of oil as well as the*

[16] The United Nations-supported Principles for Responsible Investment (PRI) initiative is a network of international investors working together to put the six Principles for Responsible Investment into practice. The PRI were devised by the investment community and reflect the view that environmental, social and governance (ESG) issues can affect the performance of investment portfolios and therefore must be given appropriate consideration by investors if they are to fulfill their fiduciary (or equivalent) duty. In implementing the Principles, signatories contribute to the development of a more sustainable global financial system.

planned dual listing of National Oil still a possibility, the country may need to undertake an impact assessment of this natural resource as a key source of energy and revenue for the country, vis-à-vis implementation of pro-renewable energy policies within the global markets.

- *Specifically, and in retrospect, there is need to reassess the viability of the development of new fossil fuel plants such as coal plants planned to be set up in Kenya.*
- *In addition, efforts towards development and implementation of a national capacity building exercise aimed at demystifying the cost of investing in a cleaner environment and healthier workforce should be stepped up. .*
- *Further, capital markets stakeholders have proposed the following policy interventions;*

i. *A minimum allocation by pension funds, asset managers, corporations, commercial banks, investment banks and other applicable players towards green and clean energy projects in the country as an asset class;*

ii. *Aa tax incentive be extended to firms that adhere to the minimum allocation prescription in their portfolio allocation;*

iii. *Noting the increasing and dominant role of Development Finance Institutions (DFIs) within the clean energy space, stakeholders proposed that such DFIs consider green finance to promote the role of the Capital Markets as an efficient resource allocator towards capital formation through mobilization of savings; and*

iv. *Consideration should be taken for a Guarantee Fund to specifically support SMEs and other entities utilizing the capital markets as a funding solution, through the establishment of a Sovereign and/or County Wealth Fund;*

2.0 Developments in the Global Markets

2.1 Efforts by the European Union to re-boot the NEXT Capital Markets Union (CMU) initiative

In September 2015, the European Commission adopted an action plan setting out a list of over 30 actions and related measures to establish the building blocks of an integrated capital market in the EU by 2019. The Capital Markets Union's overall aim is to foster growth of EU Capital Markets and provide a broader range of funding and investment alternatives to the real economy and consumers.17

In its formative stages, the initiative was spearheaded by the UK, hosting the continent's biggest capital markets. However, since the Brexit vote in 2016, not much progress had been made on this front as the UK is scheduled to leave the EU by January 31st, 2020.

More recently during the quarter, new efforts have been observed in reviving the CMU agenda with discussions held amongst the Finance Ministers of Germany, France and the Netherlands who are supported by high level finance ministry experts from Spain, Sweden, Poland and Italy. These countries formed the Next CMU Group and tasked it with coming up with recommendations to bring CMU to fruition.

[17] https://blogs.pwc.de/capital-markets/general/capital-markets-blog-series-part-ii-the-mechanisms-and-key-objectives-of-the-capital-markets-union-key-building-blocks/247/

While a unified position on approach has not yet been arrived at, some of the key objectives of the Next CMU Group include;

i. Strengthening the role of the euro by establishing it as a reference asset currency which involves fostering a common market for a euro reference asset;

ii. Boosting the equity markets – both in size and liquidity to help fund businesses as well as increase returns for pension funds. This was informed by the fact that many pension funds across Europe are struggling to make decent returns as they hold highly rated bonds that either yield very little or have negative yields.

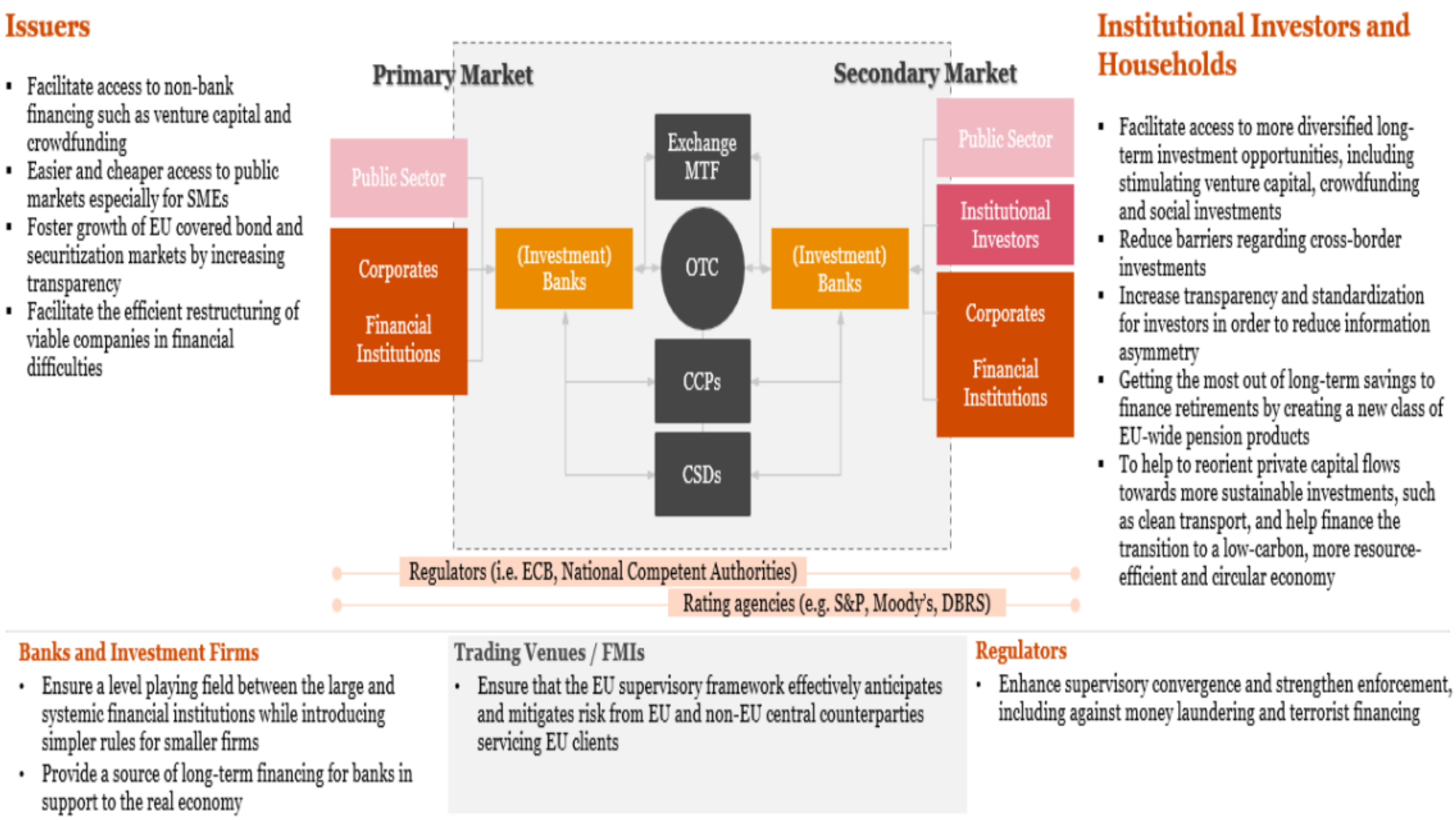
iii. Development of an ambitious EU-wide digital finance action plan with cross-border dimensions.

"The Next CMU High-Level Expert Group ("Next CMU Group") is composed of high-level experts from Germany, France, the Netherlands, Italy, Spain, Poland and Sweden and reflects various parts of capital markets with public, private and academic experience. The task put by the Ministers to the Next CMU Group is to analyze, with a "fresh eye", the EU's market-based financing capacity five years after the launch of the Capital Markets Union ("CMU") and to make appropriate recommendations."

Savings and Sustainable Investment Union

The Next CMU High Level Group Report (October 2019)

Fig 6: Pictorial Depiction of European Union's Interventions/Action Points in the Next CMU



Source: PWC

This is even as the Financial Conduct Authority forwarded discussions on the development of UK regulations post Brexit on 31st January 2020. Senior officials from the FCA have expressed their desire to move towards more outcomes-based approaches and relying less on reporting and disclosure, which has been the regulator's mantra since the 2007-09 global financial crisis and the basis of most EU Based regulations[18].

- *An outcome-based approach aims to cure regulatory fragmentations across jurisdictions as a way of building increased cross border transactions and is well aligned with CMA's strategic thinking. It is therefore about acknowledging the quality of outcomes of another regulatory regime while accepting differences in underlying rules.*

2.2 China's Move to Slash Red Tape to enable Startups and Small Businesses to List

China has been on the forefront in introducing market innovations to attract listings amidst a persistent slowdown

[18] Global Risk Regulator, December 2019 Issue

in growth. In July 2019, a new technology board in Shanghai was launched targeting listing of big-ticket technology firms.

More recently in the month of December 2019, in a bid to promote more listings on its exchanges by Small and Medium Enterprises, Chinese lawmakers are reported to have agreed to slash Red Tape for Initial Public Offerings (IPO), approving an amendment to the country's securities law that also aims to better protect investors and prevent insider trading.

The amendment is considered a big breakthrough as it cuts red tape and the cost for companies when going public and was considered the most significant revision of the Securities Law in history. The new registration-based IPO system in the newly amended law – which comes into effect on March 1, 2020 – requires strict information disclosures from companies seeking to list.

The listings however do not need approval from the China Securities Regulatory Commission, according to a draft law. It has also removed the need for companies to be profitable before listing.

- *While the Authority has introduced a raft of regulatory and tax incentives to attract small and medium enterprises to be active participants within the capital markets and potentially list, experience from more successful jurisdictions points to speed of processing applications, mainly based on disclosure, being a key incentive to capital raising and listing by Small and Medium Enterprises (SMEs).*
- *The Authority will continue to review its approval/registration model to improve its turnaround time, but without compromising on investor protection and market integrity.*
- *As a result, creative and innovative approaches aimed at encouraging small businesses to operate with a greater motive towards profitability should be adopted. The recent policy decision by Government to ensure that all Pending Bills are cleared is very welcome.*
- *Further going forward, Government agencies and other contractors of small business services should ensure payment for services in time to enable the businesses to focus more on building the business value rather than meeting operational costs.*
- *Other interventions include facilitating innovation through platforms such as the Authority's regulatory sandbox where technical assistance is provided to build ideas to reality.*

2.3 A Call to Review the Dodd-Frank Act

The United States Dodd-Frank Act implements changes that, among other things; affect the oversight and supervision of financial institutions, provide for a new resolution procedure for large financial companies, create a new agency responsible for implementing and enforcing compliance with consumer financial laws, introduce more stringent regulatory capital requirements, effect significant changes in the regulation of over-the-counter derivatives, reform the regulation of credit rating agencies, implement changes to corporate governance and executive compensation practices, incorporate the Volcker Rule, require registration of advisers to certain private funds, and effect significant changes in the securitization market[19].

The Dodd-Frank Wall Street Reform and Consumer Protection Act is a massive piece of financial reform legislation passed during the Obama administration in 2010 as a response to the financial crisis of 2008[20]. However, critics have forwarded the argument that the Act is too regulator-centric and there should be a return of powers to private firms. Key effects of the Act that was introduced in 2008 include;

i. Through the Financial Stability Oversight Council (FSOC) and Orderly Liquidation Authorities, more scrutiny was placed in monitor the financial stability of major financial firms whose failure could have a serious negative impact on the U.S. economy;
ii. The law provided for liquidations or restructurings via the Orderly Liquidation Fund, established to assist with the dismantling of financial companies that have been placed in receivership and prevent tax dollars from being used to prop up such firms;
iii. FSOC was also given the Authority to break up banks that are considered so large as to pose a systemic risk and also force them to increase their reserve requirements;
iv. The Federal Insurance Office was tasked with the role of identifying and monitoring insurance companies considered "too big to fail".
v. Volcker Rule, restricts the ways banks can invest, limiting speculative trading, and eliminating proprietary trading. Banks are not allowed to be involved with hedge funds or private equity firms, which are considered too risky.
vi. The Act also contains a provision for regulating derivatives, such as the credit default swaps that were widely blamed for contributing to the 2008 financial crisis. Dodd-Frank set up centralized exchanges for SWAPS trading to reduce the possibility of counterparty default and also required greater disclosure of swaps trading information to increase transparency in those markets;
Dodd-Frank established the Securities and Exchange Commission (SEC) Office of Credit Ratings. The office is charged with ensuring that agencies provide meaningful and reliable credit ratings of the businesses, municipalities, and other entities they evaluate;
vii. It established a mandatory bounty program under which whistleblowers can receive from 10% to 30% of the proceeds from a litigation settlement, broadened the scope of a covered employee by including employees of a company's subsidiaries and affiliates, and extended the statute of limitations under which whistleblowers can bring forward a claim against their employer from 90 to 180 days after a violation is discovered

Siding with the critics, the U.S. Congress passed a Bill in 2018 known as the Economic Growth, Regulatory Relief, and Consumer Protection Act, which rolls back significant portions of the Dodd-Frank Act. It was signed into Law by President Trump on May 24, 2018 citing that the Act limits banks from on-lending to small businesses.

[19] The Dodd Frank Act – A Cheat Sheet – by Morrison & Foerster

[20] https://www.thebalance.com/dodd-frank-wall-street-reform-act-3305688

Subsequently the discussions escalated during the quarter, with SEC adopting new rules and amendments under Title VIII of the Dodd Frank Act. The new rules however focus on the establishment of a regulatory regime for security-based swap dealers.

The actions establish record keeping and reporting requirements for security-based swap dealers and major security-based swap participants and amend the record keeping and reporting requirements for broker dealers.

- *Global trends point to regulations being periodically reviewed reflect global realities; whether economic, political, social or technology based. It is therefore no surprise that the USA is undergoing a period of review of the Dodd Frank Act.*
- *The CMA Board is well seized of the dynamic nature of the capital markets and has recently established the Capital Markets Review Panel whose key objective is to ensure that the Law is kept sync with global and domestic realities. The Panel shall act as a think tank for early identification of potential legislative gaps or challenges that could affect the functioning of financial markets including ancillary legislation, and propose legal and regulatory reforms, which may extend beyond financial regulation and encompass commercial, contract, property or trust law.*
- *Some of the key areas of discussion by this Panel at its inaugural meeting scheduled for Q1 of 2020 include: Review of existing Principles-Based Regulatory Approach; Corporate Governance Requirements Tailor-Made For Small Medium Enterprises and Family Owned Businesses; Review of the Public Offers, Listings and Disclosures Regulations; Collective Investment Schemes Regulations; and Recognition of Credit Rating Agencies domiciled in other jurisdictions*

2.4 Developments on Central Counter Party (CCP) operations in the United States and arising discontent with the International Organization of Securities Commissions (IOSCO) Principles for Financial Market Infrastructure (PFMI) amidst calls for the regulators to increase supervisory role amongst CCPs service providers.

In October 2019, nine companies[21] jointly published a working paper titled; *"A path forward for CCP Resilience, Recovery and Resolution"* questioning the effectiveness of the IOSCO Principles for Financial Market Infrastructure (PFMI)[22] amidst calls for the Regulators to increase supervisory role amongst CCPs service providers.

These principles have largely been incorporated into statutory and/or regulatory regimes in key jurisdictions, providing meaningful frameworks to enhance CCP safety and soundness, particularly in light of' increased systemic importance post derivative market reforms.

Last year's September 2018 major default[23] by a member of Nasdaq Clearing AB notably raised again broader concerns

[21] The 9 companies include Allianz Global Investors, Blackrock, Citi Group, Goldman Sachs, Societe Generale, JP Morgan Chase & Co, State Street, T Rower Price and Vanguard.

[22] The *Principles for financial market infrastructures* are the international standards for financial market infrastructures, ie payment systems, central securities depositories, securities settlement systems, central counterparties and trade repositories. Issued by the CPMI and the International Organization of Securities Commissions (IOSCO), the PFMI are part of a set of 12 key standards that the international community considers essential to strengthening and preserving financial stability.

[23] On Monday September 10, 2018, the markets in Nordic and German power experienced an extreme movement in the spread. One of Nasdaq Clearing´s members had a portfolio containing a large spread position between Nordic and German Power that was negatively impacted by the fluctuations. When the member no longer could meet the margin requirement due to the losses in the

related to CCP governance as well as risk and default management standards and practices[24]. Recommendations made were organized based on three broad categories;

- Resilience;
- Recovery; and
- Resolution.

The paper brings together perspectives from clearing members and end-users, identifies issues that regulators and CCPs should consider, and makes recommendations to address these outstanding issues.

- *As a signatory to the IOSCO Multilateral Memorandum of Understanding (MMoU) and facilitator of implementation of the PFMI, the Authority will closely and continuously monitor if the proposed changes to the paper are adopted globally and the impact of the same on its current infrastructural environment, subject to continuous self-assessment for compliance with existing and updated Principles while taking due care not to push for incremental implementation subject to size and the level of sophistication of the Kenyan capital markets This will be considered within the context of the recently upgraded Central Depository and Settlement Corporation (CDSC) and NSE market infrastructure to ensure that operations remain seamless.*
- *Further, the Authority will continue push for extension of the scope of oversight powers of the Central Bank of Kenya (CBK) Central Depository System, bearing in mind the systemic importance of the facility and ultimately for the unification of the CDSC and CBK CSDCs and or establishment of a single Horizontal Central securities Depository (CSD) that may operate as a CCP in future to enhance settlement efficiency.*

2.5 A Summary of an Analysis of the Future of Capital Markets in 2020

As the year 2019 comes to an end, progressive analysts and executives continue to engage in discussions aimed at pro-actively looking into what the capital markets is likely to look like in 2020 taking note of global changes and developments, technological advancements, evolution of client needs and relationships amongst capital markets participants.

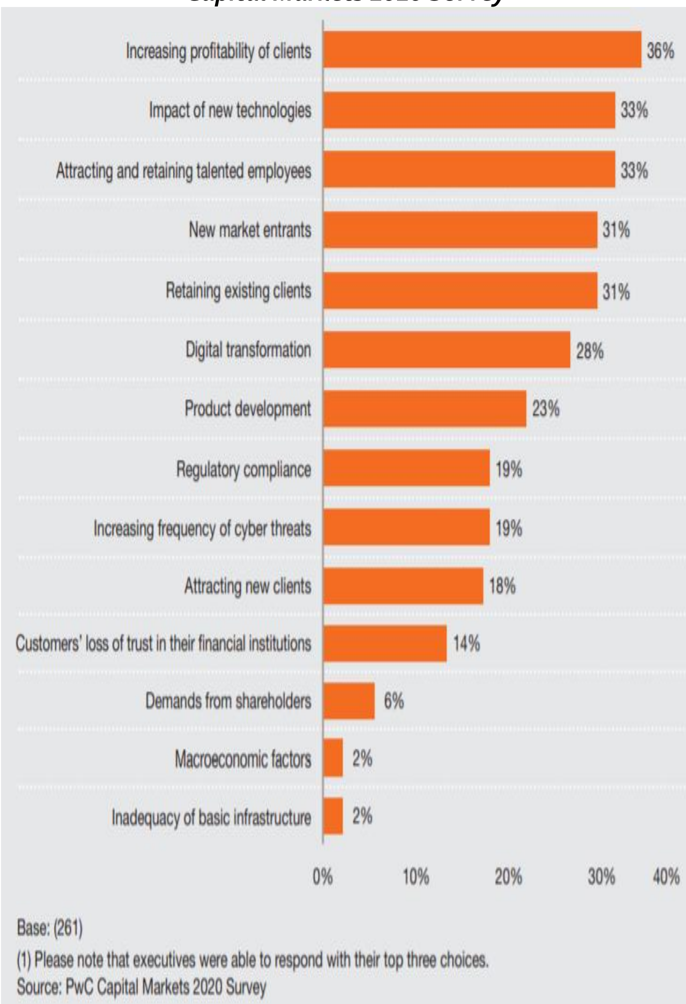
According to Price Waterhouse Coopers, " *Capital Markets 2020*" report[25], the capital markets is expected to play an increasingly important role in 2020 in providing everything from financing to the world's most innovative companies to generating the investment returns needed to support an ageing population in the developed world.

portfolio, Nasdaq Clearing declared the member in default, on Tuesday, September 11. Within 48 hours after the default, the portfolio was closed out through an auction according to Nasdaq Clearing's close-out procedures. However, the close out resulted in a loss for Nasdaq Clearing that exceeded the defaulting member's collateral and default fund contribution. On 14 September, Nasdaq temporarily contributed 20 mm EUR (200 mm SEK) to its Junior Capital fund, in addition to the EUR 7M that Nasdaq already had replenished in the Default Fund as Junior Capital.

[24] A path forward for CCP Resilience, Recovery and Resolution

[25] https://www.pwc.com/hu/hu/kiadvanyok/assets/pdf/pwc_capital_markets_2020_final.pdf

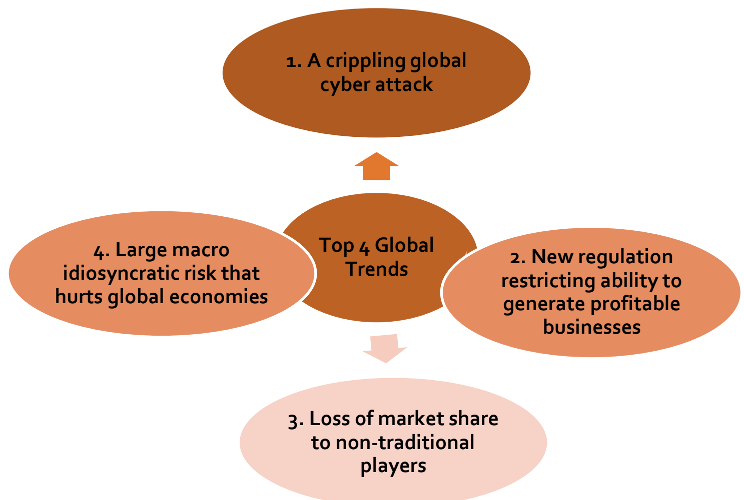
Fig 7: Top Challenges for the Capital Markets in 2020 – PWC Capital Markets 2020 Survey



To fulfill this goal, capital markets as well as banking executives continue to ask several questions; **i.** Where will the leading financial markets be in 2020 and beyond? **ii.** How will regulation shape capital markets in the future? **iii.** How will megatrends such as urbanization translate into opportunities for capital markets and financial institutions to fund infrastructure and trade? **iv.** What will be the revenue drivers moving forward? **v.** Do businesses need to consider different business models going forward? **vi.** Will new players disintermediate existing financial institutions or provide for innovation and partnership opportunities?

According to the PWC Capital Markets 2020 Survey, many have gloomily predicted a shrinking capital markets landscape, overregulation and the fall of traditionally powerful financial centers such as London and New York.

Fig 8: Top 4 Global Trends to watch out for in 2020



1. **Crippling Global Cyber Attack**

A crippling global cyber-attack is likely to shut down global markets for some period, prompting a new round of Government interventions and unprecedented focus on cybercrime, terrorism and their perpetrators, including state actors. The likely effect would be growth in mistrust, likely to result in a serious fragmentation of the global financial system.

Assessment of the Domestic Economy;

- Like other jurisdictions, Kenya has suffered its own share of cyber-attacks both in Government and within the private sector, noting that Kenya has the highest internet penetration in Africa with over 31 million people having access to the internet[26].

- According to the Communication Authority's fourth quarter sector statistics report for the financial year 2018/19the National KE-CIRT/CC detected 26.6 million cyber threat events as compared to 11.3 million cyber threat events detected in the period Jan –Mar 2019.

Table 3: Summary of Cyber Threat Events in Kenya

Cyber Threat Events	Jul-Sep 19 '000	Oct-Dec 18	Jan – Mar 19	Apr – Jun 19
Malware	1,844.9	9,026.9	8,883.9	21,137.5
Botnet/DDOS[27]	911.3	453.4	1,133.9	2,353.5
Web application attacks	1,064,971	737,289	1,222,23 7	3,084.7
System Vulnerabilities	2.5	3.4	13.3	28.6
Total No. of Threats	**3,823.7**	**10,221.0**	**11,253.3**	**26,604.2**

Source: National KE-CIRT/CC Report

- With the growing number of cyber-attacks in the country, the Assent of the Data Protection Bill 2019 into Law by the Head of State in November 2019 was welcome by industry players. Some of the provisions of the Act include;

  i. It establishes the office of the Data Commissioner and sets out the requirements for the protection of personal data processed by both public and private entities;

  ii. It outlines key principles that will govern data processing, sets out the rights of data subjects and assigns duties to data controllers and data processors;

  iii. In addition to setting the conditions for the transfer of personal data outside Kenya, the Act provides for the exemptions to processing of data and outlines data handling offences and attendant penalties.

- *In August 2019, the Joint CMA/NSE/CDSC Joint Boards meeting identified cybersecurity and cyber resilience as a key emerging capital markets stability risk and resolved to adopt the following mitigation measures for the industry;*

  i. Development of a harmonized and principle-based strategy/plan aimed at ensuring resilience to cyber-attacks;

  ii. Use of a proactive cyber risk management approach;

  iii. Having in place the right resources (human, financial, etc.) to support market infrastructure in terms of advisory, implementation of preventive measures;

  iv. Continuous system monitoring and periodic system upgrades; and

  v. Enhanced awareness and sensitization of market players on cyber-risks and cyber-resilience.

[26] https://www.mtn.co.ke/insights/cybersecurity-threat-landscape-in-kenya-and-the-remedy-2/

[27] In computing, a denial-of-service **attack** (DoS **attack**) is a **cyber-attack** in which the perpetrator seeks to make a machine or network resource unavailable to its intended users by temporarily or indefinitely disrupting services of a host connected to the Internet.

2. Restrictive Regulation and loss of market share to non-traditional players

Over-regulation of financial markets is projected to stimulate significant additional growth in the shadow banking system, which will further magnify growth for monoline finance companies, hedge funds, private equity firms and other buy-side players. Traditional financial institutions are projected to lose market share to non-traditional players.

Assessment in the Domestic Economy;

- Regulation within the Kenyan financial sector has faced challenging times as costs of regulation continue to be stated as an inhibiting factor to the growth of some of the sectors, particularly the capital markets. With increased concern on the shrinking size of the Kenyan capital markets, deliberate attempts need to be made to ensure regulation promotes a wholistic growth of businesses in the industry.
- While the primary role of the Authority is to regulate the market, deliberate efforts must be made in having a flexible and balanced regulatory regime reflective of the economic cycle and prevailing economic conditions in the country to avoid increased apathy with respect to regulated markets. The effect of which has seen an increase growth of shadow financial sector players to tap into a frustrated segment of the market.

- *The Authority continues to adopt a Principles-Based Regulatory regime to attract alternative capital markets related business, through Policy Guidance Notes (PGNs) in the immediate to short term but with a clear intention to develop more robust regulatory frameworks to ensure investor protection and uphold market integrity in the medium to long-term*

3.0 Developments within Sub Saharan Africa

3.1 African Nations Making progress in Building Deeper and more Transparent Financial Markets

In October 2019, the ABSA Official Monetary and Financial Institutions Forum published the its third edition of the ABSA Africa Financial Markets Index. The index provides a toolkit for countries seeking to strengthen their financial markets infrastructure. It tracks progress on financial market developments annually across a range a countries and indicators. The first edition in 2017 shed light on the disadvantages of rigid foreign exchange regimes, which handicapped investors and constrained countries' ability to deal with global developments. Subsequently, many countries have moved to more flexible exchange rates, improving their policy responsiveness and shock absorption capability.

Similar positive changes can be seen in growing consciousness of the importance of local investors and improvements in the transparency and availability of market data. The index focuses on six fundamental pillars: **i**. Market depth, **ii**. Access to foreign exchange, **iii**. Market transparency, tax and regulatory environment, **iv**. Capacity of local investors, **v**. Macroeconomic opportunity, **vi**. Legality and enforceability of standard financial markets master agreements

Overall assessment on the ranking of the African countries from the report showed substantial progress by African countries in developing their financial markets on the back of new products, regulatory improvements and more responsive economic policy.

The report showed that 13 of 20 countries evaluated across the continent now score more than 50 out of 100 overall, compared to just three out of 20 in 2017. Botswana, Kenya and Namibia all joined these ranks over the 2018/19 financial year, indicating a quickening development of their respective capital markets.[28]

Kenya is reported to have retained its third position amongst the 20 ranked African nations mainly due to the fact that the country has a progressive financial market in the African continent, with Mauritius being ranked second most improved with market depth following a substantial listing of bonds by the central bank. A graphical depiction of Kenya's overall ranking and positioning across the six fundamental pillars is provided in fig 10 below.

- *While the financial markets are rated to be performing well, there is need to increase the contribution of the Capital Markets into the overall economic performance.*
- *A key factor that affected this year's ranking is forwarded as Kenya's perceived intermediate foreign exchange rate system[29], classified with other countries as Morocco, Rwanda, Angola, Egypt and Ethiopia.*
- *The Authority notes its role in deepening the Kenyan Capital markets as a key factor monitored by investors in determining the destination for their funds.*
- *While significant effort is being made by the Authority in promoting the Capital Markets as a capital raising solution for players, concerns remain on the National Government's increased appetite for domestic debt that has resulted in passive investment strategies by financial markets players as returns by Government securities remain comparatively attractive in comparison to other asset classes.*

4.0 Developments within the Domestic Economy

4.1 Repeal of Interest Rate Caps

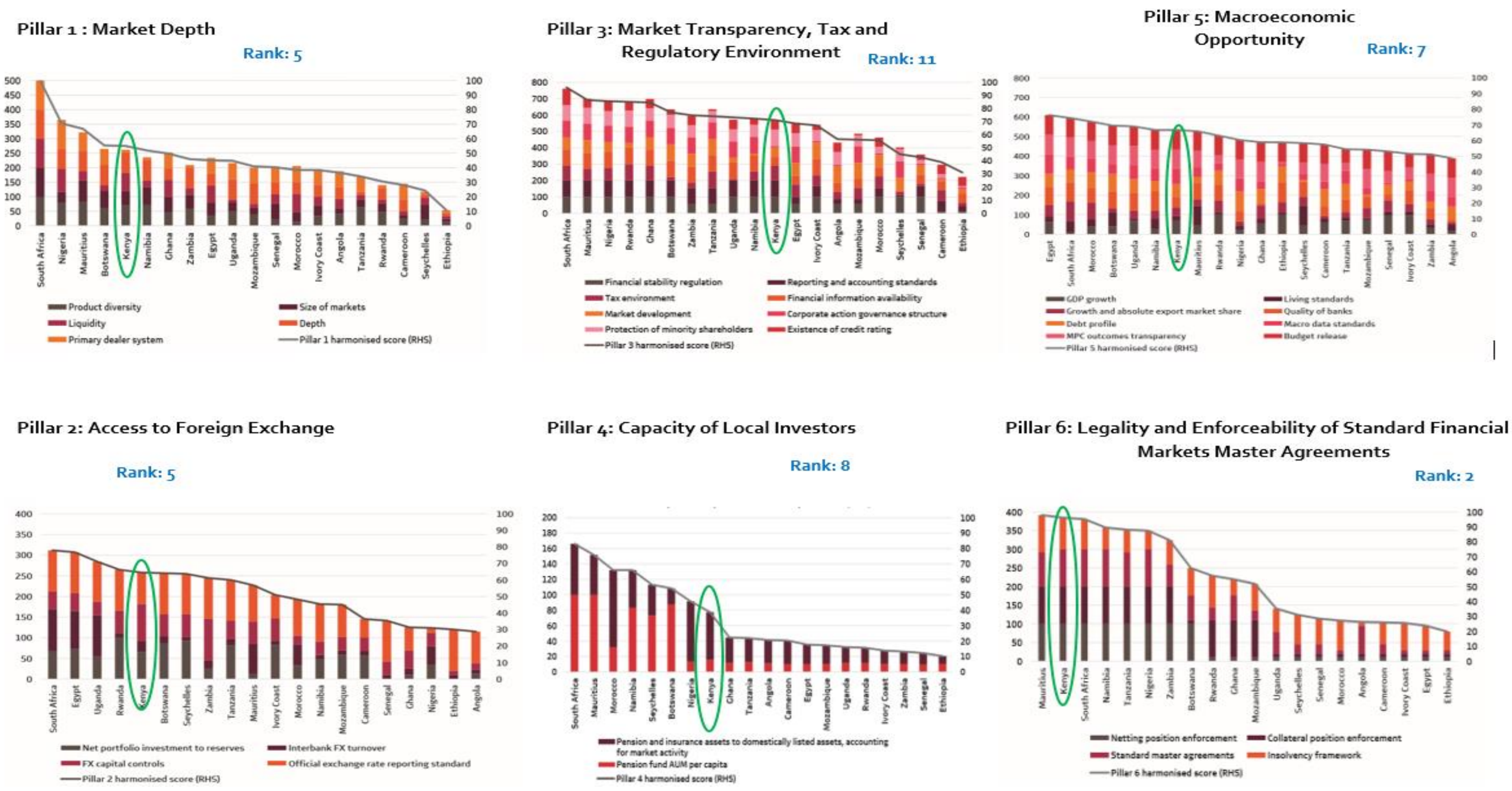
In early November 2019, the Finance Act 2019 repealed section 33b of the Banking Act that provides for the capping of interest rates following presidential ascent after rejection of the finance bill. The rate cap, imposed in 2016, has been blamed for curbing private sector lending growth and reducing the effectiveness of monetary policy. The cap has also had an impact on the wider economy as credit-starved businesses had to lay off staff. Although annual economic growth rates have exceeded more than five percent in the last five years, analysts continue to question the quality of the reported growth citing widespread unemployment and lack of access to funds for small businesses. The Central Bank of Kenya had publicly stated that the rate caps had rendered its monetary policy tools ineffective making it difficult to control inflation and the amount of money in circulation.The World Bank had also stated that interest rate caps undermined monetary policy transmission and implementation, with implications for CBK's independence and its ability to steer the economy.

[28] https://www.cnbc.com/2019/10/23/omfif-african-nations-building-deeper-more-transparent-financial-markets.html

[29] Intermediate exchange rate is defined by the ABSA report as one that floats within a pre-determined range, or the central bank may intervene occasionally in a managed float arrangement. May also be referred to as a soft or crawling peg.

Kenya's Ranking in the Absa Africa Financial Markets Index

Fig 10: Kenya's Overall Ranking and Positioning on Absa Financial Index 2019



Source: ABSA Africa Financial Index 2019

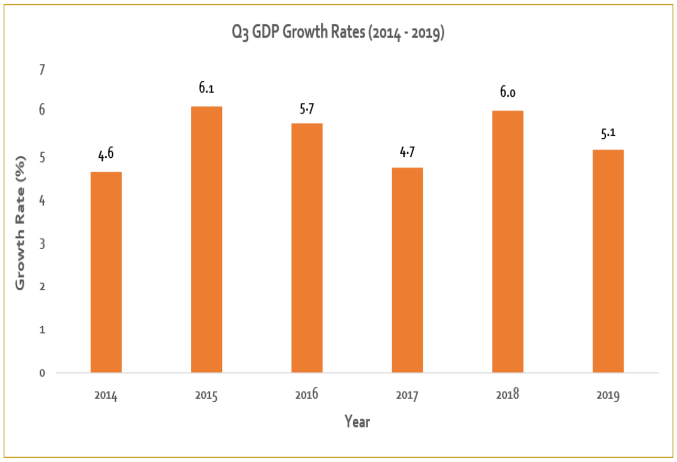
4.2 Growth Domestic Product (GDP) Growth Rates

The recent release on GDP by the Kenya National Bureau of Statistics (KNBS) indicates that economic activity grew at the rate of 5.1 per cent in the third quarter of 2019, down from the 5.6 per cent pace in the second quarter of 2019. The economy was subdued in the third quarter of 2019, growing by 5.1 per cent from 6.0 per cent growth registered during the same quarter in 2018. This growth rate has not been experienced since 2017 when Kenya recorded a growth rate of below 5.0 per cent.

Agriculture, Forestry and Fishing was mostly hampered by notable drop in production of key crops. Manufacturing was negatively impacted by low level of activity in the two main subsectors of the activity. That is, manufacture of food products and nonfood products. Electricity and Water supply sector was affected by insufficient rains during the second quarter necessitating increased use of expensive thermal energy during quarter three. Transport and Storage, Accommodation and food service, information and communication sectors recorded slowed growth during the quarter under review.

On the other hand, Construction, Financial and Insurance Activities, Mining and Quarrying, and Real Estate maintained high growths and thereby supported the overall gross domestic product (GDP) growth.

Figure 11 : Q2 GDP Growth Trend (2014-2019)

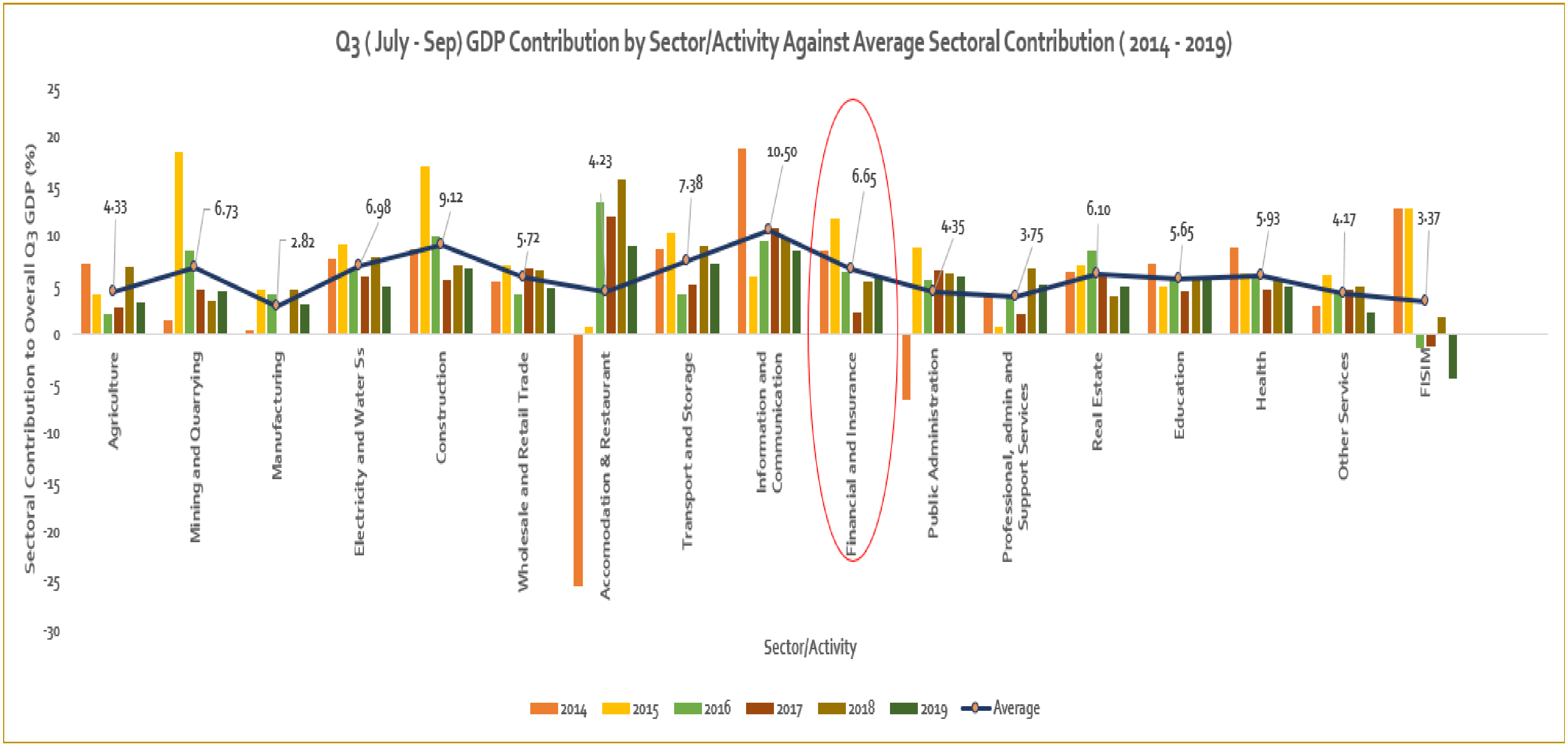


Source: KNBS

An analysis of sectoral contribution to Q3 GDP performance (*a graphical representation in fig 12 below*) indicates that only three sectors out of seventeen had a relative improvement in performance compared to Q3.2018. The sectors include mining and quarrying, financial and insurance and real estate whose Q3.2019 contribution increased marginally by a%, 0.3% and 1.10% respectively compared to Q3.2018 performance.

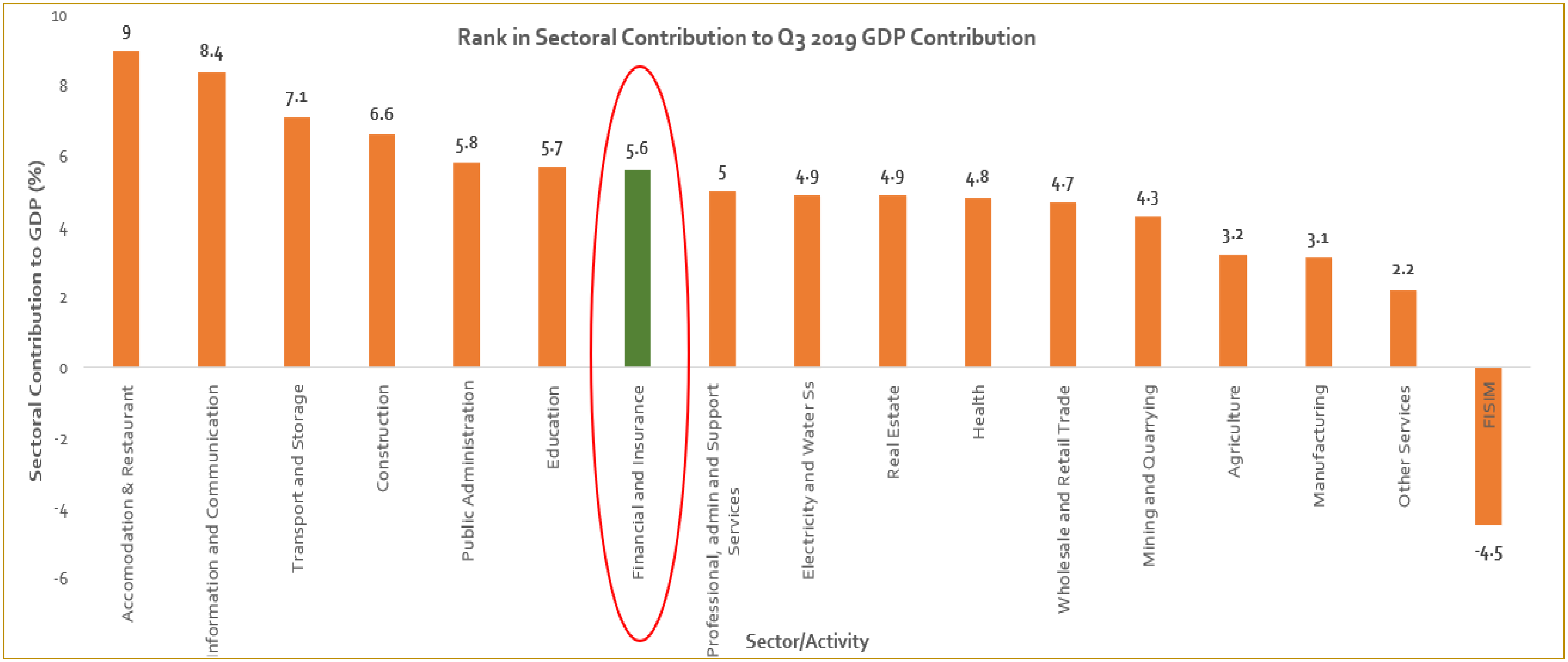
All other sectors recorded decreased GDP contribution with the highest loss of (6.7) % recorded by the accommodation and restaurant services.

Figure 12: GDP Contribution by Activity/ Sector



Source: KNBS

Figure 13: Rank of Sectoral Contribution to Q3. 2019 – Largest to Lowest



Source: KNBS

4.2 Inflation

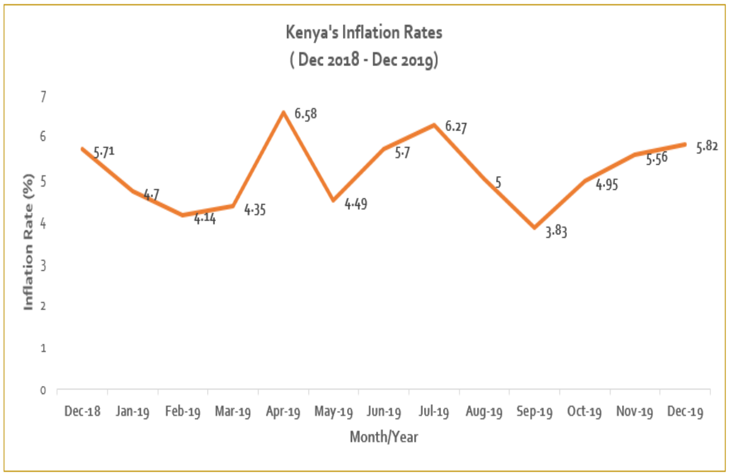
According to the most recent publication by Kenya National Bureau of Statistics on Consumer Price Indices (CPI) and Inflation Rates, overall year-on-year inflation stood at 5.82 % in December 2019. The CPI increased by 0.90 per cent from 202.94 in November 2019 to 204.77 in December 2019.

Between November and December 2019, Food and Non-Alcoholic Drinks' Index increased by 1.46 per cent mainly as a result of increase in prices of some foodstuffs outweighing decreases recorded in others.

For example, in December 2019 prices of Kales (Sukuma wiki), tomatoes, spinach, and onions increased by 5.6, 7.8, 9.1, and 5.1 per cent, respectively.

The 'year on year' food inflation dropped from 7.13 per cent in August 2019 to 6.31 per cent in September 2019. During the same period, Housing, Water, Electricity, Gas and Other Fuels' Index, increased slightly mainly attributed to higher prices of charcoal. The Transport Index increased by 2.1 per cent mainly due to increase in public transport fares.

Fig 14: Month-on-Month Inflation trends (Nov.2018 – Nov. 2019)



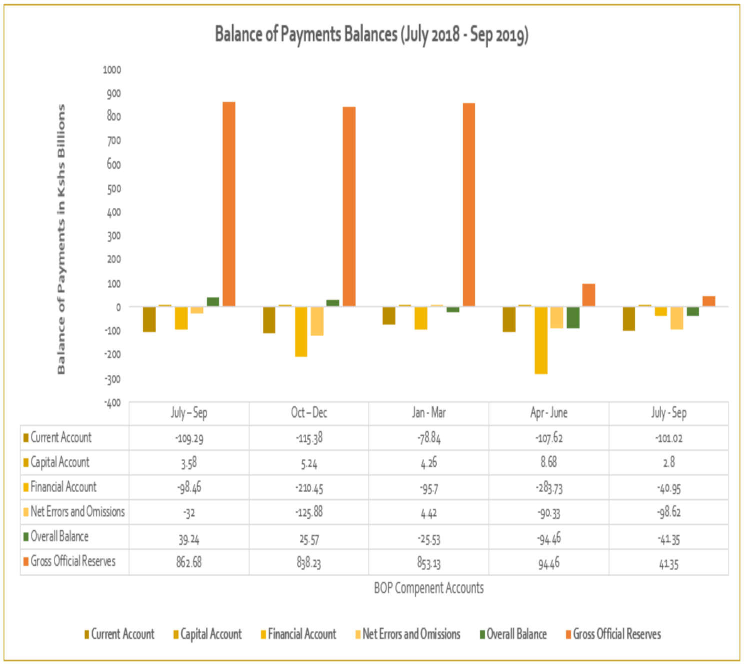
Source: KNBS

4.3 Balance of Payment Position

The most recent Q3.2019 Balance of Payments report by the Kenya National Bureau of Statistics indicated that the overall balance of payments position improved to a surplus of KShs 41.3 Bn in the third quarter of 2019 from a deficit of KShs 39.2 billion in the corresponding quarter of 2018. This, was as a result of the sum total of;

i. Improvement in the Current Account deficit from Kshs 109.29 Billion recorded in Q3.2018 to Kshs 101.02 Bn recorded in Q2.2019.
ii. Marginal increase of 1.0 per cent in the net inflows of international trade in service receipts accompanied by 2.5 per cent growth in service payments translating into 2.4 per cent decline in the net inflows to a surplus of Kshs 40.3 Bn.
iii. Increase in diaspora remittances by 5.1 per cent to Kshs. 68.0 Bn, boosting the secondary income account to a surplus of Kshs.128.9 Bn in Q2.2019.
iv. Surplus of Kshs 40.9 Bn in the financial account which reduced by more than 50 per cent from Kshs 98.5 Bn recorded in the corresponding quarter of 2018.
v. A 13.4 per cent increase in the stock of gross official reserves, standing at Kshs 978.6 Bn.

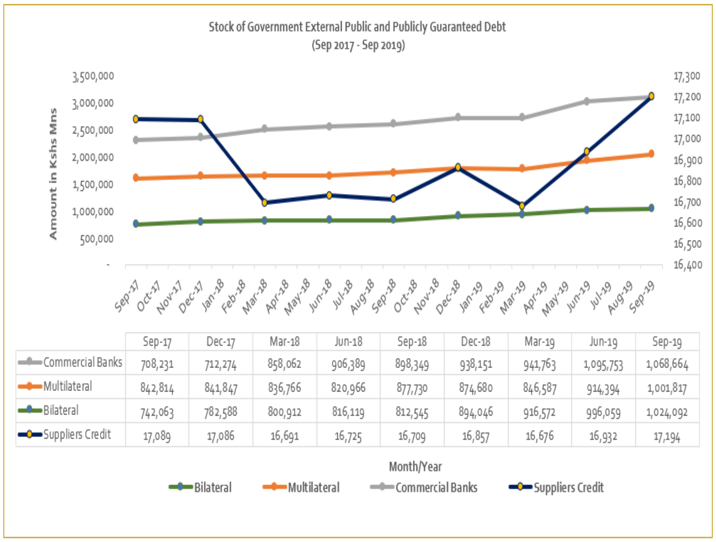
Fig 15: Balance of Payment Balances (July 2018 – Sep 2019)



Source: KNBS

4.4 Stock of Public External Debt

Figure 12: Stock of Government External Public and Publicly Guaranteed Debt



Source: KNBS

The outstanding external public and publicly guaranteed debt from 2016/17 to 2018/19. The stock of public external debt increased by 19.4 per cent from KShs 2,605.3 billion to KSh 3,111.8 billion as at end of September 2019. Stock of debt from commercial banks increased by 19.0 per cent to KSh 1,068.66 billion as at end of 2019

- *The development of a comprehensive Public Debt and Borrowing Framework by the National Treasury and Planning is a crucial step towards developing a comprehensive Public Debt and Borrowing Framework for Kenya. When finalized and implemented, we are confident that this policy document will guide high-quality and impactful decision making in public debt management and sustainability;*
- *We further observe that the draft framework asserts TNT&P[30]'s intention to enhance the Public Debt Management Office (PDMO); prepare an annual borrowing program and auction calendar, which will be key in accelerating ongoing Bond market reforms in Kenya. We further hope that this policy document will be able to clearly outline the borrowing/capital raising arrangements for Counties, which has remained ambiguous.*

4.5 Performance of Listed Companies

4.5.1 Price Gainers

Table 4: Top 10 Price Gainers – Q4.2019 Vs Q3.2019

Counter	Q3.2019	Q4.2019	% change
Equity	37.45	53.50	42.86%
WPP Scangroup	12.35	17.20	39.27%
Co-op Bank	11.90	16.35	37.39%
KCB Group	42.00	54.00	28.57%
Britam	7.08	9.00	27.12%
Stanlib	7.60	9.42	23.95%

[30] TNT&P – The National Treasury and Planning

NIC Group	29.95	36.85	23.04%
Home Afrika	0.49	0.60	22.45%
BBK	11.00	13.35	21.36%
Flame Tree Group	2.10	2.47	17.62%

Source: NSE

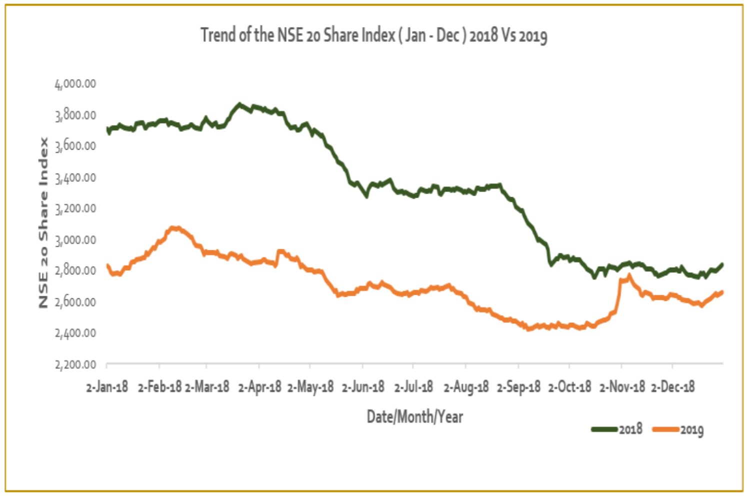
4.5.2 Price Losers

Table 5: Top 10 Price Losers – Q4.2019 Vs Q3.2019

Counter	Q3.2019	Q4.2019	% change
NBV	0.90	0.70	22.22%
TransCentury	3.16	2.50	20.89%
KQ	2.55	2.05	19.61%
Bamburi	93.00	80.00	13.98%
CIC Insurance	3.07	2.68	12.70%
TPS EA	19.25	17.55	8.83%
HF Group	7.04	6.46	8.24%
Total (K)	29.85	27.50	7.87%
Centum	31.45	29.50	6.20%
KPLC	2.92	2.81	3.77%

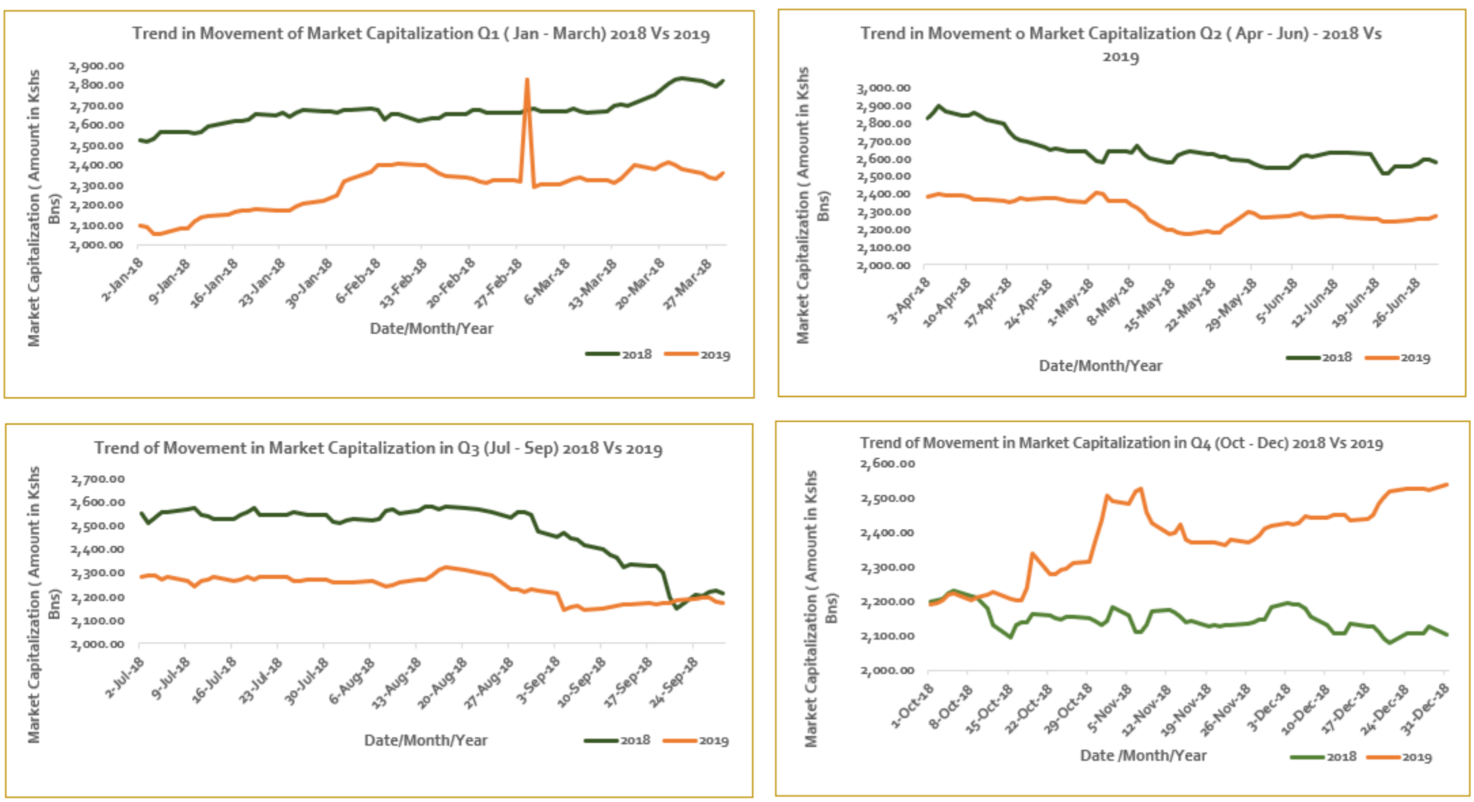
Source: NSE

Fig 17: Trend of the NSE 20 Share Index (Jan – Dec) 2018 Vs 2019



Source: CMA/NSE

Fig 18: Trend in Movement of Market Capitalization (Q1 – Q4) 2018 Vs 2019



Source: CMA/NSE

5.0 New Capital Markets Developments in Kenya

5.1 Kenya's Doing Business rating improves 5 places

Kenya has improved five positions to 56 globally on attractiveness to investors, the latest World Bank Ease of Doing Business has revealed. This is up from 61 last year. This has been pegged on among others, automation of systems that have made starting business in Kenya easy. The report also shows the introduction of online registration, modification and cancellation of security interests as well as public online searches of its collateral registry have lifted Kenya's access to credit ranking to fourth best in the world.

Further, the implementation of corporate governance rules that require shareholders to approve election and dismissal of external auditors has raised Kenya's investment profile, earning the country global acclaim as top protector of minority investor rights. The World Bank Doing Business 2020 report ranks Kenya top in the minority shareholder protection parameter. The rule on external auditor hiring and firing mark an improvement on minority investors' protection efforts Kenya adopted last year. The measures include increased disclosure requirements, regulation of transactions involving related parties and enhanced shareholders' role in major corporate decisions. Despite the improved position, the slow registration of property and starting a business remain the biggest hindrance.

Table 6: Kenya's 2020 Ease of Doing Business Metrics

	Indicator	Measure
1.	Dealing with construction	Permits Kenya made dealing with construction permits more transparent by making building permit requirements publicly available online, and by reducing fees.
2.	Getting electricity	Kenya improved the reliability of electricity supply by modernizing its existing infrastructure and by inaugurating a new substation in Nairobi.
3.	Registering property	Kenya made property registration more difficult because of an additional payment slip generation and increased online consent application and title search fees. At the same time, property registration was made faster by moving consents to transfer and payment verification online.
4.	Getting credit	Kenya strengthened access to credit by introducing online registration, modification and cancellation of security interests, and public online searches of its collateral registry.
5.	Protecting minority investors	Kenya strengthened minority investor protections by requiring shareholders to approve the election and dismissal of an external auditor. Paying taxes: Kenya made paying taxes easier by implementing an online filing and payment system for social security contributions.
6.	Resolving insolvency	Kenya made resolving insolvency easier by improving the continuation of the debtor's business during insolvency proceedings.

Source: World Bank EADBR 2020

5.2 Official launch of the Stewardship Code for Institutional Investors

The Authority officially launch the Stewardship Code for Institutional Investors on Thursday 5 December 2019 at 6.00pm at Fair View Hotel in Nairobi. The event brought together institutional investors to discuss the implementation of the Stewardship Code for Institutional Investors and the responsibilities of all the stakeholders. It provided an opportunity to celebrate the milestone, briefly share with institutional investors and other stakeholders on their very important responsibilities and have a conversation on how to collaborate for the betterment of our market.

5.3 Protection of Minority Investors Index

The Authority continue to implement the provisions of the Code. Kenya was ranked number 1 in the world in protection of minority shareholders. The Protection of Minority Investors Index measures the following-

- Conflict of interest regulation and the necessary disclosures;
- Extent of the liability of company directors;
- Ease of shareholders to file suits/cases to protect their interests; and
- Shareholder rights
- Ownership and control of companies and the disclosures
- Corporate transparency

Kenya's number one ranking was because of the following-

- The Companies Act and the amendments done in 2018 and 2019
- The Capital Markets Public Offers Regulations
- The Capital Markets Takeover and Mergers Regulations
- The mandatory provisions of the Corporate Governance Code
- Insolvency Act
- The online processes of the registration of companies

5.4 Integration of the capital markets surveillance system with the upgraded ATS and new CDSC system

The upgrades at the NSE and CDSC necessitated an upgrade to the integration of the current surveillance system deployed by the Authority that is MSS Capizar. The system obtains information from both the NSE and CDSC systems through an integration interface. The information is received on real time basis, stored in MSS Capizar and analyzed by surveillance analysts. In this regard, the vendor has completed the installation of the new patches to the MSS Capizar, and users are conducting user acceptance testing to the live environment.

5.5 Information Repository, Financial Analysis System, E-Learning and Video Conferencing

The contract for the consultancy was effected on 28th August 2017 with International Securities Consultancy (ISC) Ltd, aimed at developing the information repository specifications that would have Advanced Financial Analysis, Business Intelligence System, E-Learning System, Video Conferencing and enhance Communication/IT infrastructure capability for the Authority. The consultancy will enable the streamlining of the Authority's use of business intelligence through improved data collection and analysis and to strengthen internal capacity through e-learning.

Following the approval of the same by the World Bank, the Project Implementation Unit (PIU) and the Permanent Secretary National Treasury, the Tenders for Supply, installation & commissioning of a Data Repository & Business Intelligence System; and supply, implementation, training and commissioning of a Learning Management & E-Learning system and Video Conferencing System were advertised between September and December 2018.

The implementation of the various components is ongoing, and the aim is to complete on these before July 2020. The eLearning system component is to be re-advertised as per the recommendation of the tender evaluation committee.

5.6 CMA Publishes Second State of Corporate Governance Report

The Capital Markets Authority (CMA) has published the second State of Corporate Governance Report based on an assessment of 53 issuers of securities to the public in the 2018/19 financial year. The report is aimed at raising visibility of the state of corporate governance of issuers of securities to the public in Kenya in order to empower investors and respective boards to encourage continuous improvement in practices. The aim of the report is to encourage issuers of securities to consistently progress as model corporate citizens by adopting and fully implementing the Code and related corporate governance laws, standards and practices."

The report follows the evaluation of the second set of regulatory reports submitted in accordance with the Code of Corporate Governance Practices for Issuers of Securities to the Public, 2015 (the Code), which became effective in March 2017. The Code sets out the principles and specific recommendations on the structures and processes, which issuers should adopt in making good corporate governance an integral part of their business dealings and culture.

The Authority seeks to continually enhance the effectiveness of the assessment process and improvement of corporate governance practices of individual issuers against the Code and other globally accepted corporate governance & sustainability standards such as G20 OECD, IOSCO Corporate Governance Principles, IGCN, King IV, IRC, GRI, and SASB; amongst others.

5.7 Stakeholders' Workshops on The State of Corporate Governance of Issuers of Securities to the public In Kenya 2018/2019

The Authority hosted two Stakeholder Workshops on the State of Corporate Governance of Issuers of Securities to the public in Kenya for the 2018/2019 Financial Times on 3rd and 4th December 2019. The stakeholders' forums were aimed at highlighting & discussing the findings of the report, update on the feedback received so far from the stakeholders & the proposed way forward, discuss emerging issues & new developments in the corporate governance & sustainability space.

5.8 CMA launches the Stewardship Award for Institutional Investors as part of the ICS Champions of Governance (CoG) Awards

In November 2019, the Authority in collaboration with ICS, launched the Stewardship Award for Institutional Investors as part of the ICS Champions of Governance (CoG) Awards. The new Stewardship Award for Institutional Investors recognizes the important role played by institutional investors in championing and strengthening good governance. This is in line with the Stewardship Code for Institutional Investors that was developed by the institutional investor community under the guidance of the Authority. The new award category will go a long way in promoting a culture of stewardship and responsible management of resources by institutional investors.

5.9 Interaction with Shenzhen Securities Exchange under the China-Kenya Capital Markets Initiative forum

In line with the NSE vision ***to be the leading securities exchange in Africa with a global reach***, the exchange has embraced strategic partnerships as a key pillar to the success and growth of the capital market in Kenya. Through this approach, the NSE is now a renowned global exchange offering best in class products and services.

The Authority participated in the CMA, NSE and Shenzhen Securities Exchange organized consultation forum geared towards sharing experiences and finding areas of synergy between the two transcontinental exchanges. The forum also provided a platform for connecting Kenyan Micro, Small and Medium Enterprises to capital raising opportunities in China. The Authority made a presentation during the forum highlighting the key partnership areas with the Shenzhen including technical support, multi-asset surveillance, capacity building support, the vNext Board that is similar to NSE Ibuka/GEMS Board and support in the development of regulatory Sand Box to drive listings by tech companies.

The collaboration between the NSE and SZSE is well aligned with the long-standing **China-Kenya Bilateral Ties**, which seek to boost trade and development in both countries. In the same vein, the NSE and SZSE agree that China and Kenya have a great potential for economic cooperation, which is presently witnessing rapid growth in both jurisdictions. The capital market services are key in facilitating capital formation to stimulate these developmental goals.

Therefore, a high-level delegation from the SZSE visited the Kenyan Capital Markets on October 14-16, 2019. During the visit, the two exchanges hosted and launched for the first time a joint investor forum dubbed the **China-Kenya Capital Market Service Initiative Forum (the "*China-Kenya Initiative*").** The forum aimed at linking Micro, Small and Medium Enterprises (MSMEs) sector in Kenya to investors in Shenzhen to allow a capital formation platform on a larger scale.

The forum also presented the companies on the Ibuka Program to potential investors in China through the V-Next Platform.

5.10 Update on Islamic Finance

During the review period, the Authority engaged National Treasury & Planning on the FSD (Africa) submitted terms of reference (TORs) for a consultancy to draft a harmonized National Policy on Islamic Finance. As a result, National Treasury & Planning communicated to FSD (Africa) requesting for amendments to the TORs prepared by FSDA to incorporate requirements that among others, TNT & Planning will be the one to sign-off on satisfactory delivery of all the TOR provisions. The team is awaiting a concurrence of the FSDA and TNT & Planning before facilitating progress towards drafting the National Policy document.

5.11 County Financing Initiatives (Kenya Cities Forum)

Throughout the quarter, the Authority participated in Inter-agency Committee [31]meetings on Sub-national City Financing aimed at matching urban infrastructure demand by the 5 Kenyan cities (*Nairobi, Mombasa, Nakuru, Kisumu*

[31] The interagency committee members include representation from the Attorney General Office, Commission on Revenue Allocation, State Department of Devolution, State Department of Housing and Urban Development, the National Treasury, Kenya Investment Authority,

and Eldoret) with potential capital sources, mobilize domestic financial resources for urban infrastructure demand, obtain policy commitment on financing of cities and urban areas and enhance external financing for urban infrastructure demand.

Following the establishment of the inter-agency, the Ministry of Devolution organized three-day breakfast sessions targeting Investment Banks, Fund Managers and Trustees, Insurance Firms and SACCOs between 18th and 20th September 2019 at Laico Regency Nairobi.

The workshop provided a forum for brainstorming on the role of the private sector in financing public infrastructure projects by Kenyan Cities and subsequent development of a sub-national finance market in Kenya.

5.12 Legal and Regulatory Amendments to the Warehouse Receipt Regulations

Following the High-Level stakeholder engagements on the Capital Markets (Commodity Markets) Draft Regulations, 2019 and the Warehouse Receipt Regulations, 2019 done on August 13, 2019 and September 18, 2019, the following activities took place:

- KOMEX Taskforce committee met in November (4th to 9th) 2019 to discuss the views and input from the stakeholder engagements;
- The Regulations were presented before the CMA Compliance and Facilitation Committee on October 30, 2019 and before the Board of the Authority on November 25, 2019;
- The Taskforce participated in the pre-Gazettement conference with the Committee of Delegated Legislation from November 28th -30th 2019 where the Capital Markets (Commodity Markets) Draft Regulations, 2019 and the Warehouse Receipt Regulations, 2019 Regulations were discussed;
- Working retreat with the KOMEX Taskforce representatives to discuss and deliberate on the issue raised during the pre-Gazettement conference;
- Tabling of the Regulations before the CMA Full board on December 6, 2019; and
- The Regulations are being progressed to the National Treasury for Gazettement.

6.0 Capital Markets Stability Indicators (CMSIs)

Stability Indicator	Quarter/Year	Market Statistics				Assessment of Risk Level (High – Medium – Low)	Performance Brief for the Quarter	Ongoing Intervention Measures
1.0 Equity Market Depth								
NSE 20 Index Volatility **Base Year = 2010**	**Q4.2019**	**Oct**	**Nov**	**Dec**	**Q.Avg**	**Low** **(indicative - <10% high; >10% - low)**	• The NSE 20 Share Index volatility for the quarter ended Dec 2019 averaged at **0.47%**, compared to **0.44%** recorded in Q3.2019	• The level of volatility of the market as evidenced by the NSE 20 Share and NASI index, remained relatively low during the quarter though with a slight increase in December 2019. The market has remained relatively stable following the handshake with minimal shock – economic, regulatory and political. Further, In November 2019, the Finance Act 2019 repealed section 33b of the Banking Act that provides for the capping of interest rates, a move that was welcomed by the industry.
		0.44%	0.54%	0.42%	0.47%			
	Q3.2019	**July**	**Aug**	**Sep**	**Q.Avg**			
		0.49%	0.31%	0.52%	0.44%			
	Q2. 2019	**April**	**May**	**June**	**Q. Avg**			
		0.64%	0.42%	0.31%	0.45%			
	Q1.2019	**Jan**	**Feb**	**March**	**Q. Avg**			
		0.49%	0.37%	0.41%	0.42%			
NASI Volatility **Base Year = 2010**	**Q4.2019**	**Oct**	**Nov**	**Dec**	**Q. Avg**	**Low** **(indicative - <10% high; >10% - low)**		
		0.50%	0.76%	0.32%	**0.53%**			
	Q3.2019	**July**	**Aug**	**Sep**	**Q. Avg**			
		0.41%	0.36%	0.57%	**0.45%**			

	Q2.2019	**April**	**May**	**June**	**Q.Avg**			
		0.23%	0.80%	0.30%	**0.44%**			
	Q1.2019	**Jan**	**Feb**	**March**	**Q.Avg**			
		0.40%	0.41%	0.52%	**0.44%**			
Turnover Ratio	**Q4.2019**	**Oct**	**Nov**	**Dec**	**Q.Sum**	**Medium (indicative – annual: <8%- Low; >15% High)**	• A turnover ratio of **1.84%** was recorded in the quarter, compared to **1.37% and 1.39%** in Q3.2019 and Q2.2019 respectively indicating increased trading frequencies in Q4.2019	• In Q3.2019, the NSE, with approval from the Authority launched official trading of derivative futures which could be one of the factors contributing towards the increased turnover ratios. • Further during the quarter, Barclays Bank Futures were the sixth entry into the Nairobi derivatives market joining already trading stock futures on NEXT; Safaricom, KCB Group, Equity Group, EABL, and BAT.
		0.66%	0.71%	0.47%	**1.84%**			
	Q3.2019	**July**	**Aug**	**Sep**	**Q.Sum**			
		0.50%	0.39%	0.48%	**1.37%**			
	Q2.2019	**April**	**May**	**June**	**Q.Sum**			
		0.42%	0.55%	0.42%	**1.39%**			
	Q1.2019	**Jan**	**Feb**	**March**	**Q. Sum**			
		0.67%	0.50%	0.67%	**1.85%**			

2.0	Foreign Exposure Risk							
Foreign Investor turnover as a % of total turnover	Q4.2019	Oct	Nov	Dec	Q.Avg	Medium (indicative – annual: <40%-Low; >90% High)	• Average Foreign investor participation during the quarter averaged at **62.96%**, a **1.99%** decrease from **64.95%** recorded in Q3.2019 and the lowest ratio for the last four quarters.	• While foreign investor participation within the Kenyan market positions us as a global competitor, the Authority notes that the sustainability of the Capital Markets is equally dependent on participation by domestic investors- both retail and institutional. • Thus, in line with its market deepening strategy, the Authority will be rolling out a plan to onboard more domestic institutional investors and High Net Worth Individuals (HNWIs) into the secondary market and/or Collective Investment Schemes (CIS) to reduce the dominance of foreign investors
		64.29%	55.97%	68.63%	**62.96%**			
	Q3.2019	July	Aug	Sep	Q.Avg			
		66.89%	62.31%	65.65%	**64.95%**			
	Q2.2019	April	May	June	Q.Avg			
		75.80%	63.43%	74.15%	**71.13%**			
	Q1.2019	Jan	Feb	March	Q.Avg			
		81.55%	72.38%	70.81%	**76.96%**			
Net Foreign Portfolio Flow (In KES Millions)	Q4.2019	Oct	Nov	Dec	Q.Sum		• Net Foreign Portfolio levels during the quarter	
		(1,361)	(730)	1,247	**(844)**			
	Q3.2019	July	Aug	Sep	Q.Sum			
		(2,073)	1,509	827	**262**			

	Q2.2019	**April**	**May**	**June**	**Q.Sum**	**High (indicative – annual: <Kshs (50million) -High (outflow; >KShs. 50 million High inflow)**	amounted to a total outflow of **Kshs 844 Mn,** compared to a total inflow of **Kshs 262** in net foreign inflows during Q3.2019.	
		93	2,166	(900)	**1,359**			
	Q1.2019	**Jan**	**Feb**	**March**	**Q.Sum**			
		(1,357)	216	1,742	**601**			
3.0	**Market Concentration Risk**							
Market Concentration (Top 5 companies by market cap)	**Q4.2019**	**Oct**	**Nov**	**Dec**	**Q.Avg**	**High (indicative – annual: >50% High concentration)**	• During the quarter, the top five companies by market capitalization accounted for **73.35%,** the highest in the last four quarters, confirming	• Market concentration remains a key risk within the Kenyan Capital Markets landscape. • To diversify the number and quality of listed entities at the bourse, the Authority has adopted a strategy aimed at attracting other big industry players to consider listing on the exchange.
		73.25%	73.34%	73.46%	**73.35%**			
	Q3.2019	**July**	**Aug**	**Sep**	**Q.Avg**			
		70.85%	72.02%	72.61%	**71.83%**			
	Q2.2019	**April**	**May**	**June**	**Q. Avg**			
		70.17%	71.62%	70.62%	**70.80%**			
	Q1.2019	**Jan**	**Feb**	**March**	**Q. Avg**			
		65.34%	67.85%	69.56%	**67.58%**			

		their dominance in the Kenyan securities market.	• This is expected to decrease the concentration as is currently and equally give investors a diversified portfolio of investments for consideration.	
4.0	**Derivatives Trading Statistics**			
Total Volume **(No. of contracts)**		**Low**	During the quarter, a total of 207 contracts were traded. Safaricom Single Stock Futures accounted for 71.06% of contracts traded.	To diversify the derivative market, the NSE is considering increasing the number of Single Stock Futures traded.

	Oct	Nov	Dec	Q. Sum
25-Share Index	-	1	-	1
SCOM SSF	59	38	40	**137**
EQTY SSF	9	15	11	**35**
KCBG SSF	7	11	9	**27**
EABL SSF	-	1	1	**2**
BATK SSF	-	2	3	**5**
BBKL	-	-	-	-
Total	**75**	**68**	**64**	**207**

<table>
<tr>
<td>Gross Notional Exposure (GNE)[32]

(Amount in Kshs Mn)</td>
<td>
<table>
<tr><th></th><th>Oct</th><th>Nov</th><th>Dec</th><th>Q. Avg</th></tr>
<tr><td>25-Share Index</td><td>-</td><td>391,200</td><td>-</td><td>391,200</td></tr>
<tr><td>SCOM SSF</td><td>1,667,800</td><td>1,128,660</td><td>1,221,350</td><td>1,339,270</td></tr>
<tr><td>EQTY SSF</td><td>386,060</td><td>738,000</td><td>573,040</td><td>565,700</td></tr>
<tr><td>KCBG SSF</td><td>343,000</td><td>547,150</td><td>471,000</td><td>453,717</td></tr>
<tr><td>EABL SSF</td><td>-</td><td>20,500</td><td>19,300</td><td>19,900</td></tr>
<tr><td>BATK SSF</td><td>-</td><td>93,000</td><td>138,750</td><td>115,875</td></tr>
<tr><td>BBKL</td><td>-</td><td>-</td><td>-</td><td>-</td></tr>
<tr><td>**Total**</td><td>**2,396,860**</td><td>**2,918,510**</td><td>**2,423,440**</td><td>**2,579,603**</td></tr>
</table>
</td>
<td>**Low**</td>
<td>The average Gross Notional Exposure recorded as at Dec 2019 stood at Kshs. 2.58 Million with Safaricom, Equity and KCB as the top 3 counters.</td>
<td rowspan="2">The NSE are engaging institutional investors (foreign and domestic) to expand the scope of fund allocations to include derivative contracts.</td>
</tr>
<tr>
<td>Total Open Interest[33]

(No. of Contracts)</td>
<td>
<table>
<tr><th></th><th>Oct</th><th>Nov</th><th>Dec</th><th>Q. Avg</th></tr>
<tr><td>25-Share Index</td><td>-</td><td>1</td><td>1</td><td>**1**</td></tr>
<tr><td>SCOM SSF</td><td>39</td><td>30</td><td>2</td><td>**24**</td></tr>
<tr><td>EQTY SSF</td><td>3</td><td>4</td><td>-</td><td>**4**</td></tr>
<tr><td>KCBG SSF</td><td>4</td><td>5</td><td>-</td><td>**5**</td></tr>
<tr><td>EABL SSF</td><td>1</td><td>1</td><td>-</td><td>**1**</td></tr>
</table>
</td>
<td>**Low**</td>
<td>The total open interest during the quarter Averaged at 31 contracts with Safaricom holding 75% of the share with 24</td>
</tr>
</table>

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

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

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<table>
<tr><td>BATK SSF</td><td>-</td><td>2</td><td>1</td><td>2</td></tr>
<tr><td>BBKL</td><td>-</td><td>-</td><td>-</td><td>-</td></tr>
<tr><td>Total</td><td>47</td><td>43</td><td>4</td><td>31</td></tr>
</table>
</td>
<td></td>
<td>open contracts for trading.</td>
<td></td>
</tr>
<tr>
<td>Settlement Guarantee Fund (SGF) Coverage[34] for Derivatives</td>
<td>
<table>
<tr><td></td><td>Oct</td><td>Nov</td><td>Dec</td></tr>
<tr><td>SGF</td><td>180,638,962</td><td>181,762,119</td><td>179,054,811</td></tr>
<tr><td>Average Market Value</td><td>126,150.53</td><td>181,469.38</td><td>337,605.71</td></tr>
<tr><td>SGF Coverage</td><td>1,432 times</td><td>1,002 times</td><td>530 times</td></tr>
</table>
</td>
<td>Low</td>
<td>The SGF coverage ratio for the derivatives market as at end Dec 2019 was 530 times reflecting high sufficiency of the Guarantee Fund to cover trading volumes in the market.</td>
<td>To maximize value from the SGF fund balances, there is deliberate effort by NSE to encourage increased activity by market intermediaries in this market</td>
</tr>
</table>

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

<table>
<tr>
<td>SGF Coverage of Clearing Member 1 and Clearing Member 2[35]</td>
<td>
<table>
<tr><th></th><th>Oct</th><th>Nov</th><th>Dec</th></tr>
<tr><td>SGF</td><td>180,638,962</td><td>181,762,119</td><td>179,054,811</td></tr>
<tr><td>Average Value CM1</td><td>97,017</td><td>141,916</td><td>266,802</td></tr>
<tr><td>Average Value CM2</td><td>29,134</td><td>39,553</td><td>70,804</td></tr>
<tr><td>SGF Coverage CM1</td><td>1,862 times</td><td>1,281 times</td><td>671 times</td></tr>
<tr><td>SGF Coverage CM2</td><td>6,200 times</td><td>4,595 times</td><td>2,529 times</td></tr>
</table>
</td>
<td>Low</td>
<td></td>
<td>for increased volumes of trade. During the quarter, the NEXT Derivatives market added Barclays Bank Futures as a tradeable contract exchange further boosting portfolio of available contracts for trading.</td>
</tr>
</table>

5.0	**Government Bond Market Exposure**						
	Q4.2019	**Oct**	**Nov**	**Dec**	**Q.Avg**	**High**	

[35] Total SGF Amount/Average value of the positions of CM1 CM2

<table>
<tr>
<td>Treasury Bond market turnover Concentration</td>
<td>
<table>
<tr><td></td><td></td><td></td><td></td><td></td></tr>
<tr><td></td><td>99.86%</td><td>98.29%</td><td>99.98%</td><td>99.37%</td></tr>
<tr><td>Q3.2019</td><td>July</td><td>Aug</td><td>Sep</td><td>Q.Avg</td></tr>
<tr><td></td><td>97.54%</td><td>98.55%</td><td>99.94%</td><td>98.68%</td></tr>
<tr><td>Q2.2019</td><td>April</td><td>May</td><td>June</td><td>Q.Avg</td></tr>
<tr><td></td><td>99.99%</td><td>100%</td><td>99.96%</td><td>99.98%</td></tr>
<tr><td>Q1.2019</td><td>Jan</td><td>Feb</td><td>March</td><td>Q.Avg</td></tr>
<tr><td></td><td>99.96%</td><td>99.84%</td><td>99.90%</td><td>99.90%</td></tr>
</table>
</td>
<td>(indicative – annual: >50% High concentration)</td>
<td>● During the quarter, Treasury bond turnover leveled at 98.68% compared to 99.98% in the previous quarter.</td>
<td rowspan="2">● The skewed shareholding of corporate bonds by local investors to the tune of 98% is an indication of demand by local investors – retail and institutional for corporate bonds as they contribute towards the growth and development of local companies. Despite a slow down in the corporate bond market in the last few years, the Authority is working closely with potential issuers to facilitate corporate bond issuance in the near future, with the successful issuance of the Acorn Medium Term Note in 2019 showing signs of positive market interest in the corporate bond market.
● The recent establishment of the Kenya Mortgage Refinancing Company (KMRC)</td>
</tr>
<tr>
<td>Corporate Bond Market ownership</td>
<td>
<table>
<tr><td>Category</td><td>No of Investors</td><td>Share Quantity (In Millions)</td><td>% of total share quantity</td></tr>
<tr><td>Local Investors</td><td>2,933</td><td>39,737.02</td><td>98.74%</td></tr>
<tr><td>East African Investors</td><td>7</td><td>43</td><td>0.11%</td></tr>
<tr><td>Foreign Investors</td><td>35</td><td>464.25</td><td>1.15%</td></tr>
<tr><td colspan="4">Source: CDSC Data as at December 2019</td></tr>
</table>
</td>
<td>High
(indicative – annual: >50% High concentration</td>
<td>● Local Corporate bond investors were the leading investors in corporate bonds at 98.74% of amounts outstanding,</td>
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<tr><td></td><td></td><td></td><td>while foreign bond investors held **1.15%** of total corporate bond holdings.</td><td>is further expected to deepen the bond market when it considers it leverages on capital markets to raise funds through bonds for on-lending to banks and other mortgage financing companies.</td></tr>
<tr><td>6.0</td><td colspan="4">Investor Profiles - Equity Market</td></tr>
<tr><td>Equity Market</td><td>
<table>
<tr><th>Type of Investor</th><th>No. of Investors</th><th>Share Quantity (In Millions)</th><th>% to Total Share Quantity</th></tr>
<tr><td>Local Investors</td><td>2,0006,348</td><td>75,822.95</td><td>79.78%</td></tr>
<tr><td>EA Investors</td><td>9,100</td><td>973.22</td><td>1.02%</td></tr>
<tr><td>Foreign Investors</td><td>15,028</td><td>18,225.52</td><td>19.18%</td></tr>
<tr><td>BR</td><td>18</td><td>12.72</td><td>0.01%</td></tr>
<tr><td>JR</td><td>276</td><td>0.1</td><td>0.001%</td></tr>
</table>
Source: CMA- *Data as at December 2019
</td><td>Medium

(indicative – annual: >50% High concentration)</td><td>• Local investors, a sum of East African institutional and individual investors accounted for 80.81% of shares held in the equity market with 19.18% being held by</td><td>• 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 in consultation with the NSE, market intermediaries and other stakeholders is implementing a public education, awareness and market deepening strategy</td></tr>
</table>

							foreign investors.	based on among other guides, the Investor Education Impact and Opportunities Analysis Study. Some of the key deliverables include the development of a National Consumer Financial Education Strategy as well as 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.
7.0	**Settlement Compensation Coverage**							
Settlement Guarantee Fund	**Q4.2019**	**Oct**	**Nov**	**Dec**	**Q.Avg**		● SGF Ratio for the quarter ended Dec 2019	● Through Risk-based supervision, the Authority has been monitoring the SGF figures and the financial
		1.27	1.21	1.56	1.35			
	Q3.2019	**July**	**Aug**	**Sep**	**Q.Avg**			

(SGF) Coverage Ratio[36]		2.01	2.33	1.92	2.09	**Medium** **(indicative – annual: > 1 times, implies full coverage)**	averaged at 1.35 compared to 2.09 in the preceding quarter. This is largely attributed to a 57.42% increase in average daily market turnover in Q4 compared to Q3 despite SGF balances increasing by 2.08% between Sep 2019 and Dec 2019.	position of the firms to ensure that they are in good standing and that investors are protected. •
	Q2.2019	**April**	**May**	**June**	**Q.Avg**			
		1.87	1.64	1.70	1.74			
	Q1.2019	**Jan**	**Feb**	**March**	**Q.Avg**			
		1.30	1.28	1.20	1.26			

36 ***Source: CDSC***

8.0	Asset Base of Fund Managers, Stockbrokers, Investment Banks							
Assets Under Management	**As at 30th November 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 30th Nov 2019 was **Kshs 7,129.38 Million, 2,197.66 Billion, Kshs.13,331.67 Million, Kshs 1,688.62 Million** and	• 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 potential bankruptcy of licensees.
	CMA Licensee	**Total Assets**	**Total Liability**	**Net Assets**				
	Fund Managers	7,129.38	1,482.35	6,734.88				
	Stockbrokers	2,197.66	744.42	1,453.23				
	Investment Banks	13,331.67	4,605.15	9,131.31				
	Investment Advisors	1,688.62	168.99	1,603.30				
	Online Forex Broker (Non-Dealing)	782.28	600.55	181.73				

							Kshs 782.28 Million respectively.	

7.0 References

1. World Economic and Financial Surveys – Regional Economic Outlook; "Sub-Saharan Africa Restarting the Growth Engine."
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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