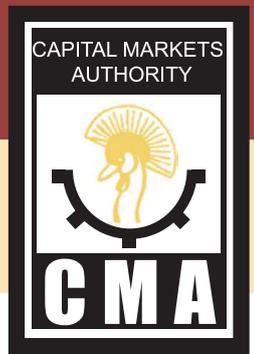


Capital Markets Authority

Quarterly Review



A quarterly Publication of the Capital Markets Authority

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INTRODUCTION

This Electronic Quarterly Review Covers the period April – June 2007.

April – June 2007, Volume 8, Number 2

Regulatory Issues

New Licences

On May 22nd 2007, Capital Markets Authority (CMA) approved and registered two new Investment Advisors, Dero Capital Ltd and Bullion Capital Ltd. Dero Capital Ltd is a corporate advisory entity targeting growing companies which seek to raise capital. It was granted an Investment Advisers licence part (a) and (b) only, i.e. the business of advising others concerning securities and issuing analyses or reports concerning securities.

Bullion Capital was granted an Investment Advisers licence part (a) only, i.e. the business of advising others concerning securities. It is a provider of offshore financial services. The full addresses and contacts of the licenses can be found at the end of this Quarterly Review.

Commonwealth Secretariat Legal Review Team

Consultants from the Commonwealth Secretariat visited Uganda between 18th and 27th June 2007. The Commonwealth Secretariat has been providing technical assistance to CMA relating to the review of the CMA Act and

an application to become a signatory to the International Organization of Securities Commissions (IOSCO) Multilateral Memorandum of Understanding (MMOU). The consultants discussed other laws and regulations that need to be amended including Insider dealing regulations, the Code of Conduct, Takeovers & Mergers Regulations, and Corporate Governance Guidelines. During their visit the Consultants met with the Board of Capital Markets Authority and gave a brief presentation on the progress made so far on the Commonwealth mission to Uganda.

Public Education

In this quarter, the Authority's public education focused on two main activities; the Eastern Regional Trade Fair and the Capital Markets Secondary Schools Challenge.

Eastern Regional Trade Fair 31st May-6th June 2007

CMA participated in the Eastern Regional Trade Fair (ERTF) that was held in Mbale, from 31st May to 6th June 2007. Information brochures were distributed to members of the public and the over 180 exhibitors from Kenya, Tanzania and Uganda. CMA officials also visited Bugisu Progressive S.S, Mbale Modern High School, Mbale Parents School, Manafwa High School and Mbale Riverside S.S. where presentations on capital markets were made. CMA officials further made presentations to the Mbale Business Community and the Mbale Rotary Club with emphasis on saving and investment

options available in the capital markets industry. CMA officials also participated in a live radio talk show at Open Gate Fm where issues on capital markets were further expounded.

The New CMA website: A more dynamic public education tool

Following the need to march with market trends, CMA has designed a new website geared at more public education and investor protection. One of the main features of the website include a discussion forum called "Capital Markets Think Tank" that is meant to encourage interaction amongst the public on current but local issues in Capital Markets.

For more information, visit our website on www.cmauganda.co.ug.

Highlights

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Capital Markets Secondary Schools Challenge 2007

This year's annual Capital Markets Secondary Schools Challenge was held over the months of April, May and June 2007. In this year's Challenge, 43 schools participated in the essay competition, of which those that presented the best twenty essays were chosen to participate in the quiz competition.

The quiz competition of the Challenge was held on 18th and 19th June 2007, at Kabira Country Club, Bukoto with Francis Kwesiga and Alex Kamugisha of Green Hill Academy emerged as overall winners of the Challenge. Joseph Tamale and Mark Arinaitwe of King's College Budo were the first runners up, whereas Robert Birungi and Stella Namatovu of Mengo Senior School were the second runners up, as well as the winners of the essay competition. Aaron Kiwanuka and Gloria Mahoro of Gateway High School were also recognized as top performing new entrants to the Challenge. The two winners, from Green Hill Academy along with their patron teacher, Mr. Francis Twesigawe, were hosted in Nairobi by the Capital Markets Authority Kenya, from 24th to 26th June 2007, where they visited Kenya's various players in the Capital Markets industry including Nairobi Stock Exchange, Retirement Benefits Authority and Suntra Investment Bank.

CMA is grateful to the GTZ/Sida FSD Programme for co-sponsoring the winners' trip to Nairobi and also the bulk of the Challenge's activities, to the New Vision, for providing prizes for the winners as well as to the Capital Markets Authority Kenya and our other Kenyan partners, for hosting the winners of the Challenge. The quiz competition will be shown on UBC on 25th & 26th August and on 1st & 2nd September 2007 on WBS.

Regional and International Co-operation

Budget Highlights

The budgets of Kenya, Uganda and Tanzania were read on 14th June 2007. Budget highlights from Kenya and Uganda pertaining to capital markets development are summarised below;

Uganda

Pension Reform

The Minister of Finance, Uganda Hon. Dr. Ezra Suruma in the Budget speech said that he had to resist pressures to move Pension reform hurriedly so as to avoid the disastrous mistakes which in the not so distant past wiped out the savings of tens of thousands of the people of Uganda. He reiterated the Government's assurance that an adequate regulatory framework would be put in place to protect the retirement savings of all Ugandans. He added that the Government would resist pressures to use pension savings for speculative gain. He assured Ugandans that the regulatory system to be established would;

- Take full advantage of best practices in the world;
- Provide for safe investment of those funds;
- Provide a fair return to members;

- Widen access to the greatest possible number of people so as to have an increasing measure of income security.

Pension Arrears

The Minister announced that financing had been provided in next year's budget to clear up US\$280 billion of arrears of which US\$200 billion will be for outstanding pension arrears. Over the medium term, resources will be set aside to clear the present stock of pension arrears, while at the same time aiming to convert the present system, to a contributory scheme, to prevent further accumulation of arrears. Additionally, the Government provided US\$17.5 billion to local governments that are increasingly burdened by the inability to pay pension leading to the accumulation of pension arrears. The funds will enable the settlement of verified Local Government pension arrears.

High Lending Rates

To address the high lending rates that have become a persistent problem, the Minister announced that Government has taken some decisive measures to solve the problem.

- First, Government has increased the capitalization of Uganda Development Bank (UDB) by

US\$20 billion in the past 2 years. The lending rates at UDB are lower than those of commercial banks and are intended to assist small and medium investors to access medium and long term funds.

- Secondly, Government has committed itself to support Savings and Credit Cooperative Societies (SACCOS) with the necessary infrastructure. This is to help reduce their cost of establishment so that they can lend at lower interest rates since they now have lower overhead costs.
- Finally Government lifted the ban on entry into the commercial banking sector in order to increase competition.

Uganda Development Bank Industrialization Bond

To maximize industrial development and to promote innovations in science and technology, the Minister announced that the Government would increase capital funds for processing and marketing through the issue of an Industrialization Bond. The Government will support the Uganda Development Bank and

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other development banks in raising at least US\$50 billion for small and medium scale enterprises, and cooperatives involved in processing. These funds will be made available to the private sector regionally, and if possible internationally, at competitive interest rates.

Tax Amnesty

The Minister stated that a number of tax defaulters would like to pay their outstanding obligations but are wary of the penalties that they face which sometimes surpass the principal tax. A few have approached Government for clemency. To encourage voluntary compliance the Minister proposed an amnesty on penalties and interest to all taxpayers who voluntarily disclose and pay their principal tax liability. The amnesty will cease on 31st December 2007. The details are contained in the Finance Bill 2007.

Kenya

Changes to the CMA Act

The Minister of Finance, Kenya, Hon. Amos Kimunya made a number of changes to the Capital Markets Authority Act, giving CMA-Kenya more authority in imposing sanctions, increasing the level of penalties and compensation under the Act, and tightening investor compensation and protection provisions. These provisions should help improve regulation and supervision in the capital markets and increase investor confidence.

In addition to advising the Minister on the development of capital markets, formulating policies, rules and guidelines, granting or cancelling licenses etc, CMA(K) now has the powers to impose financial penalties to persons committing a breach of the Act or Regulations. CMA (K) can also order the violator to remedy the breach, including compensating the aggrieved party. Furthermore, CMA(K) will have specific powers to deal with various types of defaulters including listed companies, licensed persons and their employees and directors.

The sanctions or penalties may range from suspension of trading and revoking licenses to forced termination of employment, disqualification from directorships of listed companies as well as financial penalties and liability to pay compensation to aggrieved parties. The CMA(K) is also required to publish a "List of Shame" in its annual report –with names of persons against whom any of the above actions has been taken. These measures are expected to strengthen the Authority's supervisory capacity, and act as a deterrent to unscrupulous companies and individuals looking to make quick profits at the expense of gullible investors. However, it will be effective only if the CMA actually enforces these sanctions.

Increased level of financial penalties and investor compensation

The Minister also made several proposals to increase

the level of penalties and compensation for breach of the CMA Act. In case of an illegal securities transaction by a licensed person that results in a loss to an investor, the guilty party is liable to compensate the aggrieved investor for:

- ⊙ The loss or adverse impact of the breach
- ⊙ The profits that have accrued to the former

However it is not clear whether the liability is the higher of the two or whatever the Authority determines. The Minister of Finance included specific penalties for breach of trading rules by a licensed person, failure to comply with reporting requirements, failure by a securities exchange to enforce compliance with the Act and the rules of the securities exchange. The Act further specifies that all financial penalties will be paid into the existing Investor Compensation Fund which will continue to compensate investors who suffer losses as a result a broker or dealer failing to compile.

In the previous budget the Minister of Finance proposed that unclaimed dividends outstanding in listed companies for more than seven years be transferred to the Investor Compensation Fund. He corrected some drafting errors in this budget and also provided that beneficiaries who resurface after this period would be paid from the Fund. The Minister also proposed to establish an Investor Compensation Fund Board, a corporate body whose function would be to administer the Investor Compensation Fund.

Quote

"A CARICATURE OF THE INVESTMENT WORLD DIVIDES IT INTO TWO CAMPS: VALUE INVESTORS, WHO BUY STOCKS THAT HAVE FALLEN IN PRICE IN THE BELIEF THAT THE REST OF THE MARKET HAS MISSED A BARGAIN; AND GROWTH OR MOMENTUM INVESTORS, WHO BUY STOCKS THAT HAVE GONE UP IN THE HOPE THAT THEY TURN OUT TO HAVE BEEN 'CHEAP AT ANY PRICE.' VALUE INVESTORS DISPUTE THE EFFICIENT MARKET HYPOTHESIS, WHICH SUGGESTS THAT PRICES REFLECT ALL AVAILABLE INFORMATION, AND SEE INVESTMENT OPPORTUNITIES CREATED BY DISCREPANCIES BETWEEN STOCK PRICE AND THE UNDERLYING VALUE OF COMPANY ASSETS."

From the Ultimate Investor

East African Investor Status

In the spirit of regional integration, the Minister of Finance increased the proportion of Initial Public Offers reserved for EAC citizens from 25% to 40%.

Dividend Withholding Tax Rate

Previously, Kenyan residents were subject to a dividend withholding tax rate of 5% while non-residents a higher rate of 10%. In the spirit of the East African Community, the Minister of Finance extended the rate of 5% to all citizens of the East African Community (EAC). This may bring smiles to those EAC citizens who are based outside the Community and who can now enjoy the lower rate effective 15 June 2007. Non-citizens who are resident in Tanzania or Uganda will not be equally happy thus the need for governments in these countries to harmonize their withholding tax rates in line with Kenya's rates.

Stamp Duty

The Minister of Finance abolished stamp duty payable on the share capital or increase in share capital of a company listed on the Nairobi Stock Exchange. However he also removed the stamp duty exemption on listings or transfers of asset-backed securities. These still remain in place in Uganda.

Tax Free Monthly Pension

The Minister of Finance introduced a new incentive for senior citizens. The monthly pension received by a pensioner who has reached 65 years of age is exempt from tax effective 15 June 2007. However, it appears that

this exemption does not apply to lump sum withdrawals. This will further encourage saving through pensions, thereby availing more funds for long-term investments not only in the Kenyan but also in the East African market.

National Social Security Fund-Kenya

Previously, the law did not allow for casual workers, self-employed persons or an employer with less than five employees to make voluntary contributions to the NSSF. This has now been rectified by the Minister of Finance with effect from 1 January 2008. This move is aimed at giving these individuals the opportunity to save for their retirement from as early an age as 16 years. This will go along way in widening the resource base of long-term funds; a positive development for Capital Markets in the East African region. However this is a position the Ugandan and Tanzanian governments should emulate if the East African region is to fully benefit from the pension sector.

Retirement Benefits & Mortgage Finance

The Retirement Benefits Act will be amended to provide for a proportion of a member's benefits arising from a scheme to be used as security for mortgage loans. This could be a major boost to the mortgage industry as well as release long-term funds to make mortgage securitization a reality in Kenya. As the Ugandan government seeks to provide affordable and quality housing to all Ugandans, might need to consider emulating the Kenyan government by allowing the contributors to NSSF use some of their contributions as security for mortgage loans.

International News

The Sovereign Loses its Crown (*Economist June 23rd 2007*)

This year, firms in emerging markets have raised more than twice as much in international markets as have sovereigns. This has been a complete shift from what the statistics showed 5 years ago. This has been as a result of several factors some of which governments like Argentina borrowed less as their fiscal positions improved, (giving an edge to corporate debt); and the credit ratings for individual firms that are higher than their home country governments. Russia's biggest energy company Gazprom and India's ICICI Bank present good examples. However, if economies take a sharp turn for the worse, investors may be risk averse in investing in corporate debt. Apart from the legal difficulties in enforcing debt contracts in emerging markets, the ability to secure payments is closely correlated with other measures of public health like corruption control and tax compliance. So, even though companies are becoming bigger borrowers than countries, government policy still matters and the sovereign still counts.

Home News

The annual Kikonyogo Capital Markets Award was held on 27th June 2007. The KCMA which doubled as CMA's 10th Anniversary dinner celebration was graced by Ambassador James Baba, Minister of State in the Vice Presidents Office who represented the Vice President as Chief Guest and Mr. Gerald Mahinda, Group CEO of East African Breweries Ltd who was the keynote speaker. The colourful occasion recognised Dr Martin Alier, Stanbic Bank Board Chairman, Mr Andrew Owiny, Executive Director MBEA Brokerage Services and Gary Watson (2007 Winner), Executive Director of African Alliance for their contribution to capital markets development. The event also honoured Mr Kitili Mbathi, Managing Director, Stanbic Bank, with an *Eximius Award* for his contribution to capital markets development in Uganda, by spearheading the listing of the largest ever Initial Public Offer in Uganda. (*More in the Press Report*)

Outlook

East African Securities Regulatory Authorities (EASRA)

The next EASRA meeting is scheduled to take place in Nairobi in August 2007. The meeting will discuss the draft Terms of Reference that have been drawn up by the International Finance Corporation (IFC) Efficient Securities Markets Institutional Development (ESMID) Project for the development of the corporate bond market in East Africa. The meeting will also review progress on the assessment of the 27 International Organisation of Securities Commissions (IOSCO) Principles and progress regional integration in view of the 2009 deadline. The Finance and Disclosure Sub Committee will also review the reporting requirements of Collective Investment Schemes, fund managers, trustees and custodians.

Capital Markets University Challenge

In our continued efforts to educate the public particularly the youth about capital markets; CMA will hold the 2nd Capital Markets University Challenge between August and October 2007. CMA will work with various universities in Uganda through an essay writing competition and a portfolio building contest to determine 3 winners. The grand prize is a visit to the South African capital markets industry.

Capital Markets in the Press Africa to Rival China in Growth New Vision Saturday June 30th 2007 By Peter Kaujuu and Sylvia Juuko

Africa is the region to look out for in the next few years due to its market potential and resources, a business leader has predicted. 'Much work remains to be done, but I am confident that Africa is on the way to becoming the next China or India', said Gerald Mahinda, the East African Breweries Group Managing Director.

Delivering a keynote address during the Kikonyogo Capital Markets Awards dinner at the Sheraton Kampala Hotel, Mahinda said the world was betting on Africa as the continent of the next century after Asia.

'But we need to constantly ask ourselves whether we are headed down the right path,' he challenged. Mahinda noted that investor confidence in the region was growing particularly from local investors. He attributed this to the population and consumer market growth and the urbanisation of most African countries. Mahinda disclosed that the regions' economies had also grown to US\$ 41 Billion in 2006 from US\$ 12.2 billion in 1980 while individual economies had averaged a 5-6% annual growth.

He, however, said the regional trade was hampered by lack of free movement of goods and people. 'Strengthening the economic potential of our region is important because our population is growing yet poverty and economic inequality are rising.' It is time to move forward with the East African Community harmonisation because the business community can't afford to wait any longer,' he argued. He warned of complacency as one of the dangers to successful business.

Mahinda encouraged companies to utilise capital markets to raise capital, expand operations, generate and develop innovative products. He cited his company as an example that had achieved the same. Through the stock exchange, the East African Breweries market capitalisation grew to US\$ 1.5 billion from US\$ 80 million. 'Our priorities are our brand, shareholders and our people. The capital markets is integral to our ability to advance each of these priorities. He explained.

Quote

"If we assume that it is the habit of the market to overvalue common stocks which have been showing excellent growth or are glamorous for some other reason, it is logical to expect that it will undervalue – relatively, at least – companies that are out of favor because of unsatisfactory developments of a temporary nature. This may be set down as a fundamental law of the stock market, and it suggests an investment approach that should be both conservative and promising."

**Benjamin Graham,
Value Investor**

Disclaimer

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As at 30th June 2007, the following were the broker/dealers, investment advisors and fund managers licensed and regulated by CMA. This list includes the trustees and custodians in the Ugandan market.

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