



# CMA

**Capital Markets Authority**  
Protecting Your Investments

## Quarterly Review

July - September 2007, Volume 8, Number 3

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### INTRODUCTION

This Electronic Quarterly Review Covers the period July - September 2007.

## Public Education

### Nakivubo Educational Drive

As part of its 10th year anniversary celebrations, the Capital Markets Authority (CMA) held a series of activities to highlight the industry achievements, as well as carry out public education, on capital markets issues.

The activities included a day-long public education exhibition on Friday 3rd August 2007 at the entrance to Nakivubo Stadium. Our main intention was to reach the average individual in down-town Kampala; the businessman, the student and the casual labourer, with the message of capital markets. The mobile cinema show at the exhibition also attracted scores of passers by who watched and identified with the soap opera that was projected onto a large screen in the evening.

Uganda Securities Exchange, African Alliance and MBEA Brokerage Services, participated in the exhibition which reached over 3,000 people on capital markets issues on a single day. As the industry grows, CMA would like capital markets to be the most comprehensible and accessible investment option to every individual, right from the secondary school

student in a classroom to the policy maker in an office, for the benefit of our growing economy.

### Rugby Game

CMA sponsored a 7 circuit rugby competition on 22nd and 23rd September 2007. Rugby has become a very popular support in the corporate sector as well as amongst university students. CMA's interest in the game is in the fact that it brings together the target groups that could invest in capital markets. Several games were played by various teams in Kampala and the finals played by the MTN Heathens and the Mango Kobs. The MTN Heathens emerged the winners.

### Capital Markets University Challenge

For the second year running, CMA will be holding the Annual Capital Markets University Challenge as a means of educating university students about capital markets. This years competition will invite 2nd year students of all disciplines from 25 universities all across Uganda to participate. The two stage competition involves an essay writing competition from which the best three universities will be selected

## Regulatory Issues

### Meeting with Licencees

The Capital Markets Authority (CMA) held a seminar for all its licensees on Friday 3rd August 2007. The seminar attracted 33 participants from the stock exchange, brokerage firms, investment advisory firms, fund management firms, and Collective Investment Schemes (CIS) operators. The seminar discussed various compliance and market development issues. It was resolved to have such a meeting on a quarterly basis.

## HIGHLIGHTS

- \* Regulatory Issues
- \* Market Development
- \* Public Education
- \* Regional and International Cooperation
- \* Home News
- \* Capital Markets in the Press

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to move on to the next stage which will involve the formation of investment clubs in their universities. The establishment of the investment clubs will be captured in a reality show and will be aired on national television at the end of the competition. The grand prize for the team that establishes the best investment club will be a study tour to South Africa. The Financial Services Board, the regulator of South Africa's financial services sector, has agreed to host the winning team.

## Regional and International Co-operation

### EASRA Meeting

The 24th EASRA meeting took place in Nairobi from 17th to 19th September 2007. As usual the consultative meeting of the Chief Executives was preceded by the meetings of the technical officials. The Market Development Sub Committee discussed the regional certification program that had been submitted and accepted for funding by the International Finance Corporation (IFC) Efficient Securities Markets Institutional Development (ESMID) Project. ESMID, whose officials were present at the meeting, reported that a consultant has been contracted to operationalise the regional certification program. The overall objective of the certification program is to enhance the proficiency and professional competency of market players in a manner that is sustainable and capable of enhancing investor protection and the professional standards in securities transactions in East Africa. ESMID also reported that a consultant had been engaged to conduct a study on the best suited model for capital markets integration in East Africa. Both consultancies will run concurrently starting October 2007.

The consultative meeting also agreed to conduct two seminars for the East African Legislative Assembly once Rwanda and Burundi have constituted their members and another for policy makers in the financial sector. The two seminars will be pertinent as we move towards regional integration in view of the need to harmonise our legislation and policies.

The Legal Committee prepared an application for funding for the 27 International Organization of Securities Commission (IOSCO) principles to FIRST Initiative. The sub committee considered that obtaining funding from FIRST Initiative for technical assistance would be an appropriate action as FIRST

## QUOTES

“People trade both for cognitive and emotional reasons. They trade because they think that have information when they have nothing but noise, and they trade because trading can bring the joy of pride. Trading brings pride when decisions turn out well, but it brings regret when decisions do not turn out well. Investors try to avoid the pain of regret by avoiding the realization of losses, employing investment advisors as scapegoats, and avoiding stocks of companies with low reputations”

*Meir Statman, Investor, Writer*

“Every great crisis reveals the excessive speculation of many houses which no one before suspected, and which commonly had not begun, or had not carried very far those speculations till they were tempted by daily rise of price and the surrounding fever’

*Walter Bagebot, 1826 – 1877, Writer, Lombard Street, 1873*

Initiative assisted EASRA in the self assessment exercise for the three core IOSCO principles on international cooperation and exchange of information. The three member states are at various stages of carrying out a review of their capital markets legislation, with a view to strengthening their legal and regulatory frameworks.

### IOSCO MMoU Application

At the 23rd Consultative meeting of EASRA, it was resolved that the members submit their respective application to become signatories to the IOSCO MMoU immediately. The three authorities prepared their respective applications in May and June of 2007. In July 2007, members of the Legal issues sub committee met in Kampala and conducted a peer review of their applications in accordance with the deliberations at the meeting and obtained approval for the submissions for their respective boards. All three authorities have now submitted their applications.

## Home News

### *Support to the Special Olympics*

CMA donated the official uniform t-shirts to the Uganda participants of the 12th world summer special Olympics games. Uganda was represented by 25 athletes who took part in the five sport disciplines of table tennis, swimming, power lifting, badminton and football. This kind gesture was a demonstration of our corporate social responsibility which goes beyond ensuring that we have a financially literate society. The Nnabagereka of Buganda Sylvia Nagginda is the patron of the Special Olympics in Uganda.

### *New Member of CMA family*

On 22nd September 2007, Ms Phoebe Kiconco, the Compliance Officer (Finance) wedded Mr. Michael Mugisa at a colourful occasion at the Kampala Pentecostal Church. CMA welcomes Mr Michael Mugisa to the CMA family and wishes the new couple a fruitful and fulfilling marriage.

## Outlook

### *University Challenge*

The annual capital markets university challenge which is currently underway will be concluded in the fourth quarter of 2007. Each investment club will be given a seed capital of US\$150,000/= and will be required to draw up an investment strategy for the realized and projected returns from the seed capital. Bonds, Shares or unit trusts must be part of the investment portfolio of the investment club. There will be a panel of judges who will choose the best investment club using the following criteria:

- i) Team work
- ii) Organizational Structure of the investment club
- iii) Strategy of the continuity of the Club beyond the founders
- iv) The investment strategy of the investment club

### *UMA International Trade Fair*

CMA will participate in the Annual Uganda Manufacturer's Association Trade Fair. The trade fair will draw exhibitors from East, West and Southern Africa. It's anticipated that it will attract scores of people especially in view of the upcoming of the Commonwealth Heads of Government Meeting. CMA will use the opportunity to talk to people in the Neighbourhood.

## CAPITAL MARKETS IN THE PRESS

### IPO FRENZY CALLS FOR BOOK BUILDING

*The Daily Monitor*

Tuesday, August 28th, 2007

**BY: PETER MUSHANGWE**

Kenya Re Initial Public Offer (IPO) results were the last nail in the coffin. The East African IPO's are either over-marketed (or under-valued) or too small for the market. It is depressing, for instance, after applying for an IPO with great enthusiasm, to find out that the shares you bought and were allotted are actually worthless.

It is equally depressing to apply for 20,000 shares, and you are allotted 2,000 shares. In both cases, an investor would suffer some loss; be it capital loss or opportunity cost. The loss may be magnified by the transaction costs and exchange rate risk in case of a cross-boarder investment.

Investment bankers will probably have to find a way to deal with this new problem in the IPO market in East Africa. It is critical to establish why the IPO's attain such levels of subscription. It could be either that the investment bankers hugely discount the share prices, or that the IPO's are too small for the markets. It could also be a result of increased participation particularly from retail investors which the markets have been experiencing since the KenGen IPO. Foreign investors are also beginning to seriously consider African markets as an important asset class. It is important however to note that the EA markets are still very basic.

Very few banks engage in script lending (lending on shares/bonds as securities) and no broker I know in Uganda provide margin accounts to clients. Underwriting of IPO's is also not a general thing in EA, and one would expect investors to carefully tread their grounds since no-one would be guaranteeing to take up the shares should there be an under-subscription.

I therefore wonder what will happen should banks and brokers decide to pump in liquidity to investors. The investment banker's effort to promote an IPO, particularly to retail and foreign investors should benefit both the issuer and the investment banker.

The issuer should benefit from having a broad-based shareholding structure (reducing shareholder risk) and investment banker should benefit by getting business from the investor. The continuation of crazy oversubscription levels from KenGen to SBU to Kenya Re, will ultimately lead to "passive resistance" from quality investors.

This of course will lead to a deterioration of the shareholder quality post listing. Probably the markets are ripe for book-building.

In book building, the book runner prices the issue and sets up a floor price. The issue is then marketed to both retail and institutional investors who will aid in the price and demand discovery. Though every book runner may be unique, generally, the Offer Price is determined after the bid closes, based on a certain evaluation, but for all we know; price aggression being the most important factor. Issuers will surely benefit (read: governments) from book building.

Investment bankers and brokers know they have done their job well when neither the issuer nor the investor is entirely happy with the valuation. Book building seems to hold both parties fairly. I usually prefer to quote this example: In 1995, Morgan Stanley took Nescape public. The initial floor price was \$14 for 3.5 million shares.

After scanning the market, they increased it to \$28 for 5 million shares. But due to huge unmet demand, the Nasdaq market-makers opened Nescape at \$75. (Nescape was later taken over by America Online). Surely under those circumstances, both the issuer and the investor are not entirely happy. The issuer sold shares for \$28, yet the market was prepared for \$75, while the investor got it for \$28 yet it was initially meant to be \$14.

If it is that our IPOs are too small for the investors, then probably issuers with the help of their investment bankers and consent from the regulatory authorities should be allowed to mop up extra funds on the table by issuing and allocating shares to the subscribers.

It would tend to water down the upside risk of the stock, but for a good company the value should be maintained since the funds will be employed in a profitable business and in furtherance of shareholder value maximization tenet.

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