

# THE DEVELOPMENT OF COLLECTIVE INVESTMENT SCHEMES IN UGANDA



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An Analysis of the Factors Affecting the Development of Unit Trusts in Uganda

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## ABBREVIATIONS & ACCROYNMS

CIS	Collective Investment Schemes
CMA	Capital Markets Authority
EAC	East African Community
MDIs	Micro-Deposit Taking Institutions
IOSCO	International Organization of Securities Commissions
SACCOs	Savings Credit and Co-operative Organizations

## EXECUTIVE SUMMARY

The Collective Investment Schemes (CIS) industry has been in existence in Uganda for six (6) years, the first and only Unit Trust Manager having started CIS operations in August 2004. In the last five (5) years the industry has grown from a Net Asset base of US\$ 523,779 at the end of 2005 to US\$ 1.97 million at the end of March 2010 a growth of 276%. Over the same period the CIS investment accounts has grown to 699 as at end of March 2010. However when compared to Ghana a market similar to Uganda, the CIS industry in Uganda lags way behind both in terms of net asset value and number of investors. In Ghana the CIS industry began operations in 2002 and within six (6) years the net asset value had grown to 123.61 million and the investor base to 128,067 investors which is way above what Uganda has been able to achieve over the same period.

An analysis of the factors that affect the demand and supply of CISs in Uganda identifies three major bottlenecks to the development of the CIS industry in Uganda;

- i) a poor culture of savings and investments,
- ii) a lack of an extensive and comprehensive marketing strategy and distribution network for CIS products
- iii) an underdeveloped capital market with a few investment opportunities for the CIS industry

The following strategies are recommended to enhance the performance and development of the CIS industry in Uganda;

- i) Enhancement of the current **public awareness programs on CIS products** in Uganda by the Unit Trust Manager and the Capital Markets Authority (CMA) as well as embarking on **financial capability programs** to empower the current and prospective investors to actually invest in CISs.
- ii) Enhancement of the accessibility and visibility of the CIS industry through innovative solutions like:
  - † **SMS Banking,**
  - † **E-transact solution** where investors can top up their CIS investment accounts using reloadable cards from the convenience of their homes, office or work place.
  - † **Strategic distribution alliances** with banks where clients can invest in CISs through the banks' branch networks and can even use their debit or credit cards to make their investments.
- iii) Promotion and facilitation of the integration of the capital markets in the East African region

## 1.0 BACKGROUND TO THE STUDY

### 1.1 Understanding Collective Investment Schemes

Collective Investment Schemes (CIS) refer to investment funds that pool together funds from a wide range of investors both retail and institutional to be invested in a number of different financial assets traded in the capital markets. Usually the CIS are managed by a regulated investment management firm which invests the pooled funds on behalf of the fund members (Sally et al, 2003, Profile Media, 2007). According to the International Organization of Securities Commissions (IOSCO) CIS is “an open ended collective investment scheme that issues redeemable units and invests primarily in transferable securities or money market instruments” (IOSCO, 1995). It excludes schemes investing in property/real estate, mortgages or venture capital. For purposes of this study the IOSCO definition of CIS shall take precedence.

#### 1.1.1 The History of Collective Investment Schemes

According to Rouwenhorst (2004) the history of CISs dates back to 1774 when a Dutch merchant and broker Abraham Van Ketwich invited subscriptions from investors to form a trust called “*Eendragt Maakt Magt*” translated as “Unity Creates Strength”. At the time of the formation of this CIS the Amsterdam stock exchange was already operating with more than one hundred (100) securities regularly traded which provided an investment avenue for the budding CIS. This CIS invested in bonds issued by foreign governments and banks as well as in plantation loans in the West Indies.

Much as at that time there were no classifications of CIS as we have today, the *Eendragt Maakt Magt* would be classified as a Closed-Ended Corporate CIS. A total of 2000 shares in this CIS were up for subscription which was open to the public. Once all the 2000 shares were placed, thereafter participation in the CIS would only be possible by purchasing shares from the existing shareholders in the secondary market.

In Africa CISs were first established in South Africa in 1965 and these CISs took the form of Trust CISs (Unit Trusts) that invested in tradable equities (Profile Media, 2007).

### 1.1.2 The Nature and Form of Collective Investment Schemes

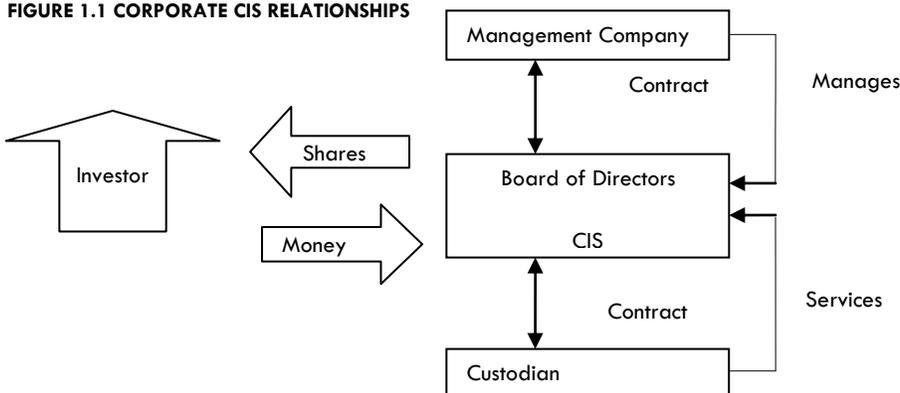
The nature and form of any CISs will be dependent on the legal, operational and management structures (Sally et al, 2003). Legally a CIS can take the form of a **company, trust, contractual pool or partnership**. Operationally it can either be an **open, interval** or **closed-ended** CIS and in terms of management structure the CIS can either be **internally** or **externally** managed. The structure any given CIS takes will vary from country to country depending on the legal and regulatory framework in a particular country (Sally et al, 2003).

#### 1.1.2.1 Legal Structures

##### 1.1.2.1.1 Corporate CISs

Unlike conventional companies that usually seek to make profits from producing goods and services; corporate CISs seek to give their shareholders good returns on their investments. The shareholders' funds are used to invest in other assets usually financial assets to generate a return for the shareholders. The directors of the company are essentially responsible for the funds and investments of the shareholders though they contract the services of a fund management company, a custodian and any other provider of services to the CIS. Corporate CISs are corporations in law and are taxable as such unless they are given special dispensations. Corporate CISs can also be operated under most legal systems though taxation treatments and inability to operate variable capital companies can restrict their development. This legal flexibility makes Corporate CISs by far the largest legal type of CISs in the world. The most common corporate CISs are the US open-ended investment companies usually referred to as "Mutual Funds".

FIGURE 1.1 CORPORATE CIS RELATIONSHIPS

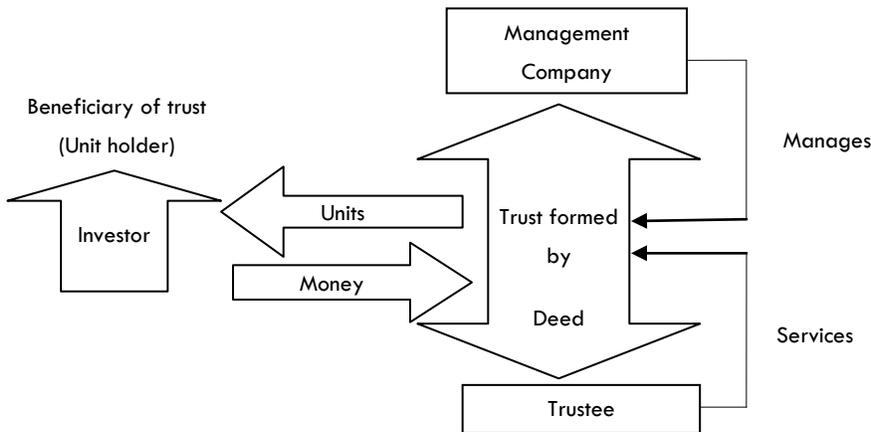


**1.1.2.1.2 Trust CISs**

Trust CISs are formed under trust law where a trust deed is the basis upon which the CIS operates. Such CISs are referred to as “Unit Trusts” and holdings in them known as “Units”. The units are created by a trust deed, to which the signatories are the management company and the trustee. Trusts are essentially an arrangement recognized by law under which one person (the trustee) holds property for the benefit of another (the beneficiary). As such, a trust is a legal person. Trust CISs are only found in countries with a common law system.

In a Trust CIS the trustee has supreme authority over the management company and can terminate its duties if it fails adequately to perform as required by the trust deed. Most Unit Trusts are open-ended CISs though theoretically there is no reason why interval or closed-ended unit trusts should be formed. Unlike shareholders in corporate CISs, the voting rights of unit holders in unit trusts are very limited. The unit trusts do not have annual general meetings; though they are required to call extraordinary general meetings to vote on specified issues such as an increase in fees or a change in investment objectives.

**FIGURE 1.2 UNIT TRUST FUND RELATIONSHIPS**

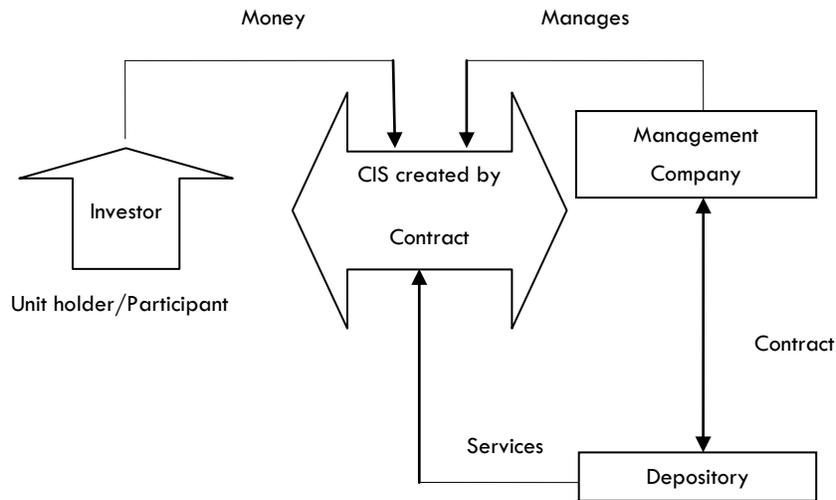


**1.1.2.1.3 Contractual CISs**

This form of CIS is based on a standardized contract between the investor and the fund management company whereby the management company contracts to provide management of the pool of assets collected according to the contract and the founding documents of the fund. However the management company is required to have a contract with a depository to provide custody and supervisory services in order for the CIS to be approved by the regulator. Investors in contractual CISs are referred to as Unit

Holders/Participants/Certificate Holders and their investments are denoted by units/participations/certificates in the CIS. The rights of investors in contractual CISs are limited to the terms set out in the contract establishing the CIS. It therefore becomes of critical importance for the investors to negotiate terms that will best meet their interests. Contractual CISs are found in countries which have a Civil Code based legal system and are common in Continental European countries and their former colonies.

FIGURE 1.3 CONTRACTUAL CIS RELATIONSHIPS



#### 1.1.2.1.4 Partnership CISs

This form of CIS is based on a partnership agreement where the management company is the general partner offering partnerships to a relatively small number of investors who become limited partners. Partnership CISs are designed to attract a few investors who are usually institutional or professional investors. Unlike the other three forms of CISs already discussed Partnership CISs are not permitted to be offered to the general public. Partnership CISs are commonly formed in offshore or low tax domiciles and are often used by so-called “hedge funds.” Partnership CISs can operate in both the common law and Civil Code countries since their operation is governed by the legislation governing other partnerships. Since they are restricted to a few sophisticated investors Partnership CISs do not fall under any securities legislation that covers public issues.

FIGURE 1.4 PARTNERSHIP CIS RELATIONSHIPS

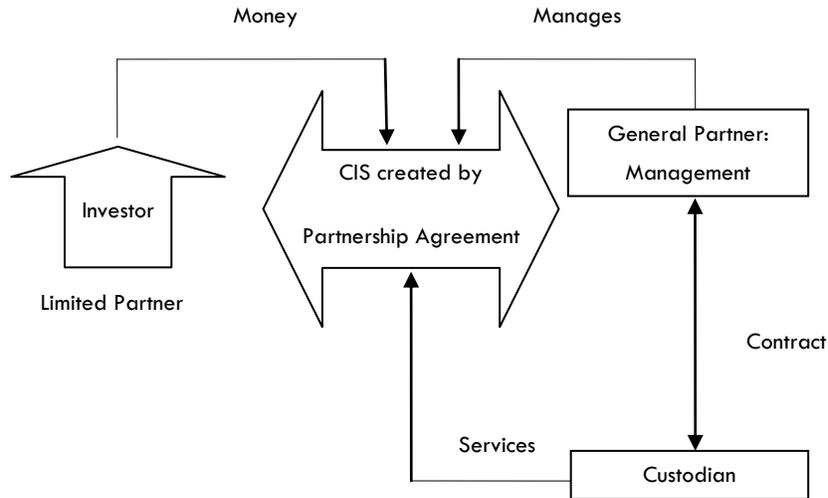


TABLE 1.1: SUMMARY OF THE IMPLICATIONS OF THE MAIN LEGAL STRUCTURES OF CIS

	Form of Collective Investment Scheme		
	Corporate	Trust	Contractual
<b>Legal Form</b>	Joint Stock Company (Corporation)	Trust	Not a legal entity: contractual pool
<b>Governing Law</b>	Company law or commercial code, CIS law	Trust law or precedent, CIS law	Law of contract or commercial code, CIS law
<b>Investors Buy</b>	Shares	Units	Units or Certificates of Participation
<b>Investor Status</b>	Shareholder	Beneficiary of trust (Unit holder)	Unit holder or Participant
<b>Voting Rights of Holders</b>	As per ordinary shareholder plus those set by the CIS law and regulation	As per trust deed plus those set by the CIS law and regulation	None or those set by the CIS law and regulation
<b>Meetings of Holders</b>	Annual & Extraordinary	Extraordinary only	None or Extraordinary only
<b>Fiduciary Duty to Investors</b>	CIS directors	Trustee	None unless specified in the CIS law or contract with investors
<b>Holder of CIS Assets</b>	Custodian	Trustee or Custodian on behalf of the Trustee	Depository
<b>Assets Registered in the names of</b>	CIS or Custodian on behalf of the CIS	Trustee or Custodian on behalf of the Trustee	Management Company or Depository on behalf of the CIS
<b>Founding Documents</b>	Memorandum and Articles of Association or equivalent e.g. Charter	Trust Deed	Contract and rules of CIS

Source: (Sally et al, 2003)

## 1.1.2.2 Operational Structures

### 1.1.2.2.1 Open Ended CISs

In an open ended CIS there is no limit to the number of units or shares that can be issued and the investors have the freedom to exit the CIS at any point in time. This means that the management company has to be in position to redeem the units or shares as and when investors wish to exit the CIS which is usually engrained in the CIS law. Dependent on the CIS law in a particular jurisdiction Open Ended CISs can be formed in Corporate, Trust or Contractual form. However Corporate Open Ended CISs can be difficult to operate in countries where company law does not recognize the concept of a company with variable capital as would be the case with Open Ended CISs. In most cases company laws provide for ordinary companies that like Closed Ended CISs have fixed capital. Thus an amendment of the existing company laws to cater for companies with variable capital may be required in some jurisdictions before Open Ended CISs become operational.

Open Ended CISs account for the largest percentage of CISs in the world largely because of the easy entry and exit accorded to investors in such CISs. However for such CISs to operate effectively the market needs to be very liquid to allow for an active market of units or shares which is critical if the management company is to meet purchase and redemption orders. This also means that the Open Ended CIS assets are usually liquid to ensure that they can easily be sold to raise capital to redeem units or shares of exiting members.

### 1.1.2.2.2 Closed Ended CISs

Closed Ended CISs like ordinary companies have fixed capital (*number of shares or units*) in issue. Such CISs can also operate in any CIS form whether corporate, trust or contractual, though the corporate form is the most common given the similarities Closed Ended CISs have with companies.

Unlike Open Ended CISs, Closed Ended CISs cannot issue shares or units at any given time. They usually have an initial period of raising capital through issuance of shares or units which is for a limited time after which no further subscriptions are permitted. Further subscriptions can only be permitted if the existing members agree to increase the share capital as is the case with ordinary companies. Therefore in such a case the management company is not obliged to redeem the shares or units of members who wish to exit the CIS as is the case with Open Ended CISs. This essentially means that the management company is not

limited to investing in only liquid assets but also in illiquid assets since their asset base is more stable not affected by frequent redemption requests. The stability of their asset base also gives room for Closed Ended CISs to borrow or “gear” or “leverage” to embark on bigger investments.

### 1.1.2.2.3 “Interval” CISs

Interval CISs are a hybrid of Closed Ended and Open Ended CISs since they have features of both CIS operational structures. They are sometimes referred to as “limited” or “closen” Funds. Such CISs are essentially Closed Ended CISs but an allowance is made for occasional regular sale or redemption of shares or units at least once a year.

TABLE 1.2: SUMMARY OF THE IMPLICATIONS OF THE MAIN OPERATIONAL STRUCTURES OF CIS

	Form of Collective Investment Scheme		
	Open-Ended	Interval	Closed-Ended
<b>Capital</b>	Variable	Fixed temporarily, varying when open	Fixed
<b>Duration</b>	Usually indefinite	Indefinite or Finite life	Indefinite or Finite life
<b>Investments</b>	90% liquid	Illiquid or Liquid	Illiquid or Liquid
<b>Borrowing</b>	Limited (10% of Fund)	May be limited	Often unlimited
<b>Share (or unit) classes</b>	Must not disadvantage other shareholders	Must not disadvantage other shareholders	May have varying rights to income and capital
<b>Listing on Stock Exchange</b>	Not required	Not required	Usually required
<b>Pricing</b>	At net asset value	At net asset value	At market price
<b>Dealing Frequency</b>	Daily	Intervals	As per listing
<b>Transactions</b>	Through fund management company or sometimes on stock market	Through fund management company or sometimes on stock market	On stock market
<b>Managed</b>	Externally	Externally	Internally or Externally

Source: (Sally et al, 2003)

### 1.1.2.3 Management Structures

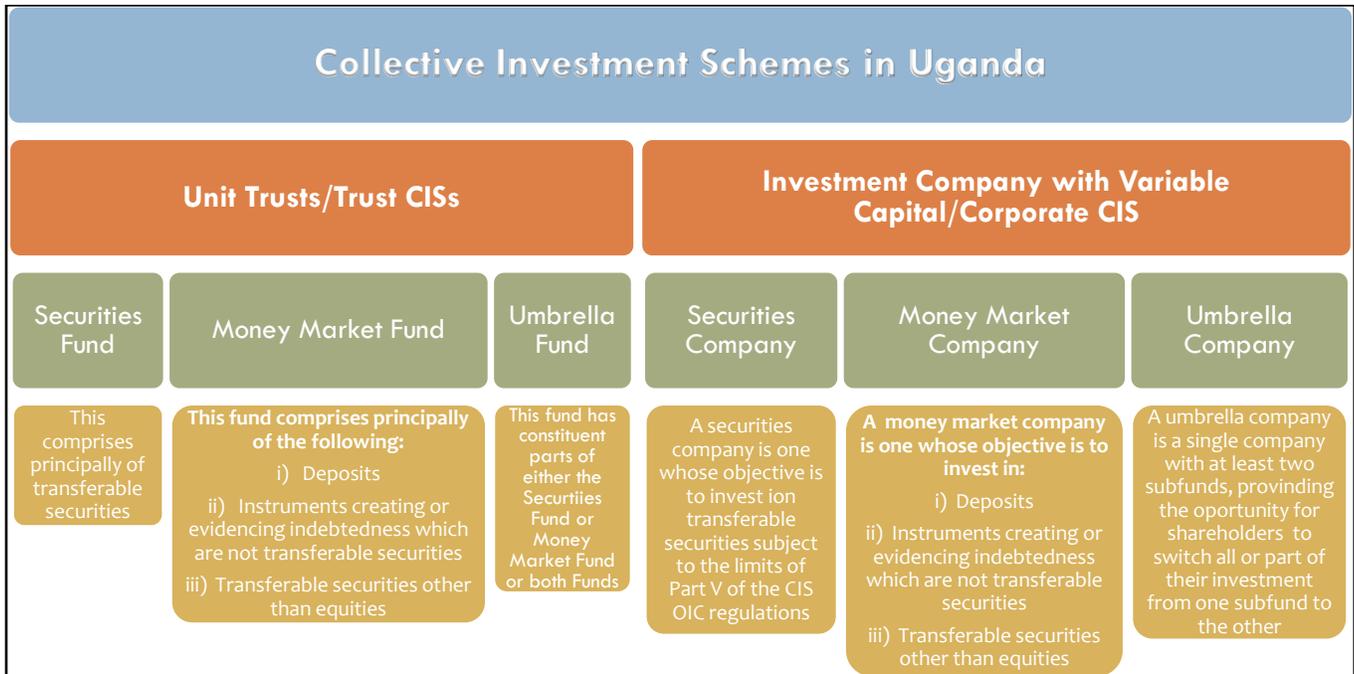
There are basically two forms of management structures for CISs; internal management and external management. In the internal management structure the CIS takes the full responsibility of all administration and fund management responsibilities where it for instance owns or rents its own offices, employs its staff, buys its equipment e.tc.

On the other hand in the external management structure a separate company from the CIS fund is contracted to manage the fund which usually includes both the administration and fund management responsibilities. In this case the CIS fund has no employees or office space which is all catered for by the management company.

## 1.2 Collective Investment Schemes in Uganda

In Uganda collective investment schemes were established under the Collective Investment Schemes Act 2003 which came into force in 2003. The CIS Act only makes provisions for open ended CISs which can take the form of a Unit Trust (Trust CIS) or an Investment company with variable capital (Corporate CIS). Figure 1.5 shows the different types of Unit Trusts and Corporate CISs permitted in the Ugandan market.

FIGURE 1.5 DIFFERENT TYPES OF COLLECTIVE INVESTMENTS SCHEMES PERMITTED IN UGANDA



Source: Capital Markets Authority-Uganda (2003a, 2003b)

Despite having provision of two forms of CISs in Uganda, only one management company is licensed so far to operate a Unit Trust and only two other companies have expressed interest in a Unit Trust license. One other interesting observation about the Ugandan CIS industry is the apparent interest in only the Unit Trust license yet there is also a possibility of acquiring a Corporate CIS license. This happens to also be the case in Kenya and Tanzania. However in Ghana a market similar to the East African markets the CIS industry has taken advantage of the two types of CISs; the Trust CIS and the Corporate CIS. At the end of 2008 with seven (7) Corporate CISs and Trust four (4) CISs operating in the Ghanaian CIS industry.

### 1.2.1 Policy Incentives

In the 2005/2006 fiscal year the Minister of Finance, Planning and Economic Development granted a withholding tax exemption to CISs licensed and operating in Uganda. However the exemption from withholding tax is to the extent of which the CIS income is distributed to participants in the Collective Investment Scheme.

### 1.2.2 Performance and Growth of Collective Investment Schemes in Uganda

#### 1.2.2.1 Industry Performance

The first and the only operational CIS began operations in 2004 as a Trust CIS with three funds which it still manages today. As at end of March 2010 the size of the CIS industry stood at US\$ 1.97 million. A look at other markets reveals that the CIS industry in Uganda is still very small even within the East African Community (EAC) (See table 1.3).

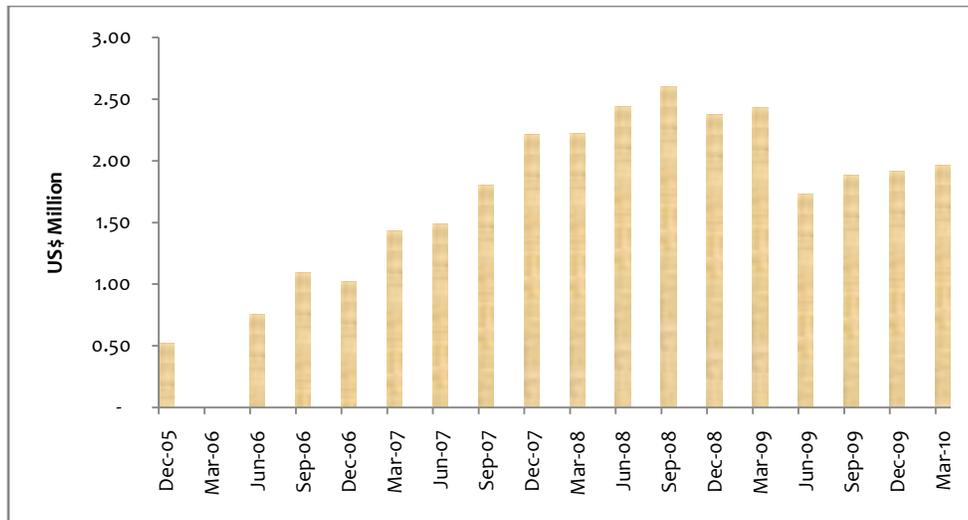
TABLE 1.3: A CROSS REGIONAL & COUNTRY COMPARISON OF THE SIZE OF COLLECTIVE INVESTMENT SCHEMES-2008

	Net Asset Value (US\$ Mn)	Number of Funds
World	18,974,521	69,032
Americas	10,579,430	16,459
Europe	6,288,138	36,780
Asia and Pacific	2,037,536	14,909
Africa	69,651.84	902
United States	9,601,090	8,022
United Kingdom	526,957	2,371
India	62,805	551
Republic of South Korea	221,992	9,384
South Africa	69,417	884
Kenya	150	8
Tanzania	61.59	4
Uganda	2.39	3

Source: 2009 Investment Company Fact Book, Capital Markets Authority-Uganda, Capital Markets Authority-Uganda, Capital Markets Securities Authority-Tanzania

In the five (5) years of its operations the size of the CIS industry has grown from US\$ 523,779 at the end of 2005 to US\$ 1.97 Million at the end of March 2010 reaching a peak of US\$ 2.6 Million at the end of September 2008 (see figure 1.6).

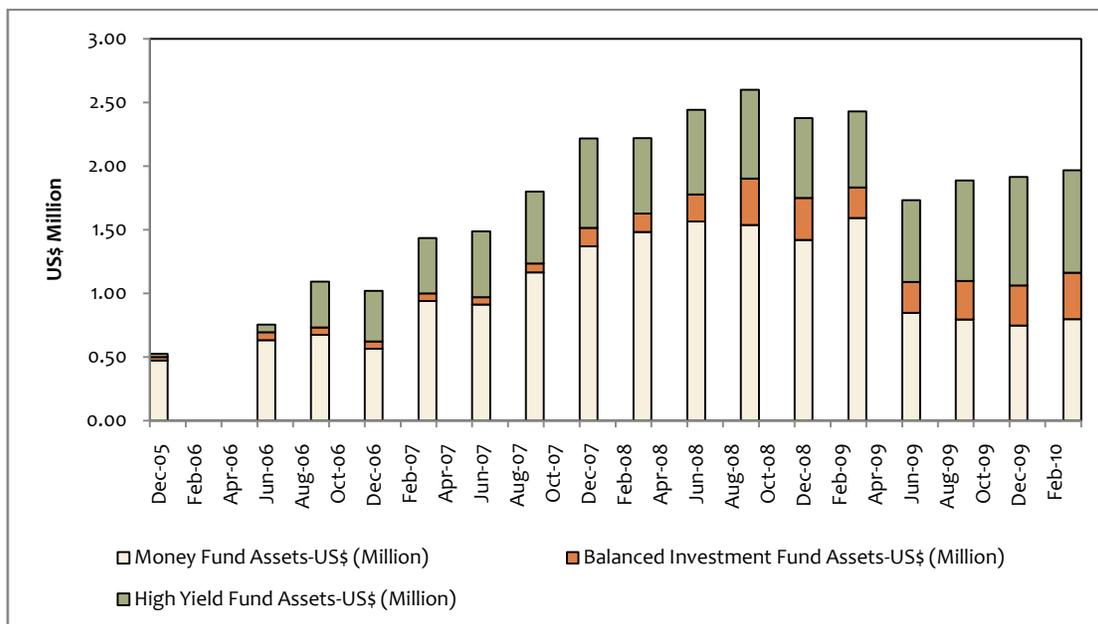
FIGURE 1.6: TRENDS IN THE SIZE OF THE CIS INDUSTRY IN UGANDA (US\$ MILLION) JULY 2006- MARCH 2010



Source: Capital Markets Authority-Uganda

The decrease in size of the CIS industry in the later part of 2008 up to date is as a result of a decrease in the size of the Money Fund which accounts for the biggest percentage of funds managed in Uganda’s CIS industry (see figure 1.7).

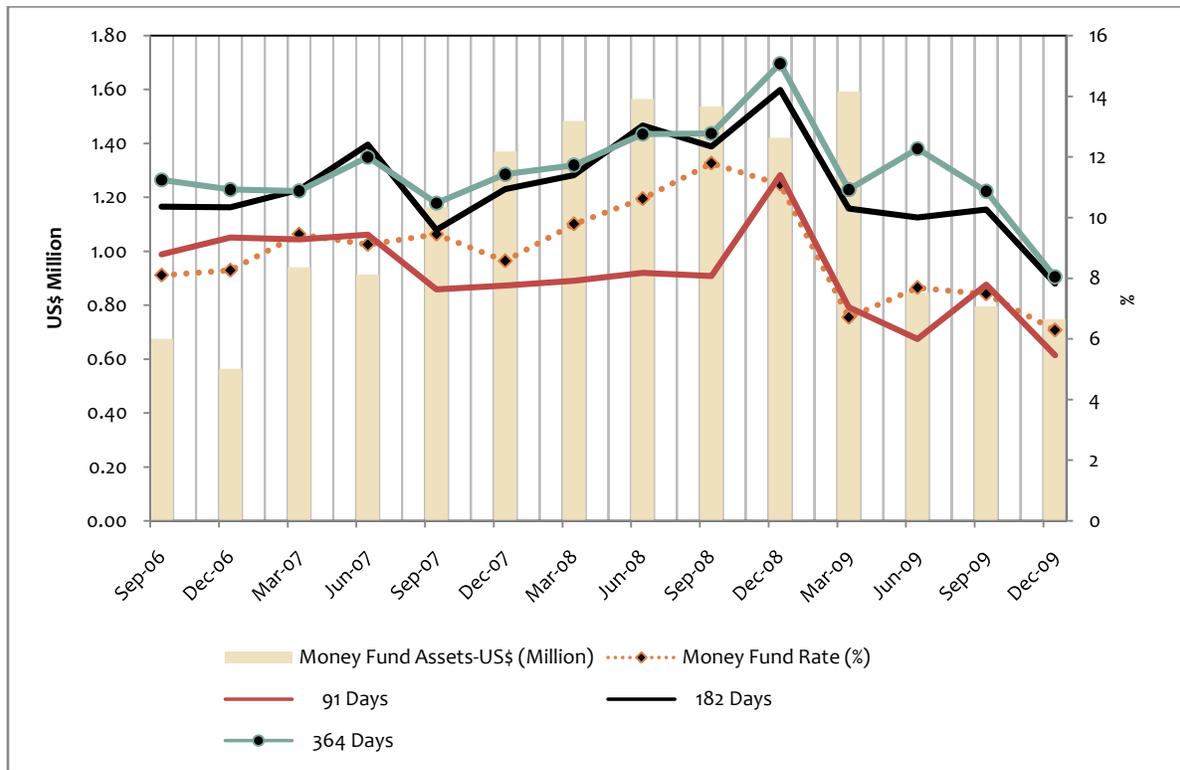
FIGURE 1.7: COMPOSITION OF THE CIS INDUSTRY IN UGANDA (JULY 2006-MARCH 2010)



Source: Capital Markets Authority-Uganda

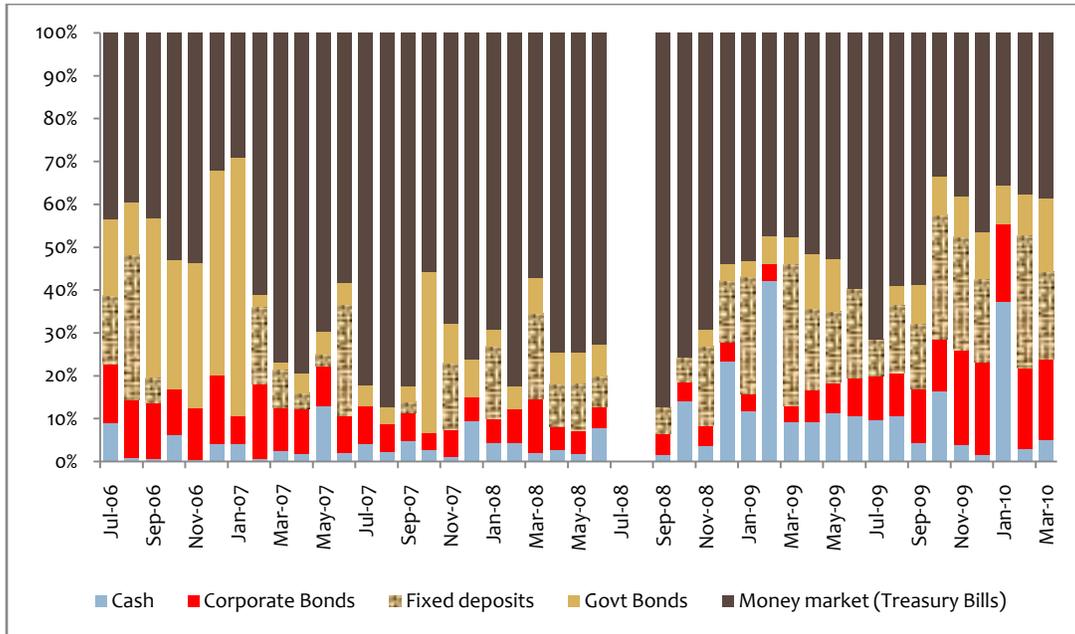
The decrease in the size of the Money fund is on account of the declining trend in the rates of return on the 91-Day, 182-Day and 364-Day treasury bills in the later part of 2008 to date (see figure 1.8). The treasury bills which are traded in the money market account for over 60% of the Money Fund portfolio (see figure 1.9) and thus any slight fall in Treasury bill rates would have a substantial effect on the Money Fund Rate which in turn is likely to affect the subscriptions to the Money Fund. As a result of the falling rates of return of treasury bills in the money market, the treasury bill portfolio has substantially decreased especially beginning from the last quarter of 2009 to date from over 60% to the current 38.6%.

FIGURE 1.8: TRENDS IN MONEY FUND ASSETS, MONEY FUND RATE AND TREASURY BILL RATES (JULY 2006-MARCH 2010)



Source: Capital Markets Authority-Uganda

FIGURE 1.9: TRENDS IN THE MONEY FUND PORTFOLIO COMPOSITION (JULY 2006-MARCH 2010)



Source: Capital Markets Authority-Uganda

### 1.2.2.2 Investor Participation in the CIS Industry

Since the establishment of CISs in August 2004 the number of CIS investor accounts stood at 699 investor accounts<sup>1</sup> as at end of March 2010. The retail investors account for 89% of these CIS investor accounts compared to 11% held by institutional investors (see table 1.4). However this investor participation compares very miserably with that of Ghana which stood at 128,067 at the end of December 2008 (Securities and Exchange Commission Ghana, 2008). Ghana is a low-income economy like Uganda and shares many economic similarities with Uganda and yet within six (6) years of CIS operations the number of CISs had grown from three (3) to eleven (11) and the number of investors had also grown from 7,995 to 128,067 (Securities and Exchange Commission Ghana, 2008). Over the same period Uganda could only master 3 CISs and a paltry 699 CIS investor accounts.

<sup>1</sup> Much as investor accounts are synonymous with the number of investors, this may not be the case in Uganda because some investors hold accounts in all the currently operational CISs. Thus the actual number of investors in Uganda's CIS industry is actually less than 699.

TABLE 1.4: A BREAKDOWN OF CIS INVESTMENT ACCOUNTS AND VALUE OF INVESTMENT (USHS MILLION) - (AS AT END OF MARCH 2010)

	Balanced Investment Fund		High Yield Fund		Money Fund		Total No. of CIS Accounts	Total Funds Invested (Ushs Million)
	No. of CIS Accounts	Funds Invested (Ushs Million)	No. of CIS Accounts	Funds Invested (Ushs Million)	No. of CIS Accounts	Funds Invested (Ushs Million)		
<b>Institutional Accounts</b>	18	477.4	27	1,178.8	33	1,165.5	78	2,821.8
<b>Retail Accounts</b>	174	278.9	207	497.0	240	509.3	621	1,285.2
<b>Total</b>	<b>192</b>	<b>756.4</b>	<b>234</b>	<b>1,675.8</b>	<b>273</b>	<b>1,674.8</b>	<b>699</b>	<b>4,107.0</b>

Source: CMA Research & Market Development Department

A further analysis from table 1.4 shows that institutional investors fair better than retail investors when it comes to the value of funds invested in the CIS industry. At the end of March 2010 institutional investors accounted for 69% of the total funds invested in the CIS industry with the retail investors accounting for the remaining 31%. The Money Fund accounted for 39% of the total CIS accounts followed by the High Yield Fund with 33% of the accounts and lastly the Balanced Investment Fund with 27% of the total CIS accounts. Table 1.4 further shows that the value of institutional investments in the CIS industry far exceeds that of retail investors by 40% in both the High Yield and Money Funds.

The popularity of the High Yield and Money Funds could be explained by two major factors; first these two funds mainly invest in treasury bills which are majority of institutional investors and some retail investors are more familiar with than shares which make up a big percentage of the Balanced Investment Fund.

Secondly the Money Fund is very similar to a typical fixed deposit account which both retail and institutional investors are already very familiar with. Thus it becomes very easy for these investors to substitute their investments in fixed deposit accounts to the Money Fund because these two products operate on basically the same terms. However it is easier to withdraw money in the case of the Money Fund than is the case if ones' investment was on a fixed account.

## 2.0 ANALYSIS OF THE FACTORS AFFECTING THE DEVELOPMENT OF CIS IN UGANDA

### 2.1 Analytical Framework for the Development of Collective Investment Schemes

FIGURE 2.1: ANALYTICAL FRAMEWORK FOR THE DEVELOPMENT OF COLLECTIVE INVESTMENT SCHEMES



The factors that could affect the development of CISs in Uganda can be classified into two categories; Demand Side and Supply Side factors as shown in figure 2.1.

## 2.2 Demand Side Factors

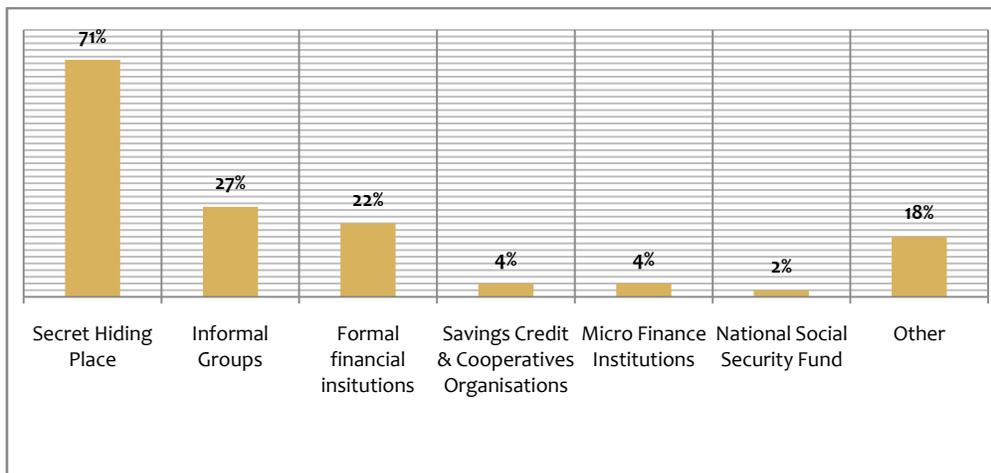
### 2.2.1 Savings and Investment Culture

The savings and investment culture of any market will greatly affect the level of demand for financial services and products and in this particular case the demand for CISs. Where there is a deeper culture of savings and investment especially formal savings and investment one will find higher levels of demand for financial services and products like CISs. Uganda one of the markets with the least developed CIS industries (refer to Table 1.3) also exhibits a very shallow culture of formal saving and investments.

#### 2.2.1.1 Savings Culture

Much as over 70% of adult<sup>2</sup> Ugandans currently save, seven (7) out ten (10) of these Ugandans either save in a secret hiding place outside the formal and semi-formal financial system (The Steadman Group, 2007)-(see figure 2.2). When this figure is extrapolated to the national population above 18 years it comes to five (5) five million Ugandans out of approximately seven (7) million adult Ugandans who are outside the formal and semi-formal financial system(The Steadman Group, 2007)-(see table 2.1).

FIGURE 2.2: WHERE UGANDANS SAVE<sup>3</sup>



Source: The Steadman Group, 2007

<sup>2</sup> Adult refers to a person who is 18 years and older

<sup>3</sup> The figures do not add up to 100% because there some who save both in the informal and formal financial systems

**TABLE 2.1: WHERE UGANDANS SAVE BY LOCATION & GENDER<sup>4</sup>**

	Rural	Urban	Male	Female
<b>Base = All those currently saving</b>	<b>1,456</b>	<b>678</b>	<b>1,062</b>	<b>1,072</b>
<b>Weighted Base +18yrs</b>	<b>6,808,853</b>	<b>2,512,121</b>	<b>4,617,117</b>	<b>4,703,857</b>
Secret Place (%)	74	60	68	73
Informal Groups (%)	29	24	26	29
Formal financial institutions (%)	17	36	27	17
Savings, Credit & Cooperatives Organizations (%)	4	3	5	3
Micro Finance Institutions (%)	4	2	3	4
National Social Security Fund (%)	2	1	2	1
Other (%)	18	18	18	19

Source: The Steadman Group, 2007

Ideally the primary purpose for saving should be investing the funds saved in assets that would yield an acceptable rate of return, however this is not the case in Uganda where a majority of Ugandans save to meet their day to day household needs and to cater for unforeseen emergencies like sickness and death (The Steadman Group, 2007)-(see table 2.2). No wonder saving in order to invest in financial products like CISs hardly features in the reasons why Ugandans save.

**TABLE 2.2: THE REASONS WHY UGANDANS SAVE BY LOCATION & GENDER**

No. of respondents	Currently saving	Currently saving			
		Rural	Urban	Male	Female
<b>Sample</b>	<b>2,174</b>	<b>1,483</b>	<b>691</b>	<b>1,081</b>	<b>1,093</b>
<b>Weighted Base +18yrs</b>	<b>9,137,725</b>	<b>6,808,853</b>	<b>2,512,121</b>	<b>4,617,117</b>	<b>4,703,857</b>
For meeting household needs (%)	82	83	78	81	83
For emergency (burial, medical) - (%)	70	73	63	70	70
For education of yourself, children or siblings or others (%)	35	34	35	34	35
For expanding your business (%)	19	18	21	20	17
To be able to leave something for my children (%)	12	11	13	13	11
For starting up a new business (%)	11	9	15	11	11
For using later in life/old age (%)	10	9	12	13	7
For purchase of livestock /cattle (%)	9	10	6	11	7
For social reasons (wedding, travel, bride price) - (%)	8	8	9	9	8
For purchasing or building a house to rent out (%)	6	5	9	8	4
For agricultural improvements e.g. irrigation, a dam, fencing, preparing land (%)	4	5	1	5	3
For agricultural implements û plough, hoe, tractor, things to use on the farm (%)	4	5	1	5	2
For fishing equipment boat, nets, engine (%)	2	3	2	3	2

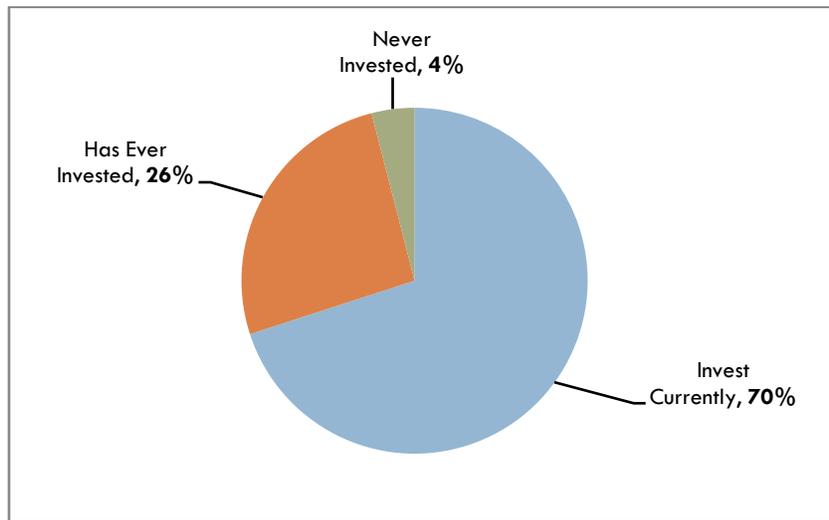
Source: The Steadman Group, 2007

<sup>4</sup> The figures do not add up to 100% because there some who save both in the informal and formal financial systems

### 2.2.1.2 Investment Culture

There is relatively a higher incidence of investment with 70% of adult Ugandans indicating that they are currently investing and less than 5% having never invested at all (The Steadman Group, 2007)-(see figure 2.3 and table 2.3). However a majority of Ugandans currently investing are more familiar and active in agricultural and trade/business related investments as well as banking accounts other than the alternative forms of financial investments like capital markets (in this case CISs) (The Steadman Group, 2007)-(see table 2.4).

FIGURE 2.3: INCIDENCE OF INVESTING AMONG ADULT UGANDANS



Source: The Steadman Group, 2007

TABLE 2.3: INCIDENCE OF INVESTING AMONG ADULT UGANDANS BY LOCATION & GENDER

No. of respondents	Rural	Urban	Male	Female
Sample	2,101	858	1,417	1,542
Weighted Base +18yrs	9,897,817	3,276,104	6,231,148	6,942,772
Invest Currently (%)	72	65	73	68
Has Ever Invested (%)	25	31	24	28
Never Invested (%)	3	4	3	4

Source: The Steadman Group, 2007

TABLE 2.4: MOST COMMON INVESTMENT OPTIONS AVAILABLE TO UGANDANS BY LOCATION & GENDER

No. of respondents	Total	Rural	Urban	Male	Female
Sample	2,959	2,101	858	1,417	1,542
Weighted Base +18yrs	13,173,921	9,897,817	3,276,104	6,231,148	6,942,772
Investment in livestock e.g. cattle (%)	68	70	62	69	66
Existing personal business (%)	64	62	67	62	65
Investment in farm land (%)	61	66	46	64	59
A house/flat/or additional rooms/property that I can rent out (%)	48	46	55	50	47
Starting a new business (%)	48	47	53	49	48
Account in a financial institution (%)	46	42	59	49	43
Investment through an informal group (%)	46	44	50	47	44
Money lending for profit/interest (%)	20	19	24	22	19

Source: The Steadman Group, 2007

There are three major hindrances to investing in financial products identified by a majority of adult Ugandans (The Steadman Group, 2007)-(see table 2.5);

- i) Lack of knowledge about the available investment options,
- ii) Fear of risks associated with investment
- iii) A lack of sufficient funds/savings to investment.

Much as these hindrances apply to mainly banking and informal financial products they would equally apply to CISs because CIS products are not any different from these financial products. In any case since they are fairly new in Uganda one may consider them more risky since they will not be very familiar with how they operate. However as Ugandans become more familiar with CISs they will appreciate that CIS products are in fact less risky since the risks is spread out across the pool of investors in the CIS and as a result this is likely to increase the appeal and demand for CISs among the Ugandan investing public.

TABLE 4: REASONS FOR NOT INVESTING

	Investment Options							
	Account in a financial Institution	Investment through an informal group in a financial Institution	A house/flat/ or additional rooms/property that I can rent out	Farm Land	Live stock e.g. Cattle	Existing personal business	Starting a new business	Money lending for profit/interest
<b>Weighted Base +18yrs</b>	<b>4,430,475</b>	<b>4,437,226</b>	<b>5,080,838</b>	<b>3,786,459</b>	<b>5,440,727</b>	<b>4,993,278</b>	<b>5,366,962</b>	<b>2,304,049</b>
Too risky - can lose money (%)	14	22	7	8	13	11	15	34
Don't know how to go about it (%)	16	12	6	7	7	8	7	9
Requires a lot of time/commitment (%)	7	14	7	17	15	9	8	5
Has low returns, poor profits (%)	7	8	5	6	5	6	4	5
Has too much tax (%)	3	2	3	3	3	6	5	3
Requires a lot of money to set up or start (%)	16	17	34	25	28	32	32	24
Too many people do the same, high competition (%)	1	3	3	3	4	7	8	4
Don't have what is needed to do it - e.g. no land to build etc (%)	4	8	25	19	12	7	7	6
Don't have money to invest (%)	36	36	43	36	38	35	44	44

Source: The Steadman Group, 2007

### 2.2.2 Competition from Other Financial Intermediaries

Competition from other financial intermediaries is the other factor that would affect the demand for CISs in Uganda. The financial intermediaries likely to pose the most competition threat to CISs in Uganda are commercial banks, Micro-Deposit Taking Institutions (MDIs), Micro-Finance Institutions (MFIs) and other Informal financial institutions like Savings, Credit and Cooperative Organizations (SAACOs). The areas where these types of intermediaries do have a competitive edge over CISs are:

#### 2.2.2.1 Accessibility

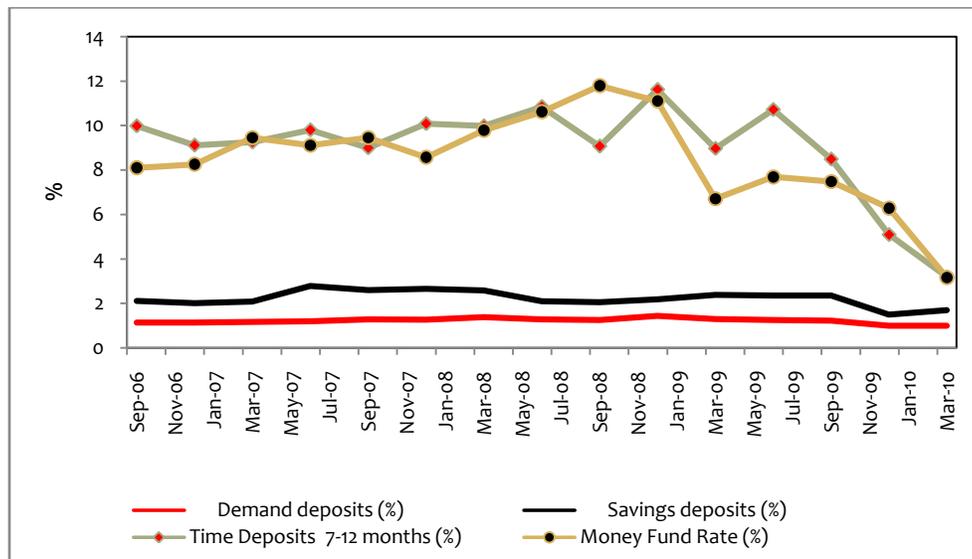
The above mentioned categories of financial intermediaries have an edge over the CIS industry in Uganda terms of accessibility through their wider branch and distribution networks. There is only one Unit Trust Manager licensed to manage, market and sale CIS products in Uganda and this Unit Trust Manager

has only one branch/outlet based in capital city, Kampala. Therefore if one is not based in Kampala it may be very difficult to access CIS products where as for the commercial banks and other formal financial intermediaries like MDIs one can easily access their financial products through their country wide branch networks and or Automated Teller Machines (ATM). Some commercial banks have also introduced E-Banking where one can access their account via the internet from any part of the country where there is an internet connection. The informal financial intermediaries like SACCOs are even more accessible than CISs in Uganda because they are established within the community and by members of the community.

### 2.2.2.2 Rate of Returns

The banking industry offers fairly competitive rates of return than the CIS industry especially with regard to rates of return on fixed deposits that mature in a period of 7-12 months. The Money Fund managed by the only Unit Trust Manager in Uganda over the last four years has offered an average annualized quarterly return of 8.5% compared to an average of 9% offered by the banking industry on fixed deposits over the same period. However the quarterly trends over the last four years shows that the money fund and the fixed deposit rates have more or less followed the same trend (see figure 2.4).

FIGURE 2.4: TRENDS IN THE RATE OF RETURN (%) ON SELECTED PRODUCTS IN THE BANKING & CIS INDUSTRY IN UGANDA



Source: Bank of Uganda Monthly and Economic Financial Reports and CMA Research & Market Development Department

### 2.2.2.3 Affordability

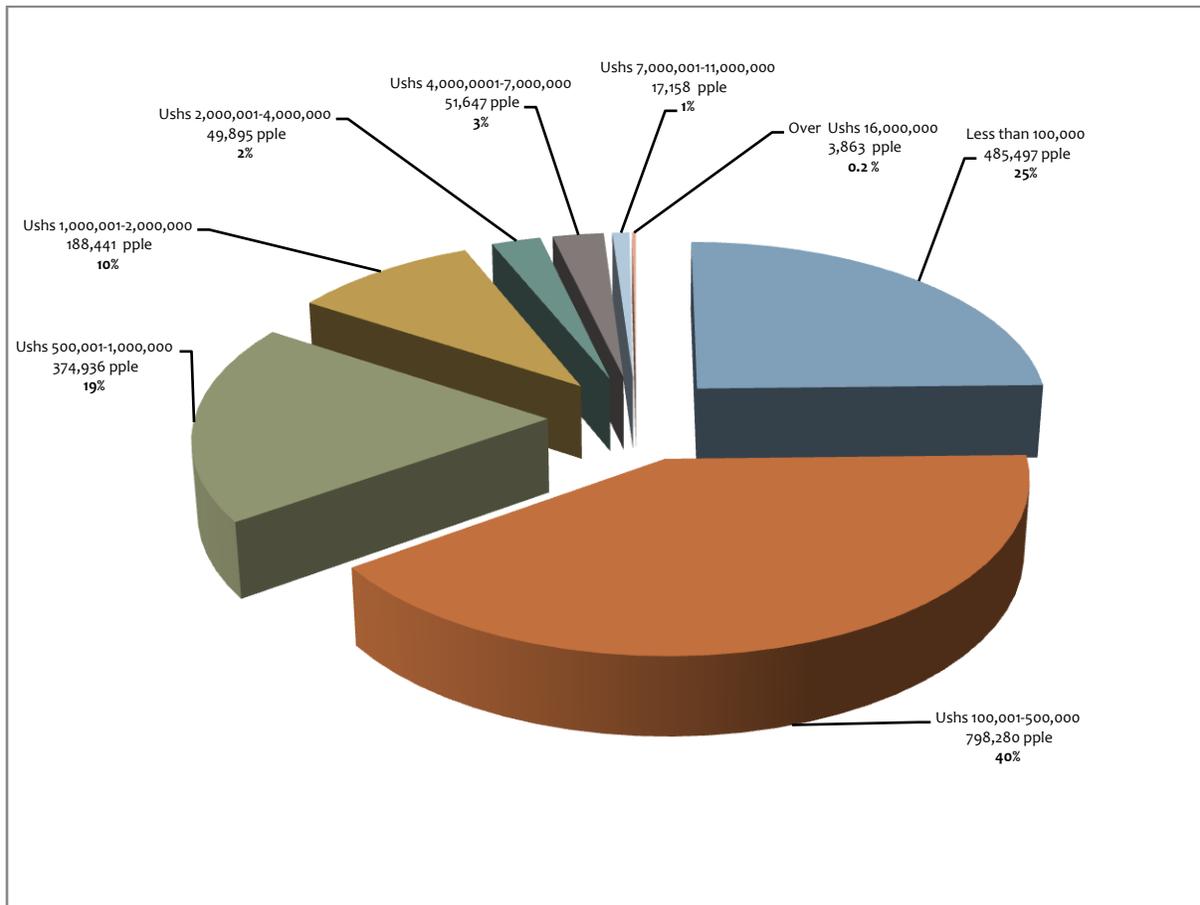
In terms of affordability the CIS industry in Uganda has a competitive edge over the other financial intermediaries (especially the commercial banks and MDIs) in comparative financial products. This is in

reference with the fixed deposit product which is comparable to the CIS products offered in Uganda. One just needs a minimum of Ushs 250,000 (US\$125) to invest in the Money Fund which has been earning an average annualized quarterly return of 8.5% compared to Ushs 1 million one needs to earn a similar rate of return on a fixed deposit in most commercial banks in Uganda.

### 2.2.3 Levels of Savings

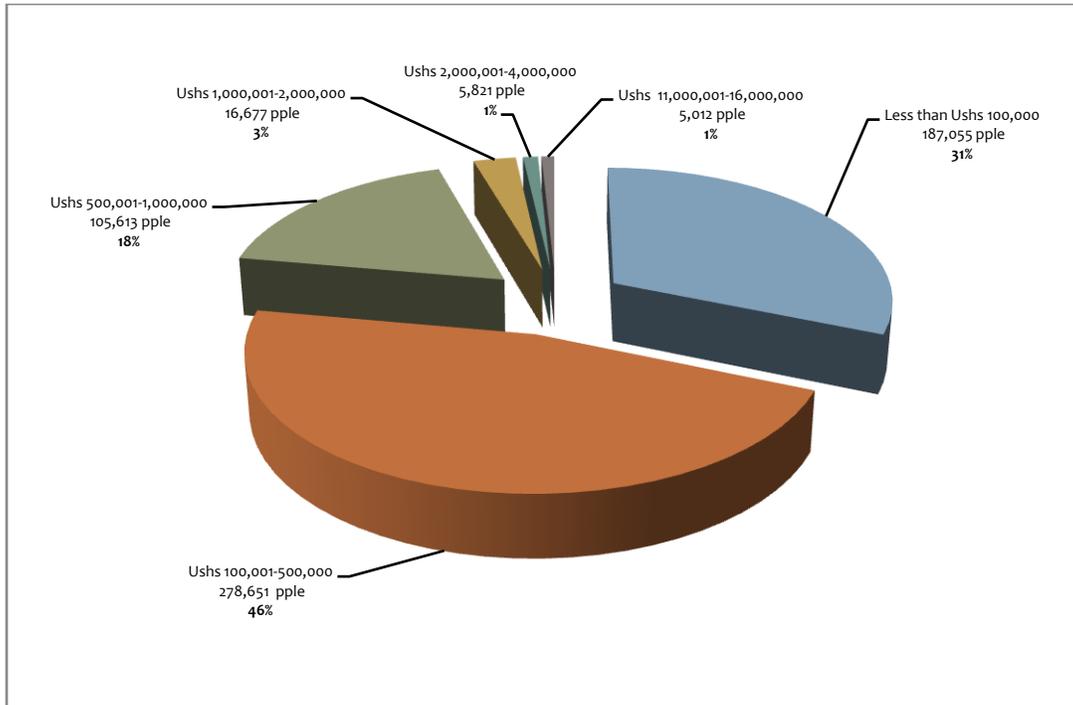
The levels of savings are very critical to the demand for CISs in Uganda because they provide the pool of money from which one can invest in financial products offered by the CIS industry. There is a huge potential demand for CIS products if one is to go by the amount of savings accumulated through the various channels of saving (see figures 2.5-2.9).

**FIGURE 2.5: NUMBER OF UGANDANS WHO HAVE SAVED VARIOUS AMOUNTS MONEY IN FORMAL FINANCIAL INSTITUTIONS**



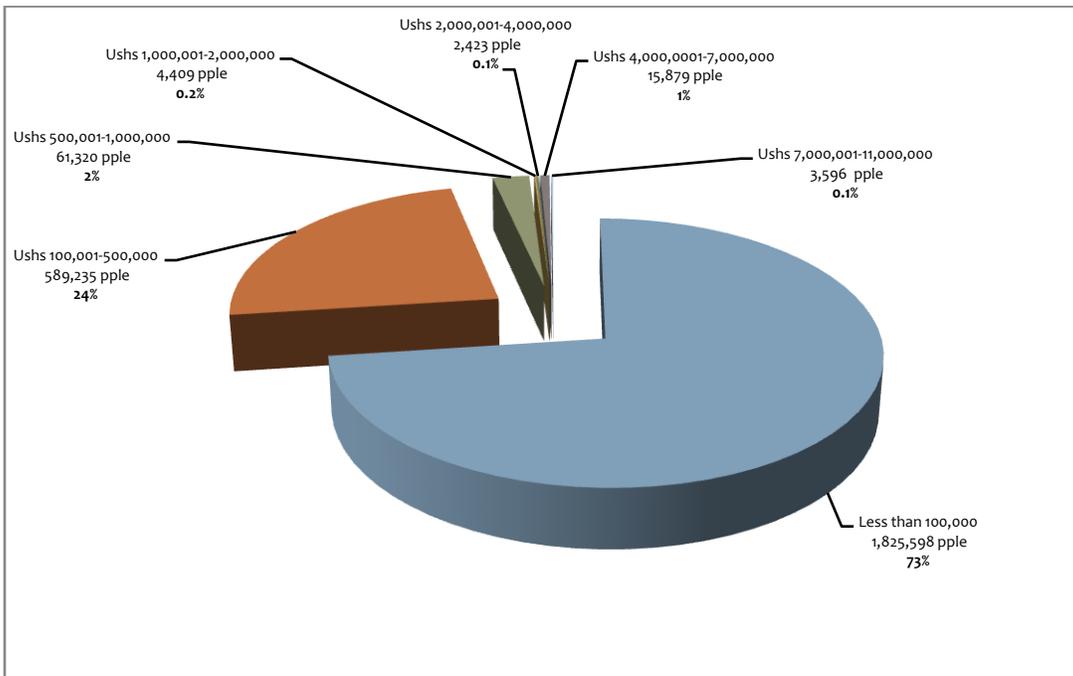
Source: Analysis based on findings of the 2006 Finscope Uganda Survey

**FIGURE 2.6: NUMBER OF UGANDANS WHO HAVE SAVED VARIOUS AMOUNTS MONEY IN SEMI-FORMAL FINANCIAL INSTITUTIONS**



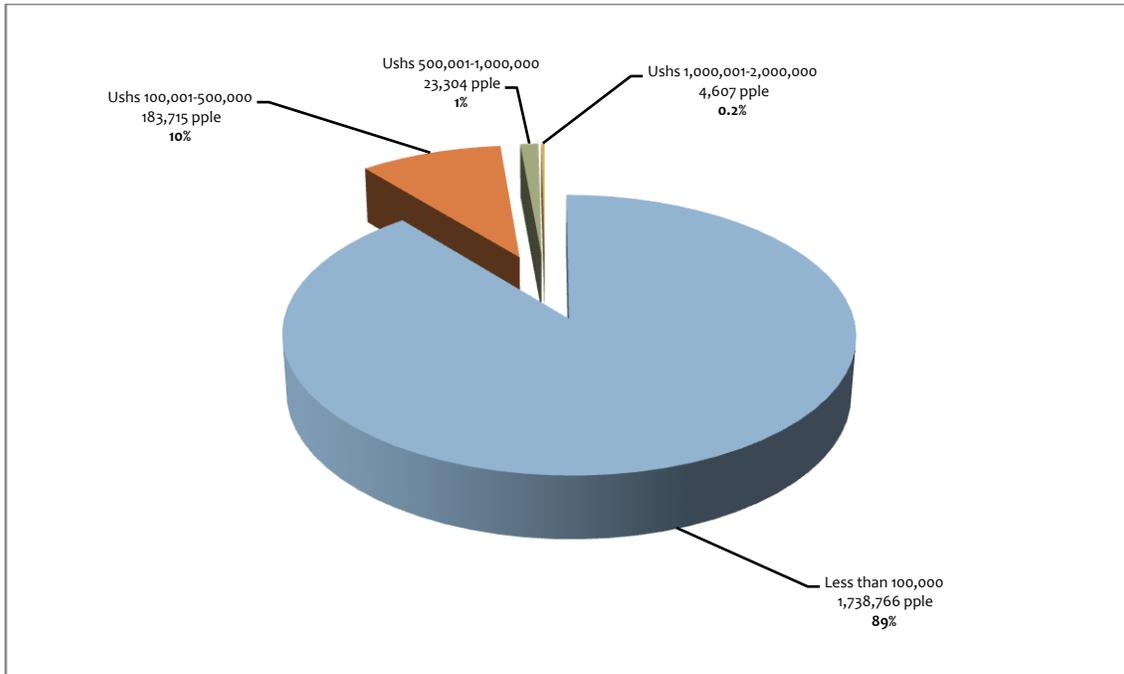
Source: Analysis based on findings of the 2006 Finscope Uganda Survey

**FIGURE 2.7: NUMBER OF UGANDANS WHO HAVE SAVED VARIOUS AMOUNTS MONEY IN INFORMAL FINANCIAL GROUPS OR PLACES**



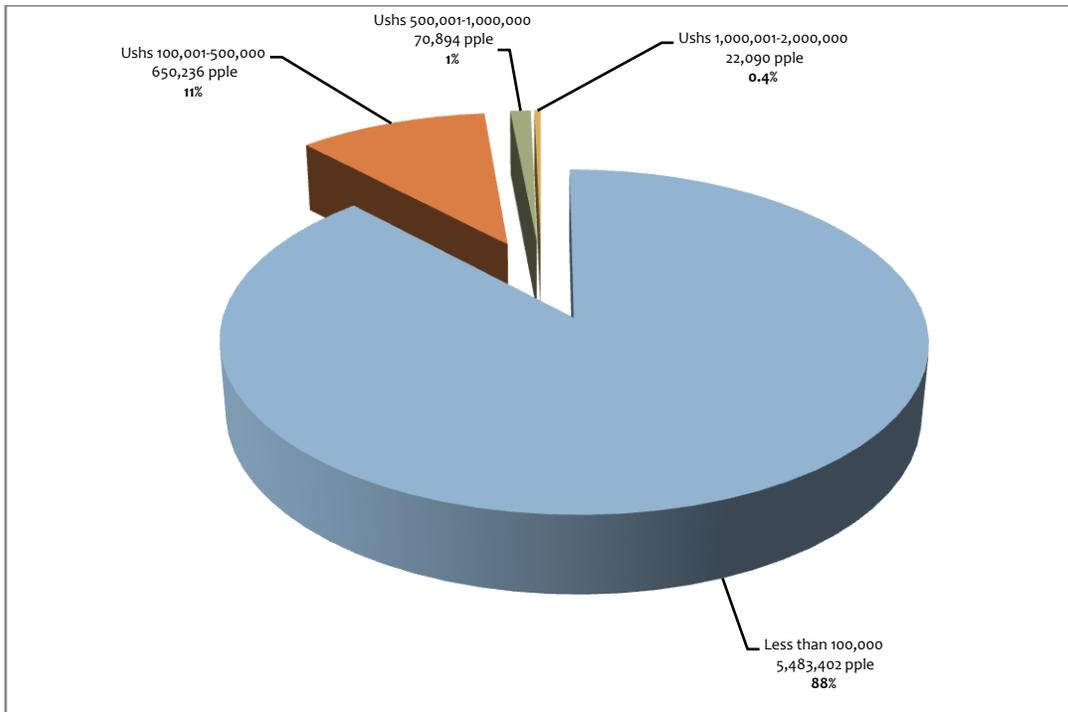
Source: Analysis based on findings of the 2006 Finscope Uganda Survey

**FIGURE 2.8: NUMBER OF UGANDANS WHO HAVE SAVED VARIOUS AMOUNTS MONEY WITH FRIENDS OR RELATIVES (%)**



Source: Analysis based on findings of the 2006 Finscope Uganda Survey

**FIGURE 2.9: NUMBER OF UGANDANS WHO HAVE SAVED VARIOUS AMOUNTS MONEY IN A SECRET PLACE (%)**



Source: Analysis based on findings of the 2006 Finscope Uganda Survey

From figures 2.5-2.9 on average there are 705, 540 Ugandans who have accumulated savings in excess of Ushs 100,000 in the five main channels of savings in Uganda. A bulk of the Ugandans who have accumulated savings in excess of Ushs 100,000 use formal financial institutions like commercial banks to save their income. However most of these savings is on the ordinary savings account (see table 2.10) whose rate of return is far much lower than that earned on the Money Fund managed by the only CIS manager in Uganda (refer to figure 2.4). Thus there is a huge opportunity for the CIS industry in Uganda to tap this consumer base whose savings would earn a higher rate of return if they were invested in the Money Fund one of the financial products in the CIS industry.

FIGURE 2.10: SAVINGS AVENUES UGANDANS CURRENTLY USE

	Total	Formal	Semi-Formal	Informal	Un-served
Sample	2,134	530	80	464	1,060
Weighted base 18+years	9,320,974	2,304,755	397,491	2,077,439	4,541,290
Savings kept in a secret place (%)	71	38	46	64	92
Voluntary savings account in any financial institution or group (%)	36	85	60	58	0
Keeping money with friends and/or relatives (%)	21	15	15	27	22
Investment through contribution to a SACCO, MFI , Group that sits regularly (%)	11	16	40	26	0
Compulsory savings account any financial institution or group (%)	8	15	20	14	0
An investment Account e.g. Shares Account, Fixed deposit account (%)	3	12	3	1	0
A joint account (%)	2	8	6	0	0
A fixed deposit account (%)	0	2	0	0	0

Source: The Steadman Group, 2007

## 2.3 Supply-Side Factors

### 2.3.1 The Level of Capital Markets Development

The level of capital markets development is very critical to the development and vibrancy of the CIS industry because the capital markets provide the bulk of investment opportunities for the CIS industry. The CIS industry thrives on diversification of investments so that the CIS investors can benefit from low risk and above average return investments through economies of scale that come with a pooling of investments. Therefore with a few active equity listings on the Uganda Securities Exchange and a very illiquid corporate bond market there are not many investment opportunities for CISs in Uganda. The government securities market which is more active with regular government listings and a more vibrant secondary market offers more investment opportunities to the CIS industry. This explains why the Money and High Yield Funds which mainly invest in government securities account for the largest percentage of the portfolio investments of the CIS industry in Uganda (refer to table 1.4).

## 3.0 STRATEGIES FOR ENHANCING THE DEVELOPMENT OF COLLECTIVE INVESTMENT SCHEMES IN UGANDA

### 3.1 Enhancing the Culture of Savings & Investment

In analyzing the savings and investment culture of Ugandans four major issues stand out:

- i) Low levels of awareness about investment options in the financial sector especially in the capital markets
- ii) A lack of sufficient experience in undertaking investments evidenced by a fear of risks associated with investment. As one gains experience in investing the more confidence they gain to face the risks associated with financial investments.

Therefore as part of the broader strategy to increase the demand for CISs in Uganda the following need to be done to inculcate a culture of saving and investing in financial products.

- iv) Enhancement of the current **public awareness programs on CIS products** in Uganda by both the Unit Trust Manager and the Capital Markets Authority (CMA). Much as there have been extensive public education programs on CISs by the above mentioned parties a lot more needs to be done because after six (6) years of operations there are very few Ugandans who are aware about CISs.
- v) In addition to public awareness programs the CMA and the current Unit Trust Manager should embark on **financial capability programs** to empower the current and prospective investors to actually invest in CISs other than just increasing their knowledge on CISs.

Investment clubs are one of tools that can be used to build the financial capability of prospective investors because they provide immense opportunities to practice saving and investment. One will find more confidence taking the first step at investing in a group setting provided by an investment club than would be the case if they were taking this first step alone. Therefore as one gains confidence within a group they can then launch out on their own. In an Investment Club one also has the opportunity to benefit from a diverse set of skills and experiences that enables them to further advance their capability to save and invest. DFCU Bank is one of the financial institutions that using investment clubs to empower its clients to better utilize and maximize their

financial investments. In its investment club program DFCU organizes forums in which its clients are trained in various aspects saving, investment and personal financial management. This is an approach that can be adopted by CMA and the market practitioners in the CIS industry.

### 3.2 Enhancing the Competitiveness of the CIS Industry

The CIS industry has two competitive advantages; affordability and higher rates of return which it has not fully maximized to compete favorably with the banking sector for prospective investors. At the core of this is a lack of a wide distributional network and comprehensive marketing strategy for CIS products.

One of the strategies the CIS industry can adopt to increase its accessibility and visibility is to use the upcoming shopping malls/supermarkets like Shoprite, Uchumi, Capital Shoppers, Quality Supermarket e.t.c as access points and marketing channels for CIS products especially the Money Fund which is very easy to understand. Other innovative ways that have been implemented by Databank Group the leading CIS Providers in Ghana (Databank Group, 2008) and which the Ugandan CIS industry can adopt include:

- vi) **SMS Banking** where investors can check out their balances and also top up their CIS investment accounts using their mobile phones by simply texting to a short CODE via SMS. With an active mobile money industry in Uganda, this innovative solution already implemented successfully in Ghana provides immense opportunities for the expansion of the CIS industry in Uganda. MTN Uganda the leading mobile money provider in Uganda already has a subscriber base of 890,000 in just a period of one year which they project to grow to two (2) million by the end of 2010 and three and half (3.5) million by the end of 2012<sup>5</sup>.
- vii) **E-tranzact Partnership** where clients can top up their CIS investment accounts using reloadable cards from the convenience of their homes, office or work place. E-Tranzact is an online real-time payment system that is mainly used in Ghana and Nigeria. E-Tranzact allows account holders to pay for goods and services purchased from merchants, transfer funds to any bank account, cell

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<sup>5</sup> Source: <http://www.intomobile.com/2010/06/04/mtn-uganda-approaching-one-million-mobilemoney-subscribers/> accessed on 21<sup>st</sup> July 2010.

phone, any card, pay bills, order products e.t.c without stress. This is possible because E-Tranzact allows cardholders to use any of the following channels to transact<sup>6</sup>:

- † Web (using any internet browser in a secured transaction)
- † Mobile Phones (GSM, CDMA or Analog)
- † POS (Point of Sale)
- † ATM (Automated Teller Machines)
- † Other Mobile Devices
- † Bank Branches

The E-Tranzact cards can either be debit, reloadable or credit cards and they are issued by banks that have a partnership with the E-Tranzact system<sup>7</sup>. There is even a possibility of linking these cards to one's bank account so that does not have to reload every time they run out of funds on their card so long as they have credit on their bank accounts. These cards can also be used at the ATMs and Points of Sales.

viii) **Establishing strategic distribution alliances** with banks where clients can invest in CISs through the banks' branch networks and can even use their debit or credit cards to make their investments. Databank Group has been able to establish strategic alliances with Barclays Bank, Zenith Bank, Intercontinental Bank and the United Bank of Africa to leverage the branch network of these banks extending to 120 branches to increase the visibility and accessibility of its CIS products.

### 3.3 The Promotion and Facilitation of the Integration of the East African Capital Markets

The Capital Markets Authority and the various stakeholders in the capital markets industry should promote and facilitate the integration of capital markets in the East African Community (EAC) especially with the coming into force of the EAC Common Market Protocol on 1<sup>st</sup> July 2010. The EAC Common Market Protocol provides for the free movement of capital, services, labour, workers, the right of establishment and the protection of cross border investments. These freedoms once implemented would

<sup>6</sup> <http://www.etransactgh.com/Web/introduction.htm> accessed on 22<sup>nd</sup> July 2010.

<sup>7</sup> <http://www.etransact.com/etransact/gep.php> accessed on 22<sup>nd</sup> July 2010.

provide an enabling environment for cross border investments in the EAC capital markets which would thus create more investment opportunities for CISs in Uganda than is currently the case.

However for these freedoms and rights to be realized there needs to be extensive and comprehensive harmonization of the legal and regulatory frameworks of the EAC capital markets which the EAC capital markets regulators have already embarked on under their umbrella body the East African Securities Regulatory Authorities (EASRA).

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