

ROADMAP TO ATTAIN THE FRONTIER MARKET STATUS



Research and Market Development Department, Capital Markets Authority,
Uganda

1. Introduction

Global investors have a preference for markets that can be classified relative to others, and that are easy to access. To achieve a distinction between different markets, index providers or country classification agencies usually place countries into three major development categories, using a transparent and evidence-driven process and a structured framework. The 3 major categories include: developed, emerging and frontier markets.¹

The vision of Uganda's Capital Markets Development Master Plan is to position Uganda's capital markets within the frontier market category of the Morgan Stanley Capital International (MSCI) for equities as a way of attracting more international capital to meet financing needs for both the government and private sector.² Uganda's classification as a frontier market status would expose the country to a vast pool of both passive and active funds. Passive funds track a market index or a specific market segment to determine what to invest in. The objective of passive funds is to find securities that will provide investors with a return equal to the index that the fund's managers are attempting to replicate. Active funds track a benchmark market index with the overall objective of outperforming the benchmark; however, they usually do not deviate from the benchmark too much.

Aside from the direct impact of the pool of funds, it is important to consider the wider effect country classification actually has on a domestic market. By fulfilling criteria for the better functioning of the market, Uganda's capital markets would in itself develop, leading to increased domestic activity such as more issuances and stronger local investor participation. Furthermore, there are a large number of funds are benchmarked against these indices which means they have to invest in the countries included in the index. Therefore, Uganda would attract a significant amount of foreign investments into its equity market. Attracting more foreign investors would increase and diversify the investor base. Foreign investors are also usually more experienced and demand higher trading standards, forcing local market intermediaries and investors to learn from them and improve their capacity to compete. Furthermore, foreign investors tend to be more active on the secondary market and are usually not buy-and-hold investors which would significantly improve liquidity in the market, one of Uganda's main challenges to market development. A country's classification status also signals confidence in a market and points to a level of sophistication through adherence to certain objective criteria required to achieve a given status.³

¹ Euromoney Trading. (2018). *Country Classification Methodology*

² Capital Markets Authority. (2016). *Capital Markets Development Masterplan*

³ Africa Advisory Group. (2018). *Attracting passive investment flows to African Markets. London Stock Exchange Group*

2. Country Classification

As mentioned in the previous section, countries can be classified into three major categories i.e. developed, emerging and frontier markets. A developed market is broadly defined as a country that is advanced in terms of its economy and capital markets. The country must be high income, but this also includes openness to foreign ownership, ease of capital movement, and efficiency of market institutions.⁴

Emerging markets are defined as countries that have some characteristics of a developed market, but are not yet a fully developed market. These countries are often considered to be experiencing rapid growth and industrialization and are attractive due to higher expected return as compensation for the higher risk over already developed countries. Early distinction between the developed and emerging markets were somewhat arbitrary and tended to focus on the relative wealth of countries as the distinguishing measure together with subjective judgements about the quality of the market.⁵

Frontier markets are a subset of emerging markets usually characterized by high rates of economic growth, but small and relatively illiquid stock markets as measured by market capitalization and total market turnover. These markets are often at an early stage of economic and capital markets development, but have attracted attention due to their diversification opportunities and growth potential.⁶ Younger populations, rising economic demand, less liquid capital markets and smaller market capitalization than emerging markets characterize frontier markets.⁷ Frontier markets tend to be less transparent and more prone to inefficiencies, but the inefficiencies create an attractive environment for skilled investors, as the potential reward for surmounting these inefficiencies can be substantial. Foreign investors seeking high, long-term returns and low correlation with other markets typically pursue frontier markets. Exposure to frontier markets can also serve diversification purposes when paired with other asset classes. Companies in frontier markets that are well positioned and managed for domestic oriented growth can be attractive to investors.

⁴ United Nations. (2014). *World Economic Situation and Prospects*

⁵ FTSE. (2018). *Equity Country Classification Process*

⁶ FTSE Russell. (2014). *Frontier Markets, Accessing the next frontier*

⁷ KFW Bankengruppe. (2011). *Focus on Financial Frontier Markets*

3. The Frontier Market Indexes

Market indexes in general measure the performance of a given security market, market segment or asset class. Stock market indexes can be categorized in many ways such as global stock market index, regional index or by level of industrialization or income e.g. developed markets, emerging markets or frontier markets.

Frontier market indexes measure the performance of equity markets in small nations that are at an early stage of capital market development. There are many frontier market indexes such as the MSCI frontier market index; the Financial Times Stock Exchange (FTSE) frontier market index; and the Standard & Poor (S&P) frontier market index. Each frontier market index uses different selection criteria and construction methodologies leading to a diverse set of underlying constituents both in terms of countries and companies. It should be noted that the group of frontier markets included in the different indexes changes over time and frontier countries can be upgraded to an emerging market index or removed from the list of frontier markets.

There are a number of global indexes, but for the purpose of this roadmap, we review and compare the frontier market classification framework of the MSCI, FTSE and S&P indexes. The aforementioned indexes are arguably the most popular among global investors. Attaining the frontier market status in any of the three indexes would have the similar effect as attaining the MSCI frontier market status i.e. opening up Uganda's capital markets to foreign investors and attracting foreign investments into Uganda.

3.1 The MSCI Frontier Market Index

Established in 1969, MSCI is a global provider of equity, fixed income, hedge fund and stock market indexes. MSCI provides independent research-driven insights and tools for institutional investors. Covering over 27,000 securities across the developed, emerging and frontier markets, the MSCI research-based indices are used by global investors to build and manage their portfolios.⁸

The MSCI frontier market index tracks the stock markets of countries that meet the MSCI frontier market classification framework. The framework aims to reflect the views and practices of the international investment community by striking a balance between a country's economic development and accessibility of its market, while preserving index stability.⁹ The framework consists of the following three criteria:

- I. Economic development

This is a quantitative criterion only used in determining the classification of developed markets due to the wide variety of development levels within the emerging and frontier markets.

⁸ <https://www.msci.com>

⁹ MSCI. (2018). *Market Classification Framework*

II. Size and liquidity

The focus of this quantitative criterion is market capitalization and market liquidity.

III. Market accessibility

This qualitative criterion includes several sub-criteria and aims to reflect international institutional investors' experience of investing in a given market. A market survey largely establishes compliance with MSCI's market accessibility criteria.

To be classified in the frontier market investment universe, a country must meet at least 2 of the size and liquidity requirements and some of the market accessibility requirements shown in *Table 1*.

Table 1: MSCI Frontier Market Classification Framework

Criteria	Frontier Market Status
Size and liquidity requirements: ¹⁰	
<ul style="list-style-type: none"> Company size (full market capitalization) 	USD 635 million
<ul style="list-style-type: none"> Security size (float market capitalization) 	USD 47 million
<ul style="list-style-type: none"> Security liquidity 	2.5% Annualized Traded Value Ratio (ATVR) ¹¹
Market accessibility criteria	
<ul style="list-style-type: none"> Openness to foreign ownership 	At least some
<ul style="list-style-type: none"> Ease of capital inflow/outflows 	At least partial
<ul style="list-style-type: none"> Efficiency of operational framework 	Modest
<ul style="list-style-type: none"> Competitive landscape 	High
<ul style="list-style-type: none"> Stability of the institutional framework 	Modest

Source: MSCI Market Classification framework

As at December 2018, the MSCI frontier market index had 29 countries from the Americas, Europe, Africa, Middle East and Asia. Out of the 54 countries in Africa, only 6 are part of the MSCI frontier market index. These include Kenya, Mauritius, Morocco, Nigeria, Tunisia and West African Economic and Monetary Union (WAEMU). WAEMU is treated as a single country for the purpose of index construction and it consists of the following countries: Benin, Burkina Faso, Ivory Coast, and Senegal. Among the African countries, Nigeria has the highest number of

¹⁰ At least two companies meeting the following standard index criteria

¹¹ ATVR is used to quantify and filter markets depending on market liquidity. It is calculated as the median value of shares traded daily in relation to the market capitalization of the stock.

constitutes in the index as shown in *Table 2*. A constitute is an individual security that is a member of an index.

Table 2: African Countries Classified as MSCI Frontier Markets (December 2018)

Country	Number of MSCI Constituents
Benin	1
Burkina Faso	3
Ivory Coast	7
Kenya	9
Mauritius	10
Morocco	22
Nigeria	33
Senegal	1
Tunisia	10

Source: MSCI Country Classification Standard

MSCI annually evaluates equity markets of countries around the world to determine each country's classification as a developed, emerging, frontier or standalone market. The annual market classification review is based on the classification framework in *Table 1* and is designed to ensure that MSCI indexes remain relevant and precise investment decision support tools for investors globally. In essence this means that countries can be upgraded (e.g. from frontier to emerging) or downgraded (e.g. from frontier to standalone) or even completely removed from the MSCI indexes.

3.1.1 MSCI Standalone Market Index

The standalone market indexes are created for countries not covered by MSCI during its index review. MSCI standalone market indexes are broadly classified into two groups:

- I. Newly eligible markets which may either be new markets, not previously covered by MSCI or markets that were previously closed to a specific group(s) of investors; and
- II. Markets previously classified under developed, emerging or frontier market categories, reclassified to standalone status as they no longer meet the index requirements.

There are two types of a standalone market index that can be created for a country i.e. a Standalone Market Standard Index and a Standalone Market Investable Market Index (IMI).

- ✚ A standalone Market Standard Index may be created for countries having a minimum of two companies with securities meeting the size and liquidity requirements for the frontier markets standard index.
- ✚ A Standalone Market IMI may be created for a market having a minimum of one company with securities meeting the size and liquidity requirements for the frontier markets standard index.

The market must demonstrate a relative openness and accessibility for foreign investors and is not undergoing a period of extreme economic or political instability. MSCI also considers the availability and accuracy of market data when deciding on the potential creation of standalone market index for a country. The creation of the standalone index generally does not require MSCI client consultation.

By December 2018, the MSCI standalone market index had 12 countries from Americas, Europe, Africa, and Middle East. Out of the 12 countries, three were African countries, namely: Botswana, Ghana and Zimbabwe.

Table 3: African Countries in the MSCI Standalone Index (December 2018)

Country	Number of MSCI Constituents
Botswana	2
Ghana	1
Zimbabwe	4

Source: MSCI Country Classification Standard

3.1.2 Uganda’ Standing as per the MSCI Frontier Market Classification Framework

Market liquidity and the size of listed companies as measured by full market capitalization are the major barriers to Uganda achieving the MSCI frontier market status as shown in *Table 8*. Some of the other identified barriers are the absence of a foreign board where non-domestic investors can trade with each other, and the lack of a regulatory framework for short selling and stock lending.

Table 4: Uganda’s Current Standing as per the MSCI Frontier Requirements

Criteria	Frontier Market Status	Uganda’s Current Standing
Size and liquidity requirements		
<ul style="list-style-type: none"> Number of companies meeting the following standard index criteria 	2	None

Criteria	Frontier Market Status	Uganda's Current Standing
<ul style="list-style-type: none"> Company size (full market capitalization) 	USD 635 million	None of the listed companies meet this requirement
<ul style="list-style-type: none"> Security size (float market capitalization) 	USD 47 million	3 listed companies have a float market capitalization greater than USD 47 million. DFCU-USD 66 million, SBU-USD 86 million, UMEME-USD 141 million
<ul style="list-style-type: none"> Security liquidity 	2.5% Annualized Traded Value Ratio (ATVR) ¹²	0.31% AVTR in 2018
Market accessibility criteria		
<ul style="list-style-type: none"> Openness to foreign ownership 	<p>Existence of qualifying conditions for international investors.</p> <p>Existence of a level playing field for all institutional investors.</p> <p>Proportion of the market being accessible to non-domestic investors.</p> <p>Proportion of shares still available for non-domestic investors.</p> <p>Existence of a foreign board where non-domestic investors could trade with each other.</p> <p>Equal economic and voting rights as well as availability of information in English.</p>	<p>Both domestic and international investors use the same Know Your Client (KYC).</p> <p>Uganda currently offers a level playing field for all institutional investors despite the dominance of NSSF.</p> <p>Uganda offers equal access to both domestic and foreign investors.</p> <p>Non-domestic investors have access to all shares.</p> <p>No foreign board in place.</p> <p>Both foreign and domestic shareholders have equal economic and voting rights as</p>

¹² ATVR is the main number used by MSCI to quantify and filter markets depending on how liquid they are. ATVR is calculated as the median value of shares traded every day in relation to the market capitalization of the stock.

Criteria	Frontier Market Status	Uganda's Current Standing
	Equal rights for minority shareholders.	well as full access to market information in English. Minority shareholders have the same rights as the majority shareholders.
<ul style="list-style-type: none"> Ease of capital inflow/outflows 	<p>Existence of restriction on inflows and outflows of foreign capital to/from the local stock market (excluding foreign currency exchange restrictions).</p> <p>Existence of a developed onshore and offshore foreign exchange market.</p>	<p>There are no restrictions on the inflows and outflows of foreign capital to/from the local stock market.</p> <p>Uganda has a well-developed foreign exchange market, ranking third in the ease of foreign exchange access in the 2018 Absa Africa Financial Markets Index.</p>
<ul style="list-style-type: none"> Efficiency of operational framework 	<p>Existence/level of complexity of registration requirements for international investors such as Tax IDs as well as ease/complexity for setting up local accounts (e.g., documents to be provided, approvals required). The time to complete the process includes the preparation of the documents.</p> <p>Level of advancement of the legal and regulatory framework governing the financial market, the stock exchange and the various other entities involved in the</p>	<p>One standard format of the Know Your Client (KYC) is used for both local and international investors. International investors therefore have similar registration requirements like the local investors. However, it should be noted that having similar registration requirements is not a guarantee that registration is easy for foreign investors. The level of complexity is determined based on a survey conducted by MSCI to obtain the views of foreign investors.</p> <p>The capital markets operational framework is governed by regulations and enforced by the CMA. Following the 2016 amendment of the CMA Act,</p>

Criteria	Frontier Market Status	Uganda's Current Standing
	<p>financial markets, an important weight is assigned to ease of access (including in English), lack of ambiguity and prompt enforcement of laws and regulations, as well as consistency over time.</p> <p>Timely disclosure of complete stock market information items (e.g., stock exchange alerts, corporate news, float information, dividend information) in English and under reasonable commercial terms, as well as the robustness and enforcement of accounting standards.</p> <p>Well-functioning clearing and settlement system based on international standards including delivery versus payment (DVP), the absence of pre-funding requirements/practices and the possibility to use overdrafts. Availability of real omnibus structures.</p> <p>Level of competition amongst local custodian banks as well</p>	<p>the CMA is now a signatory to Appendix A of the International Organization of Securities Commissions (IOSCO), a global securities standards setter. This means Uganda is compliant with most of the international best practices in regulation. The aspect of prompt enforcement is however a subjective matter.</p> <p>Under continuing listing obligations, listed companies are required to disclose information to investors through the exchange, online and print media, which provides timely disclosure of information of stock market information to both local and foreign investors.</p> <p>There is basically DVP which ensures finality of the transactions. Settlement is effected by T+3 through commercial bank money. There are no pre-funding requirements although retail and foreign accounts are usually prefunded. Overdraft facilities are possible if arranged with the settlement bank. The MSCI survey will further establish how the clearing and settlement process is rated.</p> <p>The market currently has 5 custodian banks, 2 of which are global i.e. Standard</p>

Criteria	Frontier Market Status	Uganda's Current Standing
	<p>as the presence of global custodian banks.</p> <p>Existence of an efficient mechanism that prevents brokers to have unlimited access to the investor's accounts and guarantees the safekeeping of its assets.</p> <p>A well-functioning central registry or independent registrars and a central depository.</p> <p>Level of competition amongst brokers ensuring high quality services (e.g. cost efficient trading, ability to execute grouped trades at the same price for the various accounts of a fund manager).</p> <p>Possibility of off-exchange transactions and "in-kind" transfers.</p> <p>Existence of a regulatory framework as well as an efficient mechanism allowing</p>	<p>Chartered Bank, a representative of State Street Corporation¹³ and Stanbic Bank, a member of Standard Bank Group.¹⁴</p> <p>Brokerage accounts are separated from the client trustee accounts that are supervised and audited by CMA and the SCD.</p> <p>The SCD is the central registry and it monitors SCD registrars that provide a full range of registry services.</p> <p>The market currently has 9 licensed stockbrokers who compete for investors in the market. This is however not evidence of competition in the market. The MSCI survey would be the determinant of the level of competition.</p> <p>The SCD rules were amended and now cater for private transfer of securities, covering the off-exchange transactions and in-kind transactions.</p> <p>No regulatory framework for stock lending.</p>

¹³ State Street Corporation is an American financial services and bank holding company headquartered in Boston with operations worldwide.

¹⁴ The Standard Bank Group is a South African financial services group and is Africa's biggest lender by assets.

Criteria	Frontier Market Status	Uganda's Current Standing
	<p>extensive use of stock lending.</p> <p>Existence of a regulatory and practical framework allowing short selling.</p>	No regulatory framework for short selling.
<ul style="list-style-type: none"> Competitive landscape 	Existence of anti-competitive clauses restricting investors' access to stock exchange information, data and investment products, including, for example the provision of independently calculated indexes or the creation of baskets of securities used in the creation of financial products. In addition, anti-competitive clauses should not result in global or regional financial products becoming in breach of local market rules, regulations or other restrictions.	The USE does not have anti-competitive clauses that restrict investors' access to derived stock exchange information, data and investment products. However, the USE charges for some data which may be seen as restrictive.
<ul style="list-style-type: none"> Stability of the institutional framework 	Basic institutional principles such as the rule of law and its enforcement as well as the stability of the "free-market" economic system. Track record of government intervention with regards to foreign investors.	The capital market is regulated by the CMA. The government is free-market and rarely intervenes with regards to foreign investors. The general rule of law is dependent on the MSCI requirements and will be determined in the survey.

Overall, Uganda meets approximately **65 percent** of the requirements for inclusion in the MSCI frontier markets index. However, it should be noted that this is a tentative score that could be different from the actual score from MSCI. Uganda's true standing as per the MSCI market classification framework can only be well established after a survey is carried out by the MSCI.

This however does not mean that the CMA and the Uganda Securities Exchange (USE) should not continue to play their part towards attaining the MSCI frontier market status. For starters, CMA and the USE need to engage the MSCI country classification team to help identify Uganda's major

barriers and develop proper measures to overcome them. The CMA should also develop a regulatory framework for stock lending and short selling.

The aim should be to attain the MSCI standalone market standard index or the standalone Market Investable Market Index (IMI), with a long-term goal of eventually attaining the MSCI frontier market status. This is because the former index can be created for countries having a minimum of two companies meeting the size and liquidity securities requirements for the frontier markets standard index, while the latter can be created for a market having a minimum of one company with securities meeting the requirements for the frontier markets standard index, and a minimum of two companies with securities meeting the requirements for the frontier markets small cap index.

4. Other Indexes

4.1 Financial Times Stock Exchange Frontier Market Index

The FTSE equity country classification process operates on an annual schedule that starts in January and ends in September, starting with an in-depth assessment of markets on the watch list, and countries highlighted for possible addition to the watch list. FTSE Russell, the FTSE index provider, operates a watch list of countries with scores on the quality of markets matrix that have been met, or are close to meeting the technical criteria required for reclassification. The watch list also includes countries with scores that have fallen below the required score to maintain the countries' current classifications and are being considered for demotion.

A quality markets matrix is central to the FTSE equity country classification process.¹⁵ The matrix includes information on the Gross National Product (GNI) per capita as calculated by the World Bank and the country's credit rating. However, the GNI and credit rating criteria are only applied to countries categorized as developing markets and are therefore not applicable to Uganda. The rest of the matrix is divided into the following four sections: dealing landscape and brokers, custody and settlement, regulation, and derivatives. Each of the four sections is further broken down into factors that are considered essential for classification. Markets are scored as pass, restricted (partial failure) or not met on each of the classification criteria. Frontier markets are required to meet five of the classification criteria as shown in *Table 5* with a pass.

Table 5: FTSE Quality of Markets Matrix

Criteria	Frontier Market
Market and regulatory environment	
Formal stock market regulatory authorities actively monitor market	✓
No objection to or significant restrictions or penalties applied to the investment of capital or the repatriation of capital and income	✓
Custody and Settlement	
Settlement - Rare incidence of failed trades	✓
Clearing & settlement - T+2 / T+3	✓
Dealing Landscape	
Transparency - market depth information/visibility and timely trade reporting process	✓

Source: FTSE Equity Country Classification Process (September 2018)

According to the matrix Uganda should meet the requirements as shown in Table 5, however, in addition to the matrix, FTSE also carries out a survey and uses a questionnaire to engage stock

¹⁵ FTSE. (2018). *Country Classification Process*

exchanges and regulatory authorities. The responses to the survey help form the basis of the initial quality of markets assessment and subsequent upgrades.

The FTSE Russell Country Classification Advisory Committee, reporting to the FTSE Russell Policy Advisory Board then undertakes an objective assessment of market against the quality of markets matrix. A country that meets the criteria for classification as a frontier market becomes eligible for inclusion in the FTSE frontier index on condition that at least three constituents pass the eligibility criteria and screens. Constituents are required to pass screens for liquidity, free float and foreign ownership restrictions as determined by the survey carried out by FTSE. However, it is unclear what exactly these requirements are.

The FTSE frontier market had a total twenty (20) countries, out of which six (6) were African as at December 2018.¹⁶ Just like the MSCI frontier market index, among the African countries, Nigeria had the highest number of constituents in the FTSE frontier market index as shown in *Table 6*.

Table 6: FTSE Frontier African Countries (December 2018)

Country	Number of Constituents
Ivory Coast	4
Kenya	16
Mauritius	4
Morocco	20
Nigeria	29
Tunisia	14

Source: FTSE. (2018). *Frontier Index Series – Factsheet*

4.1.1 Uganda’s Current Standing as per FTSE Frontier Market Requirements

Despite the fact that Uganda meets the requirements of the FTSE frontier market status, as per the quality of market matrix (*see table 7*), it should be noted that a questionnaire, which is used to engage stock exchanges and regulatory authorities, is also used. The responses from the questionnaire are used to form a basis of the initial quality of market assessment.

¹⁶ FTSE. (2018). *Frontier Index Series – Factsheet*

Table 7: Uganda’s Current Standing as per the FTSE Frontier Requirements

Criteria	Uganda’s Current Position
World Bank Gross National Product per capita Rating	USD 600
Credit worthiness	Uganda’s credit rating by Standard and Poor, Moody’s and Fitch is B, B2 and B+ respectively, all with a stable economic outlook ¹⁷
Market and regulatory environment	
Formal stock market regulatory authorities actively monitor market	The stock market is actively regulated and monitored by the CMA, a semi-autonomous body established in 1996.
No objection to or significant restrictions or penalties applied to the investment of capital or the repatriation of capital and income	There are no restrictions or penalties on the inflows and outflows of foreign capital to/from the local stock market and in/out of the country.
Custody and Settlement	
Settlement - Rare incidence of failed trades	The SCD has never experienced a failed trade. As a requirement, the broker/dealer verifies availability of securities in the client’s securities account upon receipt of the trade orders.
Clearing & settlement - T+2 / T+3	T+3
Dealing Landscape	
Transparency - market depth information/visibility and timely trade reporting process	The USE prepares daily market reports that are emailed to investors. A daily market snap shot is also uploaded on the USE website. A detailed market report

¹⁷ <https://tradingeconomics.com/uganda/rating>

	and historical data are available at a fee.
--	---

Based on the given criteria, Uganda seems to have a perfect score as per the FTSE frontier market requirements. However, it should be noted that this can only be determined by the FTSE country classification team, subject to a survey of the market and an assessment by the FTSE Russell Country Classification Advisory Committee.

The CMA and the Uganda Securities Exchange (USE) should engage FTSE country classification team, because it is only through the survey that CMA will know the market’s current position. Working with an experienced partner with a reliable and relevant framework will also help Uganda to advance and meet the requirements by following clear guidelines and focusing on specific problem areas.

4.2 Standard and Poor Frontier Market Index

S&P Global Inc., formerly McGraw Hill Financial Inc., incorporated on December 1925, is a provider of ratings, benchmarks, analytics and data to capital and commodity markets around the world.¹⁸ The company operates through three segments: Ratings, Market and Commodities Intelligence, and S&P Dow Jones Indices.

The S&P Dow Jones indices country classification analysis utilizes both quantitative and qualitative factors. Many of the factors in determining if a market is developed, emerging or frontier are not amenable to quantitative decisions. An initial classification provides S&P Dow Jones with a list of countries to include on its annual country classification consultation, with the final decision made by the S&P Dow Jones Indices Global Equity Index Committee based on both consultations and the quantitative criteria. The quantitative criteria cover a range of factors reflecting macroeconomic conditions, political stability, legal property rights and procedures, and trading and settlement processes. Countries that meet most of the minimum requirements are eligible for inclusion in the frontier market category.¹⁹ Countries must meet a minimum of 2 of the S&P Dow Jones initial criteria to be considered for the S&P frontier market status as shown in *Table 8*.

¹⁸ <https://www.reuters.com/finance/stocks/company-profile/SPGI.N>

¹⁹ S&P Dow Jones. (2018). *Country Classification Methodology*

Table 8: Initial Criteria for S&P Dow Jones Indices' Global Equity Index Series Eligibility

Initial Criteria	Frontier market status
<ul style="list-style-type: none"> • Full domestic market capitalization greater than USD 2.5 billion • Annual domestic turnover value greater than USD 1 billion • Exchange development ratio²⁰ greater than 5% (full domestic market capitalization of the exchange divided by the country's nominal GDP) 	A country must meet a minimum of two of the requirements

Source: *Country Classification Methodology – S&P Dow Jones Indices (December 2018)*

The S&P frontier BMI index includes more than 500 securities from 34 small and illiquid frontier markets. Out of the 34 markets, 10 are from Africa as shown in *Table 9*.

Table 9: S&P Frontier African Countries (December 2018)

Country	Number of Constituents
Morocco	22
Nigeria	16
Kenya	22
Mauritius	24
Tunisia	45
Botswana	11
Cote D'Ivoire	16
Ghana	13
Namibia	4
Zambia	8

Source: *S&P Dow Jones Indices (December 2018)*

²⁰ Market development ratio is calculated by dividing the full domestic market capitalization of the exchange by the country's nominal Gross Domestic Product (GDP)

The S&P Frontier BMI serves as the universe for the S&P Africa Frontier, S&P Pan Africa and S&P Pan Eastern Europe indices. The S&P Pan Africa serves as the universe for the S&P Pan Africa ex South Africa. The indexes use the same index rules and selection criteria of their parent index. Within each index, constituents must meet minimum size and liquidity requirements to ensure that it is investable and tradable.²¹ Once a market is a member of the S&P Frontier BMI, it is eligible for the S&P Africa frontier, S&P Pan Africa, S&P Pan Africa ex South Africa indices as long as it meets all the required criteria. Just like the MSCI and FTSE frontier indices, the S&P frontier BMI index also undergoes a review where new constituents are added and constituents no longer meeting eligibility criteria are removed.

4.2.1 Uganda’s Current Standing as per S&P Frontier Market Requirements

Uganda falls short of all the initial requirements for inclusion in the S&P frontier market status as shown in *Table 10*. The only criteria Uganda comes close to achieving is the exchange development ratio, falling short by 0.3% compared to the 5.0% required (*see table 10*).

Table 10: Uganda’s Current Standing as per the S&P Frontier Requirements

Initial Criteria	Uganda’s Current Position
<ul style="list-style-type: none"> • Full domestic market capitalization greater than USD 2.5 billion 	USD 1.44 billion
<ul style="list-style-type: none"> • Annual domestic turnover value greater than USD 1 billion 	USD 19.31 million
<ul style="list-style-type: none"> • Exchange development ratio²² greater than 5% (full domestic market capitalization of the exchange divided by the country’s nominal GDP) 	4.70%

Uganda is close to meeting the exchange development ratio and USD 1.06 billion away from meeting the full domestic market capitalization requirement, which would suffice to obtain S&P frontier market status as only 2 of the requirements need to be met. However, the market capitalization in Uganda would have to nearly double. For this to be possible many of the requirements for the other indices would have to be implemented. Therefore, by encouraging more companies to list and by implementing the requirements for the FTSE and MSCI, Uganda would also be working towards achieving the S&P frontier market status. As a recommendation, the CMA should direct its efforts towards attaining the MSCI or FTSE frontier market index.

²¹ S&P Dow Jones: *S&P Frontier Indices Methodology*

²² Market development ratio is calculated by dividing the full domestic market capitalization of the exchange by the country’s nominal Gross Domestic Product (GDP)

5. Cross Country Comparison

As seen in *Table 11*, countries like Ghana, with a market capitalization to GDP ratio lower than Uganda's, are part of the MSCI index; Ghana has a standalone index. This trend can also be seen across countries with GDP lower than Uganda's such as Mauritius, Botswana, Zimbabwe and Namibia. One explanation for this could be that the aforementioned markets worked towards meeting all the requirements to attain the frontier market status. Another observation from the table is that only Zimbabwe is included in the MSCI and FTSE and not the S&P, while Namibia and Zimbabwe are included in the S&P, but not MSCI and FTSE.

Table 11: Cross Country Comparison

COUNTRY	GDP 2017 (USD MILLION)	TOTAL MARKET CAP 2017 (USD MILLION)	MARKET CAP AS A PERCENTAGE OF GDP	MSCI	FTSE	S&P	NUMBER OF LISTED COMPANIES
WAEMU	100,325.92	11,826.28	11.79	✓	✓	✓	44
Kenya	74,938.19	24,294.73	34.42	✓	✓	✓	66
Mauritius	13,338.15	9,736.85	73.00	✓	✓	✓	99
Morocco	109,139.48	67,022.55	61.42	✓	✓	✓	76
Nigeria	375,770.71	37,201.30	9.90	✓	✓	✓	167
Tunisia	40,256.68	8,936.98	22.20	✓	✓	✓	83
Botswana	17,406.53	4,216.09	24.22			✓	36
Ghana	47,330.02	1,318.23	2.79	✓		✓	39
Zimbabwe	17,845.82	12,737.43	71.37	✓			65
Namibia	13,244.60	2,913.81	22.00			✓	42
Zambia	25,808.67	4,695.00	18.19			✓	44
Uganda	25,891.06	1,207.21	4.66	✗	✗	✗	17

Source: World Bank, FTSE, MSCI, S&P

6. Steps to Achieving Inclusion into a Frontier Market Index

The goal should be to attain the MSCI standalone index, with a long-term view of obtaining the frontier market status, or the FTSE frontier market status. However, the S&P should not be ruled out because as seen in *Table 11* in the previous section, the S&P index has more countries, some of which are not included in MSCI or FTSE.

As some of the requirements are judged through market surveys, CMA needs to interact with all the three index providers to determine which index is the easiest for Uganda to join and what measures need to be implemented for this to take place.

However, in order towards moving closer MSCI frontier market status, it is clear the following actions need to be undertaken:

- Encouraging/mandating more companies to list
- Improving the settlement process, especially introducing the settlement through central bank money
- Developing a securities lending and short selling framework

Ministry of Finance Planning and Economic Development (MoFPED), CMA and USE, with help and support from market intermediaries need to take coordinated measures to address key shortcomings in Uganda's capital markets that would serve as barriers to achieving the frontier markets status. The steps are highlighted in the table that follow.

Table 12: Steps for Inclusion in a Frontier Market Status

Engaging Index Providers			
Index	Objective	Required Action	Responsible Organization
MSCI FTSE S&P	Clear Guidelines of the requirements for attaining Frontier Market Status	<p>a) Engagement the MSCI, S&P and FTSE country classification teams and establish a full set of requirements to attain frontier market status.</p> <p>b) Engage Financial Sector Deepening Africa (FSDA) and other development partners to support to implement the requirements.</p> <p>c) Form a committee charged with the responsibility of overseeing the attainment of frontier market status. The committee should work closely with the committee that was set up in CMA Kenya to carry out a similar role.</p>	CMA CMA CMA
Steps to Meet Specific Criteria in the Indexes			
Index	Criteria	Required Action	Responsible organization
MSCI FTSE S&P	Market Capitalization	<p>a) Continue with the Issuer Education program with the target shifting to large companies (as measured by market capitalization) in the oil and gas sector, banks and telecommunication companies.</p> <p>b) Engage the Ministry of Information Communication and Technology together with the Uganda Communications Commission (UCC) to ensure implementation of the National Broadband Policy that requires the mandatory listing of all telecommunication companies.</p> <p>c) Engage MoFPED and BoU on the mandatory listing of all Tier1 banks.</p>	CMA, USE, Market Intermediaries CMA, Ministry of ICT, UCC MoFPED, CMA BoU

		<p>d) MoFPED should follow up the listing of all former state-owned companies that were privatized with a provision requiring them to list (Kakira and Tororo Cement).</p> <p>e) CMA should engage the MoFPED on the possibility of listing state owned enterprises such as Pride Microfinance and Housing Finance Bank.</p> <p>f) Set up the Deal Flow Facility (DFF) that will take business enterprises through the preparatory steps they need to undertake in order to tap into either private equity or public equity. This will encourage more companies to come to the market.</p>	<p>MoFPED, CMA</p> <p>CMA, MOFPED</p> <p>CMA, USE, Market intermediaries</p>
MSCI FTSE	Market accessibility and liquidity	<p>a) Formation of a foreign board where non-domestic investors can trade with each other.</p> <p>b) Develop a regulatory framework for short selling and stock lending.</p> <p>c) Continue with the countrywide investor education program to encourage retail investor participation and ease the opening of trading accounts to develop a diverse investor base. This would increase investor participation and improve market liquidity.</p>	<p>CMA, USE</p> <p>CMA, BoU, MOFPED</p> <p>CMA, Market Intermediaries</p>

7. Roadmap

Table 13: Timelines for Steps for Inclusion into the Frontier Market Indices

No.	Steps for Inclusion	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25	2025/26
1.	Engaging MSCI, S&P and FTSE							
2.	Engaging development partners for support							
3.	Formation of a committee charged with overseeing the attainment of the frontier market status							
4.	Continue with the Issuer Education program							
5.	Engage Ministry of ICT and UCC on implementation of the National Broadband Policy							
6.	Engage MoFPED and BoU on the mandatory listing of Tier1 banks							
7.	Follow up the listing of all former state-owned companies that were privatized with a provision requiring them to list (Kakira and Tororo Cement)							
8.	Engage MoFPED on the possibility of listing state owned enterprises such as Pride Microfinance and Housing Finance Bank							
9.	Set up the Deal Flow Facility							
10.	Continue with investor education to encourage retail participation							
11.	Develop a regulatory framework for short selling and stock lending							
12.	Formation of a foreign board where non-domestic investors can trade with each other							
13.	Attain MSCI standalone market index, FTSE & S&P frontier market status							