2018/2019 RESEARCH BULLETIN

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Glossary of Terms

Administrator of a pension or provident fund - means a person who provides administration or similar services to the fund.

Pension Fund - means any fund the principal objective of which is to provide for the payment of a pension to a person, who has been a member of the fund, on his retirement.

Provident Fund - means any fund which is not a pension fund where a lump sum payment is made at retirement.

Trustee of a Pension or Provident Fund - means a person acting as a trustee of a pension or provident fund.

ABBREVIATIONS USED IN THE BULLETIN

AML/CTF		Anti Money Laundering/Combatting The Financing of Terrorism
ASEA	-	African Securities Exchanges Association
ASIC		Australian Securities and investment Commission
ATM		Automated Teller Machine
ATS		Automated Trading System
BSEL		Botswana Stock Exchange Limited
B2B		Business to Business
B2C		Business to Client
BSM		Botswana Share Market
BTC		Botswana Telecommunications Corporation
BWP		Botswana Pula
BSE		Botswana Stock Exchange
BURS		Botswana Unified Revenue Services
CEE		Central and Eastern Europe
CEO		Chief Executive Officer
CIPA		Companies Intellectual Properties Authority
CSDB		Central Securities Depository Botswana
DCI		Domestic Companies Index
EU		European Union
FCI		Foreign Companies Index
FED		Federal Reserve Bank
FSB		Financial Services Board
GDP		Gross Domestic Product
IFSC		International Financial Services Centre
IOSCO		International Organization of Securities Commissions
JSE		Johannesburg Stock Exchange
MMOU		Multilateral Memorandum of Understanding
MSCI		Morgan Stanley Capital International
NASDAQ		National Association of Securities Dealers Automated Quotations
NBFI		Non Bank Financial Institution(s)
NBFIRA		Non-Bank Financial Institutions Regulatory Authority
OECD		Organization of Economic Co-operation and Development
SIB		Securities Infrastructure Businesses
SRO		Self-Regulatory Organization
SSE		tockholm Stock Exchange
SWOT		Strength, Weaknesses, Opportunity and Threats
UK		United Kingdom
US		United States
USD		United States Dollar
WFE		World Federation of Exchanges

Foreword

The purpose of the Research Bulletin is to provide a forum where research relevant to the economy and the financial sector, with particular reference to the non-bank financial sector can be disseminated.

It is my pleasure to present the 2018/19 NBFIRA Research Bulletin which discusses issues pertaining to global and domestic capital markets. This bulletin documents major developments in the domestic capital markets and global trends with significant impact, either now or in the future of the domestic capital markets. A special report on the performance of the domestic capital markets is included to put the deliberations into context.

The purpose of the Research Bulletin is to provide a forum where research relevant to the economy and the financial sector, with particular reference to the non-bank financial sector can be disseminated. Comments and suggestions on papers published in the Bulletin are welcome from the wider public and will be published in future issues. The scope of the bulletin includes dissemination of information on developments, the regulatory policy changes and initiatives; as well as news and information of interest to the members of the public.

The Research Bulletin is published on an annual basis and, as and when necessary, several volumes maybe published in any one year.

The articles in this publication are contributed by staff of the Authority and guest authors who gave permission for publication of their work. Articles of relevance to the non-bank financial sector are welcome from members of the public for future publications. Views expressed are not necessarily those of the Authority but of the authors and their contributors.

I wish to acknowledge all our guest authors and the regulated NBFIs, Board, Management and Staff of NBFIRA for working diligently in providing all the information required to make this publication a success.

The document is only published as a soft copy on the Authority's website in view of cost considerations.

Ramasedi O. M (Mr.)
Chief Executive Officer

Mandate

The Regulatory Authority derives its mandate to regulate and supervise the non-bank financial institutions (NBFIs) from Section 8 of the NBFIRA Act (CAP46:08). In terms of the NBFIRA Act, the principal object of the Regulatory Authority is to foster the following:-

- Safety and soundness of the NBFIs;
- The highest standards of conduct of business by the NBFIs;
- Fairness, efficiency and orderliness of the Non-Bank Financial sector;
- Stability of the financial system; and
- Reduction and deterrence of financial crime.

Vision, Mission And Values

To support its fundamental and principal object, the Regulatory Authority subscribes to the following vision, mission and values statement in order to embrace a culture of a high performance organization.

Vision: To be an efficient and effective regulatory and supervisory authority in line with international best practices.

Mission: To regulate and supervise the Non-Bank Financial Institutions for the purpose of contributing towards financial stability.

Values:-

Integrity	We adhere to the highest ethical standards.
Transparency	We are open and frank in our operations.
Fairness	We consistently promote equal treatment in our dealings with all stakeholders.
Accountability	We are responsible to our stakeholders.
Diligence	We are thorough and persistent in the execution of our duties.

Editorial Commentary

The 2018/19 Annual Research Bulletin is themed around developments, policies and practices that support the Authority in executing its mandate.

The objective of this issue is to provide insights into the Authority's role of regulating the capital markets and its market players, thereof, in the context of the evolving global trends. It takes into context the fourth industrial revolution brought about by blockchain technology in the institutions and delivery of capital markets services. Furthermore, the report reflects on performance of the domestic capital markets. All articles were prepared by staff and guest authors of the Authority.

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The following four articles were authored and are published with the express permission of the CEO, of Botswana Stock Exchange, Mr Thapelo Tsheole. Though the articles were published in the local newspapers in the year 2018, they are being published in this document to underscore their importance and to mark a significant milestone in the history of the Botswana capital markets.

Demutualization And The Evolution Of Stock Exchanges

INTRODUCTION

Stock Exchanges are vital enablers of economies in that they facilitate the transfer of capital from economic agents with surplus capital to those with a deficit in order to create economic activity. In other words, stock exchanges provide a platform on which Governments and Corporates can issue securities in exchange for capital (from investors seeking returns) as well as serve as a market on which these issued securities can be traded.

Evolution of Stock Exchanges

Typically, *stock exchanges evolved through three distinct stages.* The initial stage was characterized by an informal network of brokers who would meet at a physical place and match orders from the public (buyers and sellers). This meeting of the brokers to match the order constituted a market.

The second stage of the evolution came when these networks of brokers gradually formalized into not-for-profit mutual or member-owned organizations that employed governance structures akin to those of associations or cooperatives. This stage brought about the earliest version of the modern-day stock exchange. Then, the Exchanges were established using the capital of the members (stock brokers) and in some instances with assistance of Government. During this stage the stock brokers owned the exclusive rights to trade on the stock exchange as well as the ownership rights. They even had the right to admit or reject any new entrants to the market.

As the stock exchanges grew in relative importance to their host economies, capital markets regulation evolved and strengthened, primarily to protect the interests of the investing public. Consequently, it was recognized that the brokers' exclusive rights to trade on the market ought to be separated from their ownership rights. This ushered in the third and the current stage of the evolution of stock exchanges: the age of demutualized stock exchanges. Most stock exchanges have transformed from mutual or member-owned organisation to companies limited by shares.

What is Demutualization?

Demutualization is the process of transforming from a member owned, not-for-profit, entity to a for-profit, investor-owned corporation which involves of changing the legal status, structure and governance of an entity. In the case of a stock exchange, the Proprietary Rights of the members, as well as the cash injection by Government, are converted to shares and the Exchange can subsequently be listed on its own platform.

History of Stock Exchange Demutualization

Demutualisation can be traced to a number of events paramount of which was *the liberation of the European Union (EU) capital markets'* regulation as prescribed in the EU Council Directive 93/22/CEE of 10 May 1993 on investment services in the securities field. The directive opened up access to stock exchange membership and financial markets in the EU to authorised firms other than stock brokers. That is, stock exchanges could also be owned by regulated market participants. As a result, this led to the demutualization of the Stockholm Stock Exchange (SSE) in 1993, the first Exchange to do so. From the 1990s, demutualization gained prominence as a way of enhancing the fortunes of stock exchanges. Following the demutualization of the SSE in 1993, more stock exchanges have followed suit especially in developed markets.

Reasons for Demutualisation

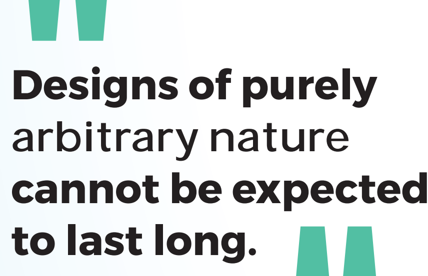
Broadly speaking stock exchanges demutualize because mainly for the following reasons:

a. Improvement of governance structures – demutualization helps in streamlining decision making by separating trading and ownership rights as well as adopting international best practise with regards to the constitution of the board of directors.

b. Access to capital– broadening access to capital needed for investment in ever improving technology (electronic trading and clearing and settlement systems), seek innovation in technology and services as well as acquire other markets, products and services.

The turn of the 20th century brought with it rapid progress in the development of technology. Consequently, stock exchanges looked towards electronic trading and settlement platforms. It was then that the open outcry trading method began to be replaced by the automatic trading system (ATS). This, coupled with the strides in the telecommunications, meant that stock exchanges could serve customers from outside their countries. Stock exchanges could list companies (primary or secondarily) from anywhere in the world and investors from anywhere in the world could trade on any exchange without having to be at the market physically. Therefore, the open-outcry floor based method of trading shares gradually became a thing of the past.

Competition amongst stock exchanges increased and they had to evolve and adapt in order to survive. This meant that Exchanges had to adopt corporate governance structures that rendered them agile enough to manoeuvre the competitive environment. Moreover, stock exchanges also needed to broaden their access to capital needed for investment. Before demutualization, stock exchanges depended on the capital of their limited members, and that of Government. It is through demutualization, and sometimes self-listing, that the stock exchanges ensured access to greater capital necessary for their growth and commercial survival. This is particularly important given the faster pace of globalisation and the rapid emergence of alternative trading platforms which threaten to lure trading activity away from regulated exchange.



The Demutualization Of The Botswana Stock Exchange (BSE)

History of Botswana Stock Exchange Limited

The modern day Botswana Stock Exchange Limited (BSEL) traces its origins to the Botswana Share Market (BSM) that was established in 1989. Back then there was only one stock broker (Stockbrokers Botswana) and it created the market by matching orders from the public on the shares of the then five listed companies. The buoyancy of Botswana's economy led to more companies and more stock brokers coming to the market and ultimately creation of the BSE in 1994 through an Act of Parliament.

Following the establishment of the BSE as a stock exchange through an Act of Parliament of 1994, which resulted in the BSE opening for trading in 1995, the exchange was owned by its members (stock brokers) through ownership of Proprietary Rights as well as the Government of Botswana. Proprietary Rights were defined in the BSE Act "as a share in the assets of the Exchange acquired for the purposes of registering as a member of the exchange in order to trade on the exchange". Historically, Government has provided majority of the financing targeted at developing the BSE infrastructure and undertaking market development initiatives, and jointly, Government and brokers have played a meaningful role of developing various facets of the BSE and the market as a whole. This includes establishing a favourable regulatory environment, driving marketing efforts and investor awareness, among others.

Commencement of the BSE's Demutualization Process

On 1 December 2015, the BSE (Transition) Act, No. 2 of 2015 came into operation to commence the process of conversion of the BSE from a mutual entity to a public company limited by shares under the Companies Act, a process known as demutualization. The BSE Transition Act was primarily aimed at governing this process by outlining the details of conduct of the BSE whilst it is undergoing conversion, following conversion, and defining the powers of the relevant stakeholders overseeing the transition of the BSE during this period, being the Minister in the Ministry of Finance and Economic Development. It is worth noting that although BSE was regarded as a mutual entity, it was by and large a parastatal.
The Main Committee of the BSE, comprising of broker representatives and Government representatives, whose responsibility was to oversee the affairs of the BSE played a strategic role in the commencement of the demutualization. As the BSE would become a company, the BSE Act would become repealed effective the date of conversion, and in its place would be the Companies Act. The Companies Act required the promulgation of the Constitution of the BSEL as a governing document of the Exchange with respect to governance issues.

Demutualization of Other Stock Exchanges

Generally, the pace of exchange demutualization has been rapid in developed markets. Research indicates that in the fifteen years since the first demutualization in the world took place in 1993, only 21 exchanges in developed markets have demutualized. This number represents almost 40 percent of the membership of the World Federation of Exchanges (WFE). In contrast, the pace of demutualization in emerging markets has been relatively slower. A report published by the International Organisation of Securities Commissions (IOSCO) in 2014 showed that only 5 jurisdictions out of a total of 76 emerging market jurisdictions had completed demutualization.

The foregoing demonstrates the difficulty with which this process is accomplished given the diverse interests of the parties involved. In Africa, as at June 2018 only 6 stock exchanges amongst the 28 members of the African Securities Exchanges Association (ASEA) were demutualized. BSE became the 7th.
Valuation of the BSE.

Some of the heated issues that delay demutualization include the allocation of shareholding in the new company by way of converting the Proprietary Rights (ownership of the brokers) and the capital injection by Government into shares on the company. By and large, the BSE has operated with just four members for a long time, each having a certain number of Proprietary Rights amounting to various amounts. Government has financially supported the Exchange for many years by way of a subvention, majority of which has gone towards the development of the BSE's technology infrastructure and initiatives around market development. For purposes of demutualisation these investments by both stock brokers and the Government had to be converted into shares in the BSEL.

Following international best practise, the Main Committee of the BSE appointed an independent consultant in 2017 to determine the value of the BSE and attribute shareholding of the BSE between the brokers and Government, and among the brokers as individual shareholders.

Determining the Allocation of the BSE Limited' Shareholding

The Transition Act, provides that "the shareholding of the Company shall be open to Government, securities brokers, employees of the Exchange and members of the public...". This formed the basis for apportioning the share capital of the BSE. However, an independent valuation by an independent consultant was to provide the appropriate, independent and objective basis for such allocation and subsequent determination by the Minister of Finance and Economic Development.

> **The Transition Act, 2015 expands shareholders** of BSE beyond Government and Securities brokers

The exercise of determining the share capital of the BSE, the value of the BSE and the attribution of shareholding in the BSE was completed in November 2017, by a consultant appointed through an open international tender which was impressively contested for. This was an impressively shorter period of time from the commencement of the Transition Act, which was just under 24 months.

As per the provisions of the Transition Act, the Minister had the power to determine the shareholding of the BSEL, and in this instance the independent valuation and share attribution report merely provided guidance, anchored on fundamentals, independence and objectivity, to this crucial decision. Perhaps, owing to the meticulousness of the report, the Minsister approved the shareholding of the Exchange as presented in the report, paving a way for each of the four brokers to then take note of their individual shareholding on the basis of the number of Proprietary Rights held by each. This approval by the Minister signalled the commencement of the conversion of the stock exchange by way of registration of the company by Companies and Intellectual Property Authority (CIPA).

On 2 August 2018, CIPA completed the registration of the stock exchange as a public company limited by shares under and in accordance with the Companies Act. The date will go into the memoires of history as the date of full demutualization of the exchange to a company called Botswana Stock Exchange Limited (BSEL). In line with Section 12 of the Transition Act, the BSE Act has been repealed.

From Botswana Stock Exchange (BSE) The Parastatal To BSE Limited The Company

Transition from Parastatal to Company

The full demutualization of the exchange to a company called BSE Limited represented a historic milestone for Botswana and the capital market as a whole. Upon reflection, this has been a fairly shorter process, and one that was characterized by diplomacy and a concerted mission by the management of the exchange, the members of the exchange and Government of Botswana to modernize the domestic capital market. It is perhaps important to note that it happened at the time that the exchange was one-year shy of its 30 years of existence. This evolution elevated the position of the BSE in the African continent, as just a few of the 28 members of the African Securities Exchanges Association (ASEA) servicing 32 countries in Africa, have demutualized whilst just 4 have proceeded to self-list.

Arguably, the milestone was worth undertaking looking at the various facets of the organisation itself and the need to promote the competitiveness of the exchange in the face of global competition and its internationalization strategy.

The BSE was converted to a Government Parastatal through an Act of Parliament in 1994, having operated as an informal share market. In the earlier years, the BSE was mainly funded by Brokers through the purchase of Proprietary Rights from time to time. In subsequent years, Government started funding the exchange through a subvention primarily financing the capital projects of the exchange and its market development activities. This investment gradually translated into improved performance of the market which positively impacted the performance of the organisation. In 2012, the exchange moved from negative profitability position and has been generating profits each year since then.

Balancing Public Interests and Profit Motives

Traditionally, stock exchanges are viewed as institutions for public good and clearly, the BSE, being a Government Parastatal (statutory body, member exchange) was seen as a national strategic asset that operates for the broader and more inclusive benefits of all Batswana. This perception was expressed in the various activities that the exchange has undertaken, which were largely undertaken to promote the reach of the exchange, the inclusion of all in the stock market and without due priority to lament on the cost or expect a return on investment.

A certain scholar, Rydzewska (2014), contests that as a public good an exchange exists to provide three basic functions to the public. These are; (a) allocation – stock exchanges are a platform on which limited capital is allocated to worthy investments; (b) valuation – stock exchanges assist in the price discovery of the listed securities and this is achieved by ensuring transparency and nurturing liquidity in the market; and (c) control – stock exchanges are also tasked with ascertaining that shareholders have meaningful control of their companies by protecting and upholding the rights of the minority shareholders.

These three functions ought to be equally pursued by the exchanges, because if there is inefficiency in one function there will be market imbalances. An analogy would be an instance where there is poor disclosure by issuers (because of lax regulation by the exchange) which leads to inaccurate market pricing, which in turn leads to inefficient allocation of resources on the market. Such has the risk of distorting rewards in the market and further threaten the stability of the market.

In relation to the foregoing, a transition from a Parastatal to a fully demutualized exchange operating as a Company or a Corporate poses one fundamental challenge in that the exchange has to reconcile being responsible for providing a public good with maximizing profit for its shareholders. The primary sources of income for exchanges are listings and annual sustaining fees as well as trading fees. If the exchange is to impose the burden of responsibilities and obligations on its issuers in favour of protecting the investors, it may crowd out the issuers and therefore lose out on the listings and annual sustaining fees, and thereby fail to maximize shareholder return. On the flip side, there is a possibility that the exchange might relax its regulation so as to attract and keep issuers for their fees, much to the detriment of the investors.

As such, it is important that demutualization efforts are preceded by bolstering and adequately capitalizing the supervision of the capital markets. Most markets have set up standalone public agencies, regulatory authorities and securities exchange commissions that regulate the capital markets. In the Botswana market, the Non-Bank Financial Institutions Regulatory Authority (NBFIRA), being the regulator of BSE Limited, with the NBFIRA Act is well equipped to accommodate this regulatory conundrum of ensuring adequate supervision of a stock exchange pursuing for-profit objectives whilst balancing the protection of investors and ensuring adequate compliance by listed entities.

As a way of improving the financial sufficiency of exchanges and cushion the heavy reliance on listing fees, annual sustaining fees and trading fees, some stock exchanges have sought to increase revenues by expanding their product offerings to include post-trade services as well as information and data services. This has helped to diversify exchange revenue from the main sources.

BSE Limited Post Demutualization

The move towards corporatisation of the BSE by way of demutualization has been well thought out in the manner in which the exchange has gradually been behaving like a corporate for this eventuality. The exchange has successfully balanced the public interests and profit motive for some time. The BSE has over the years been embarking on initiatives to diversify its revenue streams, whilst putting in place robust programmes to equally rationalise expenditure. In 2014, the BSE signed several data vending agreements with international data vendors. Besides promoting the visibility of the BSE and enhancing the reach of market statistics, these have generated revenue for the exchange. This area represents an immense potential for the BSE, which owns the Central Securities Depository Botswana (CSDB). The CSDB also functions as a data repository with respect to listed and unlisted instruments and can offer a broad range of cash generating services at its maximum capacity. Undoubtedly, pre and post-trade data services represent a growing income avenue for the exchange.

Notably, there has been modernization also in the manner in which the exchange has undertaken its market development initiatives. Until 2016, the BSE would undertake public roadshows across various places in Botswana primarily in various public arenas and these would be characterized by entertainment to pull the crowd. This was a necessary mode of execution given the low levels of awareness at the time, the myths and misconceptions about the stock market and the low retail investors participation in the stock market. As the financial literary improved over the years, along with retail participation from as low as 3 percent to 15 percent, the BSE remodelled this approach to be represented by highly targeted Open Days, still open to the general public for free and also introduced targeted annual listings and investment conference to cultivate the supply side of the market. As an institution moving towards corporatization, the remodelling of these highlighted activities was inevitable as, as a corporate, the focus will be on striking an optimal balance between attaining shareholder expectations without compromising the broader reach and inclusion of everyone in the stock market, more so that Government remains the majority shareholder in BSE Limited.

All these aspirations of becoming a competitive corporate and a world-class securities exchange are enshrined in the strategic plan which spans 2017 to 2021. Evidently, the design of the strategic plan had foresight to the corporatization of the exchange. The strategies are highly cost and revenue conscious, there is greater indication of product and services diversification, a shift towards optimising the technology infrastructure, commitment towards building a conducive regulatory environment, human capital uplifting and traction towards previously unchartered territories such as the derivatives market. The BSE Limited, however, will refine its 2017 to 2021 Strategic Plan to capture post-demutualization initiatives.

Self-Listing – The BSE Limited Perspective

History of Self-Listing
More often than not, demutualization is just an interim step for many exchanges in their evolution. Post demutualization, the exchange can evolve further by listing on its own platform, what is referred to as self-listing. Globally, a number of exchanges progressed to self-list after they demutualized as a way of further enhancing their governance and competitiveness as a listing expands the shareholder base and enables further access to capital.

Early examples of exchanges that underwent a self-listing are the Stockholm Stock Exchange AB in Sweden, Australian Stock Exchange, Hong Kong Stock Exchange and Singapore Stock Exchange. As time progressed Deutsche Bourse, London Stock Exchange, Euronext and NASDAQ followed suit.

The same phenomenon has been experienced in Africa. For example, the Johannesburg Stock Exchange was the first to self-list in 2006, following its demutualization in 2005. The Nairobi Securities Exchange self-listed in 2014 in the same year that it demutualized. The most recent self-listing in Africa was by the Dar Es Salaam Stock Exchange in 2016, a year after its demutualization in 2015. Notwithstanding, few of the demutualized exchanges in Africa, such as Zimbabwe Stock Exchange, Stock Exchange of Mauritius, and Bourse de Casablanca remain unlisted. The BSE Limited as a newly demutualized stock exchange, is also unlisted. A handful, especially those that were established in recent times, such as Rwanda Stock Exchange, Trop-X (Seychelles) and Lesotho Stock Exchange were registered from the onset as companies limited by shares and have never had to experience the transition from a mutual to a demutualized entity. Perhaps, with this background, it's worth exploring a key perspective with respect to self-listing especially that it is the only next and ultimate stage in the evolution of BSE Limited. This perspective is to do with maintaining a balance between serving the regulatory functions and pursuing the corporate objectives without jeopardy to stakeholders.

Benefits of Self-Listing
Transformation of stock exchanges is undertaken primarily to revitalise their business models. Evidently, the listing of stock exchanges has transformed their business models extensively. Although demutualization is undertaken to alter the ownership of stock exchanges, in some cases significant ownership stakes were often retained by previous member firms, particularly in exchanges that were predominantly member owned from the onset. Therefore, the fundamental governance structure of exchanges was not significantly impacted in such cases. Self-listing and the subsequent dispersion and dilution of ownership of exchanges have immensely impacted the governance of stock exchanges.

A self-listing is a privatisation of the exchange. Experience has shown that privatisation brings about a broader mix of shareholders ranging from institutional investors, retail investors, listed companies, technology companies, the public at large, and in some cases foreign investors. Often, as is common practise in most government-driven privatisation efforts, foreign institutions might become owners of newly privatised entities to a certain extent.

In the context of BSE Limited, demutualization has ushered the exchange into an era of corporatisation. This is particularly necessary as the exchange itself is mandated to regulate corporatized institutions, being listed companies. Corporatisation brings about significant expectations from the shareholders of BSE Limited. One such is the focus on maximising the profits and value of the exchange - a mission that the exchange will continually pursue should it undertake a self-listing.

The listing of a stock exchange strongly accentuates the business orientation of the exchange. As with any listed company, the exchange can be expected to be more value oriented, more efficient, more innovative and growth oriented and therefore highly motivated by short-term profit maximisation. Where the open ownership attracts outside investors, they will expect a return on their investment that is commensurate with the return they could earn on their investment alternatives. However, this probably will not be the case if the owners are insiders (members, issuers) with other interests in the exchange than outsiders.

BSE Limited as a Self-Regulatory Organization (SRO)
A self-listing of the exchange presents such conundrums as how does an exchange maintain a balance between serving its regulatory functions and pursuing its corporate objective without jeopardy to its stakeholders?

Common practise is to delegate a demutualized stock exchange a Self-Regulatory Organization (SRO) status. An SRO is "an organization whose object is to regulate the operations of its members or of the users of its services and include the organizations that may be recognised as such".

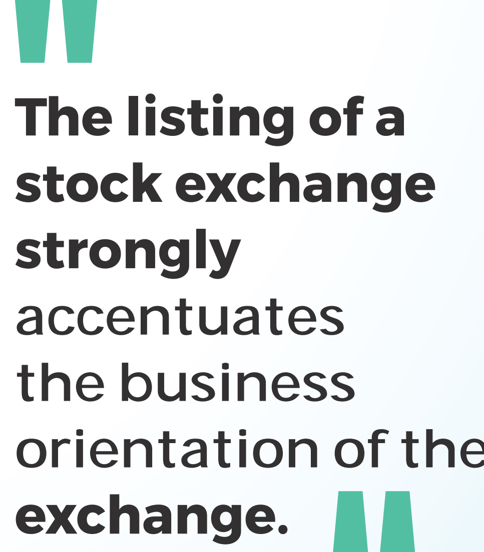
Under its SRO status, the exchange maintains its primary regulatory functions of setting rules, conducting surveillance, and enforcing the rules and these may be financially demanding functions, particularly in the context of an increasingly competitive environment. However, not doing these functions can be detrimental to the reputation of the exchange and the definition of the securities market as a whole, whereas doing them may be unfavourable to the value maximisation objective of the exchange.

A number of approaches have been undertaken to deal with this, for example, when the Stockholm Stock Exchange (SSE) demutualised, it set up an independent Disciplinary Committee to handle compliance of the SSE with the listing rules and also to decide about enforcement against issuers and members. Before, these functions had been handled by the board. The stock exchange law was later amended to require that all authorised exchanges organise such committees. When the Johannesburg Stock Exchange (JSE) demutualized and self-listed the JSE equities rules were amended to include the establishment of the SRO Oversight Committee which was the Board Sub-Committee responsible for overseeing the issuer regulation and market regulation functions of JSE Limited. Subsequently, compliance of JSE Limited with its listings requirements was seconded to the financial market regulator, the Financial Services Board (FSB). These two examples represent some of the strategies used to work around promoting the independence and objectiveness of the exchange with respect to its regulatory function of other listed entities and members, the compliance of the exchange to its own listings requirements, to ensure the exchange discharges its functions in a manner that is transparent and equitable to all.

Regulating the SRO

The Non-Bank Financial Institutions Regulatory Authority (NBFIRA) regulates BSE Limited and the NBFIRA Act provides that an institution such as BSE Limited can be declared a SRO. However, if declared, the status will not absolve the exchange of its supervision by NBFIRA and NBFIRA will continue with its role of approving any rules, including the amendment of listings rules. Section 36 of the NBFIRA Act outlines this relationship and due process by SRO in detail.

Recent developments are that NBFIRA is undertaking this assessment regarding BSE Limited being declared a SRO to enable them to make a recommendation to the Minister of Finance who will make this declaration. The declaration of SRO status will evolve and possibly expand, in line international best practise, when the BSE progresses to the next phase of its development, which is a self-listing at a future point in time. International best practice suggests that once BSE Limited is self-listed, it will continue to regulate companies and securities listed on the BSE, the listings and trading platform, whereas NBFIRA regulates BSE Limited with the same set of listing requirements that BSE Limited uses to regulate companies listed on its platforms.



What Is An International Financial Services Centre

– By Mojadi Kwerepe

International Financial Services Centre (IFSC) refers to the entirety of international financial services companies and their respective approved financial operations, and the institutions which have been appointed to regulate and supervise such companies.

What is an IFSC Company

An IFSC company in the context of Botswana is a company registered and licensed in Botswana to do business with people resident outside Botswana. Such a company trades in foreign currencies and uses the Pula currency only for domestic operating costs such as office and residential rent, office supplies, staff salaries, payment for utilities etc.

Who Licenses and Supervises IFSC Companies in Botswana

IFSC companies are licensed and supervised by either the Non-Bank Financial institutions Regulatory Authority (if it is a non-bank financial institution (NBFI) or a holding company for a NBFI(s)) or Bank of Botswana (if it is a bank or a holding company for a bank(s)).

How is the Tax Structure for an IFSC Company?

(i) Corporate tax for IFSC companies is 15 percent whereas other companies are taxed at 22-25 percent.
(ii) IFSC Companies are also exempted from withholding tax ad capital gains tax

Why is the Corporate Tax for an IFSC Company lower than that of Other Companies?

The lower tax rate for IFSC companies is meant to, among others:
(i) Attract foreign direct investment into the country
(ii) Promote skills transfer to Batswana and;
(iii) Create employment opportunities in Botswana

How does a Company Attain IFSC Status?

Currently a company gets classified as an IFSC company following its approval by the IFSC Certification Committee which is appointed by the Minister of Finance and Economic Development (the Minister). The Committee's main functions are as follows:
(i) Processing of applications for a tax certificate referred to it by the Botswana Investment and Trade Centre;
(ii) Recommending to the Minister, the grant and revocation of tax certificates, including any conditions to be attached to a particular tax certificate; and
(iii) Recommending to the Minister, any matters related to the operation of the IFSC.

What General Conditions are IFSC Companies Subjected to?

The following are the general conditions IFSC companies are required to abide by, in order to continue to benefit from the low tax regime:
(i) An IFSC company is required to keep trading records and accounts;
(ii) The company's records and accounts, and the records and accounts of the company's other trading operations, if any, are to be available for inspection by the Commissioner of Taxes or any other authorised officer of the Botswana Unified Revenue Services (BURS);
(iii) For tax purposes, including allowances and charges in respect of capital expenditure, the carrying-on of the trading operations to which the certificate refers, are treated as a separate trade distinct from all other activities, if any, carried-on by the company issued with a tax certificate;
(iv) The company should not, in the course of the trading operations to which a tax certificate

refers, either directly or indirectly, acquire assets or receive services from or dispose of assets or provide services to or for a connected person, unless all such transactions are on an arm's length basis:
(v) Business operations conducted under the tax certificate are required to be any of the financial services prescribed under Section 138 of the Companies Act;
(vi) The company is required to achieve and maintain a prescribed minimum employment level within a specified time period, a proportion of whom should be Botswana citizens, as would have been specified in the Project Proposal approved by the IFSC Certification Committee;
(vii) The company is subjected to prudential and supervisory requirements and conditions as the designated regulator may specify from time to time;
(viii) Any material change in the control of the company, including shareholding, are to be pre-cleared with the designated regulatory authority and the Botswana International Trade Centre;
(ix) IFSC company is required to commence business and have a physical presence in Botswana within one (l) year from the date of approval by the designated regulator;
(x) IFSC company is required to ensure that after two (2) years following the year of
accreditation, tax returns are filed with the BURS;
(xi) IFSC company is prohibited from carrying out any activity, which has, or will have an adverse effect on the use or development of the Botswana International Trade Centre.

IFSC Accredited Companies Dominated Employment Creation In The Capital Markets Sector In Botswana For Period Ending March 31, 2019

– By Mbiganyi Modise

What is an IFSC Company and Staffing

The Regulatory Authority has assessed the rate of employment creation by the Capital Markets Sector in Botswana as at March 31, 2019 and the study has shown that the sector is dominated by citizens who are highly qualified and experienced to meet the requirements of the Securities (Institutions Licensing) Regulations, 2017 and other Financial Services Laws. As at March 31, 2019, the Capital Markets Sector in Botswana had employed a total number of 477 (See Figure 1 below) staff members. As at the end of the reporting period, the locals constituted 98% of the total number of employees in the sector. Only a minority of non-citizens are employed in the Capital Markets sector, constituting 2% of the employees.

Governance

In terms of the requirements of the Financial Services Laws, every Capital Markets industry player is compelled by law to appoint the following key personnel; Managing Director, Compliance Officer, Internal Auditor and AML/CFT Compliance Officer. These roles are played by separate individuals and they are not supposed to conflict each other. This has contributed to the employment creation rate in the financial services sector by separating these functions. Types of Institutions in the Capital Markets sector currently consists of the following industries which have been licensed and some approved by NBFIRA; Asset Management, IFSC accredited companies, Management Companies, Investment Advisors, Securities Brokers, Trustees and Custodians.

Market Share of Employees

The major sector contributor to the employment creation in the Capital Markets sector is the IFSC accredited companies, which had employed 175 individuals out of the 477 total employees as at March 31, 2019. This constituted 37% of the total employees in the Capital Markets sector. Secondly came in Asset Managers at 26%, translating into 122 employees. The third contributor were Investment Advisors which stood at 17%, translating into 82 number of individuals employed. The remaining least employers were securities brokers and securities infrastructure business, who both contributed 20% of the total employment in the Capital Markets sector.

Assets

As at end of February 2019, Asset Managers and Asset Management Companies in Botswana had assets under management amounting to P48 Billion and this continues to evoke smiles on the faces of Managing Directors/CEOs of Fund Managers, who are all citizens. Citizen Managing Directors have been entrusted with the Capital Markets sector in Botswana. This has also contributed to the market confidence, for citizens to be at the helm of this very sophisticated and volatile sector. The Stock Exchange and the Central Securities Depository have both employed 100% citizens.

Figure 1 -Number of Employees in the Capital Markets Sector

The Botswana Capital Markets Soundness Report 2017

– By Gosego Chilume

INTRODUCTION

This paper presents an analysis of the Botswana Capital Markets industry financial soundness for the year ending December 31, 2017. The paper utilizes information published by the Botswana Stock Exchange and information submitted to the Regulatory Authority through regulatory returns of regulated capital market players. This paper focuses on the capital markets and capital market players' performance and financial stability issues.

Equity Market Performance

The 2017 Botswana Stock Exchange Annual Report reported a decline of 5.8 percent in the Domestic Company Index, to end the year at 8,860.1 points from 9,400.7 points in 2016. This was as a result of a slowdown in the performance of the Retail & Wholesaling, Banking, Financial Services & Insurance and the Security Services sectors, contributing 9.2 percentage points to the depreciation of the DCI. The other sectors contributed positively an aggregate contribution of 3.4 percentage points.

The Foreign Company Index also registered a marginal decrease of 0.7 percent, closing the year 2017 at 1,574.9 points and winding down the marginal increase of 0.9 percent recorded in the previous year. The Foreign Equity Board is dominated by the Mining and Minerals sector, and accounted for 94.4 percent of the foreign companies' market capitalization, contributing 0.84 percent points to the FCI's depreciation.

DCI
DECLINED BY
5.8%%

Table 1: Market Performance Statistics

	2016	2017
Index Performance		
DCI*	9,400.7	8,860.1
% Change	(11.3)	(5.8)
FCI**	1,585.8	1,574.9
% Change	0.9	(0.7)
Liquidity		
Turnover (P'Mn)	2,138.7	2,144.4
Average Daily Turnover (P'Mn)	11.5	11.5
No. of shares Traded (Mn)	653.1	655.6
Market Capitalization		
Domestic Companies (P'Mn)	46,571.9	44,408.1
Foreign Companies (P'Mn)	374,741.2	373,735.7
Total (P'Mn)	421,313.1	418,143.8

Source: Botswana Stock Exchange

Note: * Domestic Company Index

** Foreign Company Index

Bond Market Performance

The table below indicates that the value of bonds traded increased to P536.7 million in 2017, from P483.9 million in the prior year. Market liquidity was dominated by Government Bonds, accounting for 90.5 percent of total turnover. Corporate Bonds also increased to P50.8 million in 2017 from P37.2 million in 2016. Corporate bonds accounted for the majority of the quantity of bonds listed.

Table 2: Bond Market Performance

	2016	2017
LIQUIDITY (P'Mn)		
Government Bonds	446.7	484.9
Corporate Bonds	37.2	50.8
Total	**483.9**	**535.7**
MARKET CAPITILISATION (P'Bn)		
Government Bonds	8.3	9.1
Corporate Bonds	3.9	5.2
Total	**12.2**	**14.3**
NUMBER OF BONDS LISTED		
Government Bonds	6	5
Corporate Bonds	35	38
Total	**41%**	**43%**

Source: BSE 2017 Annual Report

Performance of Capital Markets Players

The number of licensed NBFIs increased to 64 in 2017, compared to 53 licenses issued in the prior year. The increase in the number of licenses was largely attributable to investment institutions who increased by 48% during the year.

The Capital Markets players registered an 82% increase in revenues to P3 billion in 2017 from P2 billion in the previous year. IFSC accredited companies continued to dominate the market with a market share of revenue of 73 % in 2017, compared to 60 % in 2016.

Table 3: Revenues of Capital Market Players

Category	Revenue 2016 P'(Million)	Revenue 2017 P'(Million)	% Change
SIBs*	37	41	10.8
Securities Intermediaries **	805	1010	25.5
IFSCs	1,272	2,790	119.3
Total	2,114	3,841	81.7

Source: NBFIRA
Note: *Securities Infrastructure Businesses (BSE and CSDB)
** Management Companies, Asset Managers, Securities Brokers (excludes Trustees and custodians)

Net profit of capital market players increased by 27% from P1.1 million in 2016 to P1.3 million in 2017. The securities intermediaries registered the highest profit growth of 217%, albeit from a lower base compared to IFSCs.

Table 4:Net Profits of Capital Market Players

Category	Net Profit/Loss as at December 31, 2016 P'(Million)	Net Profit/Loss as at December 31, 2017 P'(Million)	Percentage Change
SIBs	9	9	0
Securities Intermediaries	93	295	217
IFSCs	991	1,086	9.6
Total	**1,093**	**1,390**	**27.2**

Source: NBFIRA

During the year ended December 31, 2017, 21% representing eight (8) NBFIs made losses and all were in the securities intermediaries' category.

Table 4:Net Profits of Capital Market Players in December 31, 2017

Category	No. of firms with losses	Total Firms	% of Total NBFIs
SIBs	0	2	0
Securities Intermediaries	8	31	26
IFSCs	0	5	0
Total	8	38	21

Source: NBFIRA

Net Assets

During 2017 the net assets increased from P7 billion in 2016 to P11 billion in 2017, primarily driven by a high increase in IFSCs which doubled in value. Capital positions of capital market players fell from P8 million in 2016 to P6 million in 2017. Similarly, when expressed as a percentage of assets the capital ratio fell slightly from 5 % to 4% in 2017. The fall in the capital ratio reflects slower capital growth of IFSC NBFIs relative to their asset base. Refer to Table 6 below.

Table 6: Capital Positions of Capital Market NBFIs

Category	Net Assets / Liabilities (1)		Total Assets (2)		Capital Ratio (%) (3) = [(2) −(1)] /(2)	
	2017	2016	2017	2016	2017	2016
SIBs	8	7	100	91	9	9
Securities Intermediaries	5,891	5,135	6,286	5,496	1	1
IFSCs	4,785	2,195	10,460	9,406	5	8
Total	**10,684**	**7,337**	**16,846**	**14,993**	**4**	**5**

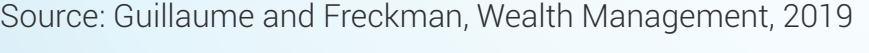
Source: NBFIRA

The Markets Must Be Crazy

– BY BOPELOKGALE SOKO

Pension funds and other institutional investors across the globe experienced weighty erosion of their asset values in 2018. Global pension assets declined by an average of 3.3 percent compared to the growth rate of 13.1 percent recorded in 2017 (Thinking Ahead Institute), as a result of negative growth rates experienced by most of pension funds across the globe. Even the big giants US, UK and Japan pension funds were affected by the decline at the rate of 2.6 per cent, 6.3 percent and 0.5 percent respectively (Thinking Ahead Institute). Botswana pension funds did not escape as they also lost 3.7 per cent of their total values in 2018 compared to an increase of 9.2 percent during 2017.

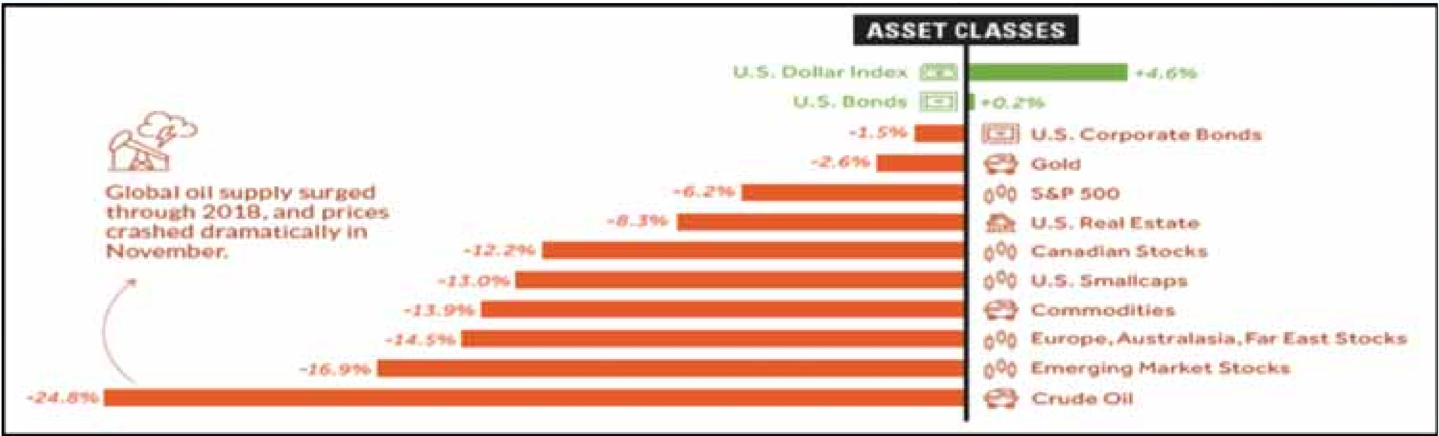
The total loss in global pension assets value is estimated to be USD 1 388 billion. What drove the seemingly rampant fall in pension assets values? Poor market performance. Are the markets crazy? That is a lot of money by any standard! It is equivalent to GDP of some countries (e.g. Guinea- Bissau: USD1350, and Solomon Islands; USD1 298) and a lot more than the GDP of other countries (e.g. Palau, Sau Tome and Principe, the Comoros). The markets must be really crazy! What happened?


Source: Guillaume and Freckman, Wealth Management, 2019

The year 2018 was uncharacteristically a down year for all major markets. All the world major indices ended the year 2018 in the red. This pitiable market performance dragged the MSCI All-Country World Index down by 11%, its biggest annual drop since the 2008 financial crisis (MSCI, 2019). The MSCI emerging markets suffered a much bigger blow with a decline of -14.6% during the same period (MSCI, 2019). Figure 1 shows that almost all markets recorded negative returns in 2018, except for a few in emerging markets.

Aren't investors supposed to be rational? Why didn't they run to "safer places" to avoid the losses? Apparently there were little to no safer place this time. All assets classes, with the exception of cash, irrespective if their level and direction of correlations, were affected by a "bug", living investors with "nowhere to hide". (This was a reverse of the 2015 market performance where all assets classes, with the exception of cash, bequeathed investors with handsome returns). See Figure 3 which shows the average world returns by asset class. According to Figure 2, even commodities and alternative investments registered negative returns in 2018.

Figure 3: Global Asset Class Returns: 2018



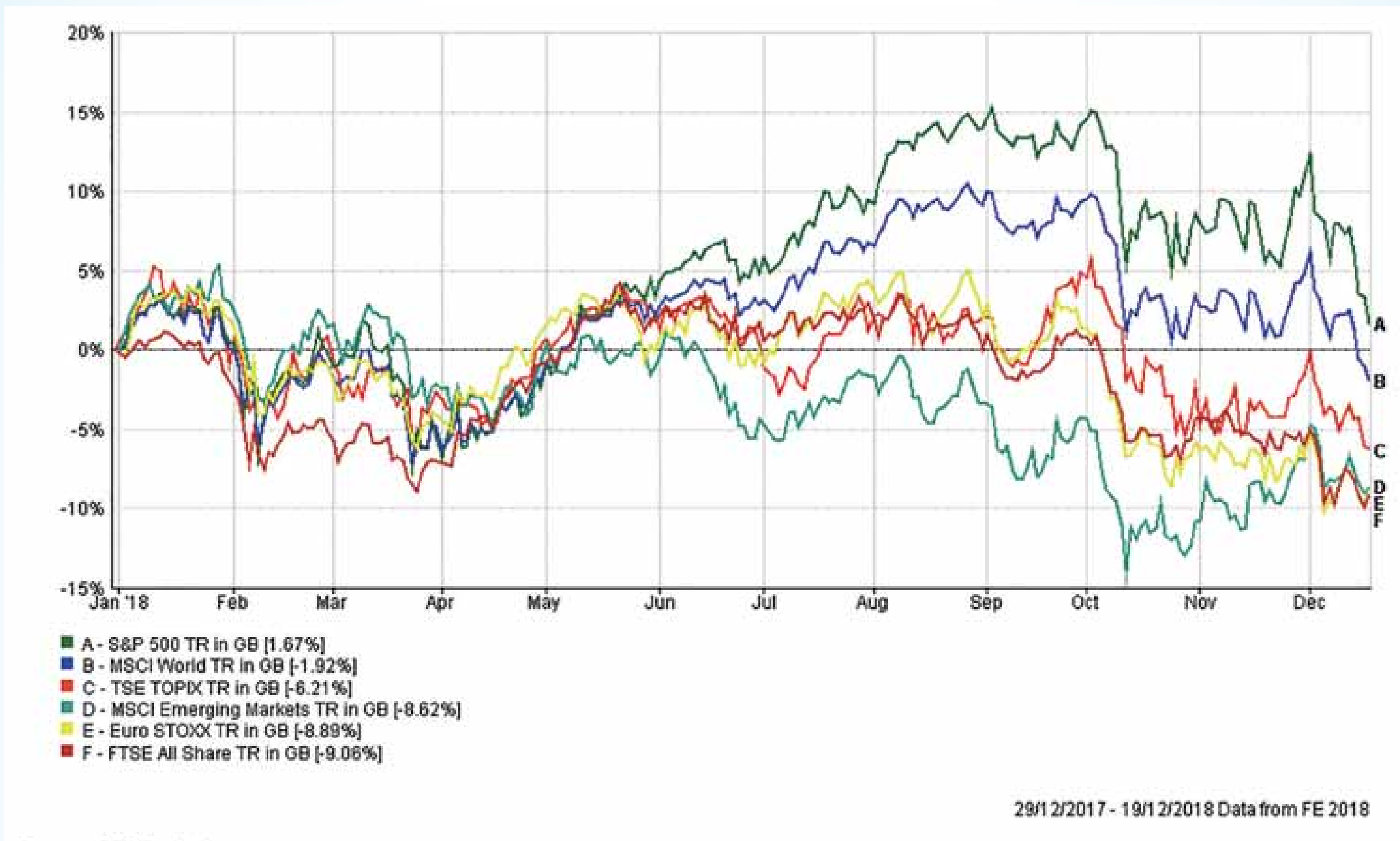
Source: Desjardines J, Visual Capitalist, 2019

Even though all assets classes performed poorly in 2018, the major contributing factor in the erosion of pension funds' assets values can be traced to the deficient performance in the equities market. Generally, as long term investors, pension funds asset allocation is weighty on equities. For example, the OECD Global Pension Statistic, 2018 published by OECD reported that pension funds in Namibia, South Africa, and Mauritius allocation to equity stood at, 65%, 72% and 56% respectively. In the same way, Botswana pension funds allocation to equities stood at 68% of the total portfolios (including offshore equity).

Similar asset allocation pattern is observed in developed markets; Hong Kong, 63%; Chile 41% and Australia 49%.

Consequently, being heavy weights in the portfolios, equities poor performance dragged the performance of the whole portfolio down, resulting in loss of value of the assets.

Figure 4: Performance of Major Stock Market Indices



Figures 4 and 5 show the performance of major stock markets indices and Botswana DCI, respectively. Both Figures indicate that the global stock markets, DCI included, experienced some declines in October 2018, a decline which resulted in a catastrophic landing of the markets as they close 2018.

Figure 5: DCI performance, 2018.

Source Tradingeconomics.com online 2019

Source Tradingeconomics.com online 2019

But what were the markets reacting to? The year 2018 was marked by political and policy controversies from all corners of the globe; First the United States of America. The US is the biggest economy in the whole World with GDP $20.1 trillion, followed at a distance by China at $14.1 trillion. There was a notable Power struggle between the White House and the FED during 2018. The Trump Administration tax cuts administered under the new and controversial Tax Cuts and Jobs Act, 2017, resulted in the Federal Reserve, under the leadership of Jerome Powell, hiking interest rates in an endeavor to alleviate potential inflation that may arise as a result of the tax cuts. This action by the FED, did not sit well with the Trump Administration resulting in a "tug of war" between the FED and the White House, with the public fearing that Powell may be fired. Trump tweeted: *"The only problem our economy has is the Fed. They don't have a feel for the Market, they don't understand necessary Trade Wars or Strong Dollars or even Democrat Shutdowns over Borders. The Fed is like a powerful golfer who can't score because he has no touch - he can't putt!*

The Government Shutdown was triggered by the President Trump's refusal to sign the Budget Funding bill which did not include USD 5 billion he needed to finance the Mexico border wall. Again this triggered a "war: between Congress and the White House, creating uncertainties in the investment space. The China – US Trade war became heightened during two countries' imposing trade tariff on each other imports.

Italy's Political Instabilities.

The last three Months of 2018, saw Italy's economy falling in to a recession as a result of the political unrests and the deadlock with the EU over its government spending which were not in line with the EU budget deficit rules. The continued unrest will obviously result in increased government borrowing and dampen business sentiment. The investing public is worried about the country's weak fiscal position and the stagnant economy.

Brexit

Still in Europe, there is a lot of uncertainties surrounding Brexit. The UK was initially scheduled to leave the EU in March 29, 2019. An extension was given until April 12, 2019 and another one (which the EU said is the last extension) until October 31, 2019. The Brexit Plan had already been rejected three times by the House of Commons. Theresa May is even threating a second memorandum, which makes sense since those who voted for the move won by only 51.9%. People may have changed their minds! These uncertainties grow bigger as the date of Brexit approaches. Obvious Brexit will affect the economic performance of Britain through number of channels including the trade policies and agreements, performance of multinational companies, especially those listed on different stock exchanges. In fact, the UK Government has predicted that the decline of about 3% of GDP over the next 15 years following Brexit.

China Low economic growth

China is the second largest world economy after US. During 2018, China's economy grew at an average of 6.4%, its first weakest growth since 1990. Economists had attributed the slow growth to a number of factors including the aging population (effects of the one child policy of 1979), pressures to increase wages in order to be competitive with other economies, reduction in trade surpluses etc. The continued trade dispute with US seems to escalate the problems. Trade tariffs slows global demand for Chinese goods and adversely affect consumer confidence.

The 2018 market selloff, may be a way of the markets raising an alarm against the world political and policy controversies undertaken by the super powers during the year, which may be detrimental to economic health. As they say, markets are the barometer to economic health. Maybe the market are not crazy... they were only doing their job as economic health barometers!

Financial Technology, "Fintech" In The Field Of Financial Services

By Guest Author

The term or in fact, word "fintech" is a combination of the words "financial" and "technology". It describes the use of technological processes to deliver financial services and products to consumers.

The expression may be relatively new, however, fintech itself is not and has constantly been a key driver of innovation in financial services. For example, the internet, combined with the widespread use of devices such as smartphones and tablets, means the speed of this change has accelerated in recent years.

Early days
I first stepped foot on the trading floor of an investment bank in December 1983 when I began my financial services career at Nomura International in London, a subsidiary of the Japanese powerhouse, Nomura Securities.

Back then, the only technology, apart from the large array of telephones on each desk and the telex/fax machines in the corner of the trading room, ***were the information screens.*** These small terminals provided general and financial news from Reuters, Telerate and a system called "QUICK" that delivered price information on stocks trading in Tokyo. The luminous green displays on the cathode ray tubes had replaced magnetic tape data storage of Quotron and Ultronics which themselves had usurped the tickertape machines that hailed from the 1920's
One could contend that Reuters was a pioneer in the field. ***Paul Reuter marked the first fintech*** inflection point as shortly after moving to England he founded Reuter's Telegram Company in 1851. This was headquartered in London and began covering commercial news, serving banks, brokerage houses, and business firms.

No less a publication than the Encyclopedia Britannica wrote that:

"...the value of Reuters to newspapers lay not only in the financial news it provided but, in its ability, to be the first to report on *stories of international importance. ..."*

Reuter's agency built a reputation in Europe and the rest of the world as the first to report scoops from abroad e.g. it broke the news of Abraham Lincoln's assassination in 1865 to a shocked European audience.

As advances in overland telegraph systems and undersea cables developed Reuters began transmitting messages electrically to London newspapers as well as expanding its news coverage into the Far East and Latin America. This was a far cry from the first days when Reuters carried news between cities by Homing

Pigeon.
In the early 1980's several investment banks attempted to develop their own financial information architecture. Indeed, Nomura was one the first with a system known as "Computer Aided Portfolio Total Analysis" or "CAPITAL". As with most "first movers" in technology it was a costly system and whilst covering a selection of international economic data its financial analytics were focused on Japanese equities and government bonds.

A revolution by Bloomberg:
In the late 1980's, a small machine began to appear in trading rooms. In many cases it sat in the corner as a single screen with a keyboard and a thick user manual. It looked as if this interloper had replaced the telex and fax machines.

The new comer was "Bloomberg" and was invented by Michael Bloomberg who as a general partner at Salomon Brothers had overseen the design of strictly "in-house" computerised financial systems.

In 1981, Salomon Brothers was acquired by the commodity trading firm Phibro Corporation and Mr Bloomberg received a $10 million partnership settlement. Still interested in financial data and analytics he used these funds to develop and build his own computerised system to provide real-time market information and financial calculations.

In 1983, Merrill Lynch invested $30 million to help finance the development of "the Bloomberg" terminal computer system and after the system has proven successful with Merrill Lynch's clients it was sold to a wider audience. No less than 5000 terminals had been installed in subscribers' offices by 1986.
This, in my opinion, was the second watershed moment in fintech. Reuters and Telerate had simply provided price data. However, Bloomberg allowed one to manipulate several variables such as:

Price Source...Bid v Ask...Mid v Mid...Time Period...Constant Spread...Local or U.S. Dollar Base

The range of possibilities was almost endless and behind the incredible array of graphical (eventually in colour), and tabular data there was the silent but sophisticated beat of complex algorithms. New developments came with offshoots such as Bloomberg Tradebook (a trading platform), the Bloomberg Messaging Service, and the Bloomberg newswire via television and radio

The range of possibilities was almost endless and behind the incredible array of graphical (eventually in colour), and tabular data there was the silent but sophisticated beat of complex algorithms.

New developments came with offshoots such as Bloomberg Tradebook (a trading platform), the Bloomberg Messaging Service, and the Bloomberg newswire via television and radio were launched in 1990. Bloomberg.com was first established on September 29th, 1993, as a financial portal with information on markets, currency conversion, news and events, and Bloomberg Terminal subscriptions.

Next developments

Bloomberg continues to thrive and as ***the new century has moved toward its third decade*** there have been tremendous advances in financial education, disruptive platforms for trading, retail banking, investment and crypto-currencies.

A typical example is ***the power and reach of the applications or "apps"*** that one can download to a smart phone or link to online. These do not have to be restricted to trading bonds, equities or foreign exchange. Peer-to-Peer (P2P) sites open channels of price discovery for personal or even small payday loans or mortgages. The rise of competition has seen a dramatic reduction in rates that are charged to end users.

The internet and the evolution to 4G and soon 5G mobile technology is the next or third wave in the fintech revolution.
Such fintech tools have undermined the need for commercial banks to have an extensive branch network as personal banking apps have replaced the need to go to the branch to move money from one account to another, of the time-consuming delay of waiting for a cheque to clear. Money literally moves as fast as electrons.

Change is blowing through other areas of financial services that were once seen as dry and extremely linear in their operation. Insurance providers for car cover use "telematics-based" insurance to monitor ones driving data, where...when...speed...breaking force etc, all collected via a link between the car and a smart phone or a smart device fitted into ones car. This data can determine how much one must pay for an insurance policy. In the future, buying insurance for a full year may become obsolete it may be possible to buy insurance on a short-term or "pay as you go" basis.

This approach of conducting ***commercial activities for business to business (B2B) and business to client (B2C) is making commerce more efficient*** and its growth is undoubtedly expected to continue.

However, one should bear in mind that for every benefit that can be cited a potential risk awaits identification.

The benefits are clear to see; greater speed, convenience, efficiency, choice and a movement away from one size fits all to bespoke financial products. Risks are not so obvious. That is their nature, to stay hidden in the dark until they make their unique unpleasantness known.

If the small print on paper was an old-fashioned curse, it is now, in the electronic world maybe even more so. Ones rights and / or obligations can be buried in an online file. Whilst any decision usually has a statutory cooling off period, we can be lazy and so going back into an email or computer file may be onerous and ignored.

What about the problem of financial exclusion? Even in G7 countries there are many people that are not computer literate because of age, education or a lack of access. As fintech migrates many decisions into the ether, we risk disenfranchising several sections of the population. Steps must be taken to stop a fintech wedge splitting society.

Lastly, and perhaps ***the greatest worry is that of technology risks***. Without adequate firewalls or protections, a computer system, be at home or in the corporate world can be hacked or infected with malware. There appears to be a daily risk of cybercrime from unethical individuals to pariah states as a means of undermining the financial system of any open society.

This technology risk is especially prevalent in the dealing rooms of the main financial centres. Remote, stay at home day traders usually have strict limits placed on their activities. Although an at home risk is the rapid rise of online gambling. Where do we draw a line or at least not blur the edges between betting on a sports event as against speculating on a stock market?

In this fintech world we must ensure the risks are known and the adage of "Caveat Emptor" or "Buyer Beware" is shouted loudly and clearly!

Back ***in the dealing room the days of aggressive traders screaming orders*** in the aftermath of a key data point ***has*** almost ***disappeared.*** Huge volumes of bonds, equities, forex or commodities for buying. selling, repo in both spot or futures are managed by quietly humming robotic-advisor services that provide online, algorithm-based portfolio management and matched trade execution.

What we thought of as periphery business, i.e. what was once called "Black-Box" or "Programme" trading is increasingly becoming mainstream.

That said, there is still the risk of a "fat finger" hitting a sell button instead of a buy, or maybe inadvertently adding an extra zero to a tickets size. That risk must be receding as smart algorithms may question a transaction that is entered completely against market trend or for a significantly different volume that is out of character.

The jury may be undecided as to the merits or accountability of cryptocurrencies, however, ***the next major leap forward in fintech looks set to be*** at the interface ***of "blockchain" and "AI" technology.*** Ultimately, the success of new fintech ventures will be dependent on the strength of consumer demand, particularly in those areas of monetary activity where the regulations remain relatively open.

What is for sure, is we have only just started and one should expect a great deal more is to come from this revolution in the next few years.

By Stephen Pope
Managing Partner, Spotlight Group
Professor of Economics and Business
University of Maryland University College
Friday, January 25th 2019

Disruptive Fintech And Capital Markets

– By Tebogo Munyengwa

Introduction

The term FinTech is short for Financial Technology. It is technological innovation in the financial services, describing internet-based transactions like cloud computing or mobile Internet with established business activities of the banking industry and other financial intermediaries like insurance companies, pension funds and investment institutions. The technological innovation brings promise of market efficiency in the form of enhanced competition in the financial sector, provision of services that ***traditional financial institutions do less efficiently*** or do not provide at all and widening the pool of financial service users by improving accessibility through cost reduction of financial services, amongst others. Notably, Financial Stability Board defines fintech as "technologically enabled financial innovation that could result in new business models, applications, processes or products with an associated material effect on financial markets and institutions and the provision of financial services."

According to Teruel (2018), Fintech originated during post-war periods, by then, very insignificant to non-existent. However, the financial system contributed greatly to technological innovations over the years, with the developments of railroads, steamships, ATMs and subsequently master cards. Steady innovation of information technology found its popularity in the financial system by the late 1900's, when internet became famous . ***Banks became completely digitised from 2005***, with consumers fully experiencing the transformation and effects of Fintech in the consumption of financial services. Arner et al, (2016), indicated that this was the real start of the FinTech era, after the financial crisis of 2008, where the public perceptions about the financial system changed, when there was an introduction of regulations and changes in economic conditions.

Fintech continued to evolve with the introduction of more complicated technologies. *The latest* in the market *being* Bitcoin and other ***cryptocurrencies.*** These currencies are a system of electronic transactions which serve to exchange goods and services without the need of an intermediary. The system adopted uses the principles of cryptography, which introduces a safe, anonymous and decentralized economy (Bunjaku et al., 2017). These developments have raised debates that the Fintech is disruptive and will be the next cause of financial market crisis. However, there has not been concrete evidence that the Fintech is disruptive, other than the rapid growth of financial products which gained sizable market share in a short period of time. This article seeks to review the debates of disruptive Fintech in capital markets.

The Transmission Channels of Fintech in Capital Markets

Fintech in capital markets is driven mainly by market participants who want alternative business models for effective solutions to address critical pain points in market infrastructure, access to capital and create new efficiencies. This resulted in remodelling of the entire concept of financial system concepts of investing, trading clearing, settlements and custody of financial assets. That is, traditionally banks set in the centre of financial world. However, ***technological innovation resulted in the changing environment and explosion of data.*** This allowed fintech firms, mostly firms without asset base and legacy banking infrastructure, to capture market share in traditional banking endeavours such as payment payments, lending, investments and financial planning (Bailey, 2016).

The influence that fintech is having on financial markets is increasing and the long-term potential is even greater. This ***might affect the financial stability*** by changing the traditional market structure. Technological innovation might affect capital market structure through different channels, including;

1 The emergence of providers of bank like services

Fintech has evolved to a much broader ecosystem that provides bank like services like fintech credit and payments which may impact capital markets and bank behaviour. The absence of legacy systems may favour new entrants, impacting on revenue basis of banks and capital markets. This might have a direct impact on financial sector resilience and risk taking.

2 The entry of large and well-established technology firms

Barberis et al (2018) indicated that non-traditional institutions with well-established networks and accumulated big data have gained mileage in the financial sector. They indicated that this could be a source of increased competition with established financial institutions. New BigTech players offer lower cost or even free services since they could use their comparative advantage of accumulated data for various business opportunities. They could also provide services that eliminates the financial intermediaries by offering direct investments and peer to peer direct payments. Trading platforms collect and analyse user and market data to uncover trends, provide aggregated market views, make forecasts and increase the profit potential of traders and firms. Many emerging firms now provide comprehensive platforms with data analytics capability which results in better-informed buyers, sellers and intermediaries directly to the individual clients.

3 The provision of important services by third parties

The Financial Stability Board (2019) anticipates the growth of the reliance of the financial institutions on third party service providers. The third-party service providers provide services like data provision, physical connectivity and cloud services.

Disruptions in Capital Markets

The *capital* markets industry is ***continuing to work hard to address several challenges.*** Faced with stubbornly high structural costs, heavy capital charges and stagnant revenues, returns on equity (ROE) continue to disappoint. Philippon (2016) shares the view that technological innovations may offer some solutions, at the same time, disrupting the existing Capital Market structures and blurring the industry boundaries, affecting existing strategic intermediation, and transforming how non-financial firms demand financial services and how capital market firms supply credit and other investment products.

Customers have had their expectations set by other industries; they ***are now demanding better services, seamless experiences*** regardless of channel, ***and more value for their money***. Regulators demand more from the industry too and have started to adopt new technologies that will reform their ability to collect and analyse information.

Expected growth of technology introduces a new set of security risks and challenges that will require serious attention in the industry. While the Capital market players think that they have resilient systems, FinTech can provide vital opportunities for criminal activities. This is evident from an increasing hacker's abilities and resources, with the nature of crimes being highly organised and almost impossible to track. The use of third-party venders, rapidly growing complex technology, cross boarder data exchanges and the high use of mobile phones are the main contributors to the creation of the criminal opportunities.

The rapidly changing capital markets environment will have an immediate and profound regulatory impact. Technology generally helps evades the tradition of borders. This poses a challenge on issues of sovereignity, legal jurisdiction, protection of customer data and tax invasions. This will require immediate attention with respect to adjustments of regulations, which will be complicated by the continuos evolution of technology.

Way Forward

The FinTech innovation and technology-oriented system in the industries are expected to bring in new perspectives of transparency, efficiency and inclusivity in the capital market services. It is also expected to re-shape customer expectations and setting new, higher standards. However, I believe that this should be viewed as the realization of the much-needed benefits of technology and should be considered competitive rather than disruptive.

Therefore, capital markets industry is mainly driven by competition, regulation and advancements in technology. Fintech innovation, thus, creates an opportunity to reposition financial services. With the technology available, the way transactions are done should be changed, that is, reducing costs, increasing efficiency and introducing new investment opportunities and new products.

In addition, collaborating with Fintech will be create an opportunity of growth or evolution to capital market industries. This will assist to revive businesses that have collapsed, and also create new ones that haven't even been considered.

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The Future Of Capital Markets In A Digital Economy

– By Oakantse Modisa

This article presents a speech delivered by Greg Medcraft, former Chairman, Australian Securities and Investments Commission (ASIC) and Chair of the International Organization of Securities Commissions (IOSCO) to the faculty and students of Carnegie Mellon University in 2015. The speech was published under the distinguished speaker series, Carnegie Mellon University (Adelaide, Australia) on 16 September 2015, and it remains of great interest to-date and for the foreseeable future. Permission to publish was sought from the ASIC International office and approved through email of 02 May 2019 06:48 AM.

The speaker prefaced his speech by recognizing the University's tradition and said it has a "long history of stimulating important conversations and exploring real solutions to the challenges facing our society". He proceeded to address "the future of capital markets, particularly the impact on those markets of ***rapid developments in digital technology; referred to as 'digital disruption'. He gave the speech from both the perspectives of ASIC and IOSCO.*** He explained that the latter "brings together markets regulators from over 120 jurisdictions – which together represent(ed) over 90% of global capital markets by value; and explained that "It (IOSCO) is the key reference point for financial services and markets regulation globally …. given its role of:

(i) Identifying emerging global risks;

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(ii) Developing guidance and standards where appropriate to deal with those risks; and

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(iii) Supporting members in developing, supervising and enforcing the law in their Jurisdictions".

The speaker further explained the regulatory mandate of ASIC across Australian financial services markets – including the exchanges and markets as well as market players who develop, sell and advise on investment and credit products. He said that ASIC monitor the conduct of these market participants, and take necessary action – including enforcement action where misconduct was detected. He underscored the regulatory objective of "ensuring that the markets (they) regulate operate to fund the real economy and drive economic growth. And, in doing so, (they) contribute to improved standards of living for all Australians". The speaker said this "can only be achieved if investors, financial consumers and those needing capital to build their businesses have trust and confidence in (their) capital markets.
The speech addressed three topics as summarized below and concluded with a discussion of "how regulators might respond":

Digital disruption to existing business models
The speaker said his main message for the day was that ***"digital disruption has enormous potential to reconfigure and radically improve the efficiency of global capital markets'.*** This he said, "will give investors, and businesses looking for capital, more direct, more immediate and cheaper access to each other." In turn, he said a regulatory response should be configured around the end users – businesses and investors – and how they behave; and that this was urgent given the speed of change – (in technical innovation and its impact on capital raising, investments and intermediaries businesses in the capital markets). He went to say the changes bring challenges "that threaten investor trust and confidence in the markets". Consequently driving the work of the regulators.

The future of capital markets in a digital economy
The speaker stated his believe that the digital disruption brings an opportunity and "the markets are seeing this with global investment in fintech ventures tripling to US$12.2 billion in 2014, from US$4 billion in 2013". (In 2018 fintech global investments more than doubling from US$ 50.8Billion in 2017 to US$ 111.8 billion in 2018 – KPMG 2018 annual report report). He incited his audience to think "about innovations like credit cards and ATMs, which were developed by banks to facilitate customer access. but now, ***new developments are going beyond the banking system directly to the customer''.*** He further said businesses saw "potential for new ways of directly creating and sharing value with technologically savvy investors and consumers. … and cited, examples that include:

"peer-to-peer lending and market-place lending; robo-financial or digital advice; Crowdfunding; and payments infrastructures (e.g. digital currencies, Apple Pay)".

In addition he hinted on developments in the insurance products as home, life and car Insurance and said such are priced to reflect deeper understanding of individual risk characteristics. He said "importantly, there is much work going on globally exploring the potential of blockchain technology".

The speaker underscored that "all these innovations have the potential to change the way that investors and financial consumers interact with financial products and payments. But many of these activities may not fit neatly within existing regulatory frameworks or policy." He said the challenge was therefore for the regulators to ensure that "they continue to deliver on the regulatory priorities of – investor and consumer trust and confidence and fair, orderly, transparent and efficient markets – in the face of these developments."

The potential that these developments have for capital markets
The speaker used ***block chain technological developments*** to underscore the challenges that digital disruption brings. He stated his believe that should this technology take off (as he believed it would) that "it ***has the potential to fundamentally change (the) markets and (the) financial system.*** He proceeded to explain the concept of block chain technology, that it allows for digital currency (also known as crypto currency) to trade without a central ledger (a central ledger is usually maintained by the central bank as issuer of money or normal currency of paper and coin – for example Pula notes and Thebe coins). He said the blockchain algorithm maintains a continuously growing records of data as the currency trades or changes ownership.

The speaker defined ***the features of blockchain*** as hereunder:-

First, it is a vehicle for ***transferring value and holding records*** – each transaction or record is evidenced by a unique data set or 'block' that attaches to the continuously growing blockchain.

Second, it does not involve a central authority or third-party ***intermediary*** overseeing it or deciding what goes into it. The computers that store the blockchain are ***decentralised*** and are not controlled or owned by any single entity.

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Third, every block in the ledger is connected to the prior one in a digital chain algorithm. So the record of ***every transaction lives on the computers*** of anyone who has interacted with it, and is updated with each entry. The continual replication and decentralised nature makes it secure.

Fourth, ***improved market access.*** Because of the global nature of blockchain, global markets have the potential to become even more easily accessible to investors and issuers; therefore making it easier for investors and for issuers to invest in and issue debt and equity securities (verbatim)

The speaker addressed how blockchain has potential to transform capital markets and highlighted four reasons as hereunder (verbatim):

First, efficiency and speed. At present, when investors buy and sell debt and equity securities or transact derivatives, they generally rely on settlement and registration systems that take sometimes several days to settle trades. It can take even longer, sometimes, where the trade involves cross-border parties. Blockchain holds potential to automate this whole process.

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Second, disintermediation. Blockchain automates trust; it eliminates the need for 'trusted' third-party intermediaries. In the traditional market, buyers and sellers can't automatically trust each other, so they use intermediaries to help give them the comfort they need. With blockchain, the decentralised ledger offers this trust. Investors can deal with each other and with issuers in private markets directly.

Third, reduced transaction costs. By eliminating the need to use settlement and registration systems and other intermediaries, there is significant potential to reduce transaction costs for investors and issuers. A June report backed by Santander InnoVentures, the Spanish bank's fintech investment fund, estimated that blockchain could save lenders up to $20 billion annually in settlement, regulatory, and cross-border payment costs.

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Fourth, improved market access. Because of the global nature of blockchain, global markets have the potential to become even more easily accessible to investors and issuers; therefore making it easier for investors and for issuers to invest in and issue debt and equity securities.

He cautioned that, "harnessing this potential will depend on the integrity, capacity and stability of blockchain technology and processes. It will also depend on industry's willingness to invest in, and make use of, new ways of settling and registering transactions. The potential is, nonetheless, enormous. Industry is seeing that potential and is looking to see how it and the markets might benefit".

In addressing the areas where blockchain is being explored, the speaker touched on four areas:

The first is in share, loan and derivative trades. A series of start-ups are looking to use blockchain to execute and settle securities and derivative trades.

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The second is in private equity transactions. The US stock exchange, NASDAQ, is experimenting with using blockchain technology as a way of recording private equity transactions. In doing so, it hopes to provide 'extensive integrity, audit ability, governance and transfer of ownership capabilities'.

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The third is in government bond trades. A US firm is developing a way to use blockchain to record and settle short-term government bond trades on a distributed ledger.

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The fourth is in money transfer. In Mexico City a firm has developed an app that lets migrants send money via the blockchain to Mexico and withdraw cash from ATMs.

Regulator and Policymakers' Response
The speaker went on to discuss how the opportunities offered ***by blockchain technology "can also threaten strategic priorities of investor trust and confidence and fair, orderly, transparent and efficient markets".*** He was reminiscent of the evolution of blockchain and other disruptive technologies and potential implications for the markets and how they will be regulated.

He noted that while, ***regulators and policymakers, should be harnessing the opportunities and the broader economic benefits – by not standing in the way of innovation and development; at the same time, they should be mindful of mitigating the risks these developments pose to the regulatory objectives.*** Further, he underscored the need to ***ensure that those who benefit from the technology trust it.*** Concluding that the objective is to ensure that investors and issuers will continue to have trust and confidence in the capital markets.

He spoke on five key areas of ASIC response to the challenges of digital disruption and ensuring that the opportunities are harnessed and risks mitigated hereunder:

First, embarking on an educational drive to support investors and financial consumers in understanding the opportunities and the risks of participating in the digital economy. For example,
The ASIC MoneySmart website, which he said received over 5 million visits in 2014.

Second, providing guidance to industry inter alia, in the following two areas:

The first being cyber resilience work by publishing guidance for businesses to help in their efforts to improve cyber resilience and manage their cyber risks. Second being the launch of the Innovation Hub in 2014 which is designed to make it quicker and easier for innovative start-ups and fintech businesses to navigate the regulatory system administered by ASIC. He said the Innovation Hub – also includes the new industry-led Digital Finance Advisory Committee which is important as it provides the information about the developments that are on the horizon, and how they might fit into the existing regulatory framework.

Third, being surveillance and monitoring of the market to understand how investors use technology and financial products and the risks that arise. Furthermore, he said ASIC continued to monitor the global landscape for new developments, the pace of change and emerging risks that may be posed by structural change driven by digital disruption. In particular he said there is a need for regulators to focus on and understand a number of issues in the blockchain, including: -

– how blockchain security might be compromised ;
– who should be accountable for the services that make the blockchain technology
work ; and
– how transactions using blockchain can be reported to and used by the relevant
regulator.
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Fourth, being enforcement, to take action against misconduct. He said thater was a challenge in understanding how regulatory action could be taken where a transaction entered domestically or overseas is recorded in the blockchain.

Fifth, to provide policy advice so as to ensure the right regulation is in place to protect investors and keep them confident and informed, while also not interfering with innovation. He outlined the need to ensure that rules are globally consistent such that international regulators can rely on each other in supervision and enforcement. He mentioned that the existing regulatory framework was continually under review to accommodate changes brought about by blockchain and other innovation.

In addition, the speaker, wearing the IOSCO hat, sad ***IOSCO*** also has a key role to play in this area, especially in ***ensuring that there is a global strategy in place and that cooperation between regulators is in place*** – in order to meet the challenge of addressing issues arising from cross-border transactions. He outlined four priorities of IOSCO work as entailing the following:

(i) To identify and understand risks flowing from digital disruption to business models. He mentioned that, the IOSCO Board was to hold a stakeholder roundtable on "The future of capital markets in a digital economy" on October 2015 in Toronto, Canada. The discussion were to address financial technological developments and regulatory responses.

(ii) International cooperation in the designing of regulatory toolkits and responses that are flexible, creative, and provide incentives for financial technology innovation that drive growth without undermining investor and financial consumer trust and confidence in the global capital markets. He gave an example of work being considered for crowdfunding.

(iii) In the cyber resilience work, a Committee for Payments and Market Infrastructures was to develop guidance that will help strengthen the cyber resilience of financial market intermediaries by end of 2015.

(iv) To strength international cooperation through the enhancements of IOSCO's Multilateral Memorandum of Understanding – or MMOU – to deal with the new technological environment. The MMOU is a cooperation arrangement that enables 105 regulators to share information to combat cross-border fraud and misconduct. The aim is to make it easier for IOSCO to take action in relation to cross-border transactions.

Conclusion

Greg Medcraft concluded his speech by ***emphasizing the importance of industry and regulators to work together to harvest the opportunities from digital disruption and financial innovation.*** He said the regulatory community supports the industry in taking advantage of the opportunities on offer, whether it is from blockchain technology or other innovations. However, he emphasised that innovation must foster investor and financial consumer trust and confidence. He said the regulators will continue to be forward looking and to engage with industry on new developments. He said it is a shared interest that these opportunities are harvested, while at the same time mitigating the risks such that the benefits of _ "trust and confidence in our markets and sustainable growth are achieved".

Interview With Director Capital Markets

–By Gorata Molojwane

Question: What are Capital Markets?

Answer: Capital Markets provide a place for those with excess funds (investors) to channel them to those who are in need of funds (capital raisers) through the buying and selling of financial instruments. This can be done through the issuing of equity and debt instruments.

Question: What are equity and debt instruments?

Answer: Equity or shares, are issued by companies in order to raise funds, and represent ownership of that company.
Debt instruments are issued by companies that seek to borrow funds from investors. For instance, a bond is a long term debt instrument where the principal amount is loaned to the issuer, who has to repay the principal, plus interest which is paid at intervals over the life of the bond.

Question: What is a securities exchange?

Answer: A Securities exchange is a market place for people to come together to exchange (buy and sell) shares, bonds and other securities.

Question: Can an Investor find shares of any company they may be interested in, on an exchange?

Answer: Only shares of companies listed on that exchange may be bought or sold to investors.

Question: Can I purchase listed shares and bonds at the exchange or through NBFIRA?

Answer: Shares are not sold directly by the exchange and NBFIRA cannot buy or sell shares on behalf of investors. Listed securities can be bought through placing your order with a licensed securities broker that is a member of the exchange. In Botswana, we have four licensed securities brokers.

Question: What happens after becoming a shareholder?

Answer: As a shareholder you are entitled to dividends, voting in directors of the company, voting at shareholders meetings, a share in the assets of the company if it goes into liquidation.
You can also benefit from capital gains, which refers to the profits made from selling the shares at a higher price than the price they were bought at.

Question: What determines dividends?

Answer: These are declared by the board of directors and represent a portion of the company's profits that will be paid to shareholders. The frequency and amounts differ from company to company and year on year.

Question: What are the risks of buying listed securities?

Answer: There is no guarantee that a company will continue to perform well and successfully implement its growth strategy.
-Capital losses may be realised, if shares are sold at a lower price that what they were bought for.

Question: What determines the share price of a listed company?

Answer: This is determined through the supply and demand for that share. If investors' views towards a certain company is that it is good and has potential for growth, they will demand more of it than is available in supply, thus putting upward pressure on the price to find a price where there are enough willing sellers to meet the increased demand. Similarly if investors lose faith in a company and do not anticipate its growth, its demand will fall and there will be an oversupply of the share, causing downward pressure on its price in order to find a price where there are enough willing buyers to meet the increased supply. Price movement of a stock therefore reflects what investors feel a company is worth and not necessarily the company's current value.

Question: Who can buy shares?

Answer: Anybody, parents can also buy shares for minors. Some trade for less that P1 per share and the minimum you can buy on the exchange is 100 shares.

Question: How will I know which company to invest in?

Answer: Read all you can about the company to see whether you have faith in its board, management, and what it is trying to achieve. Know all positive or negative information there is about the company;

- If it is an initial public offering, read the prospectus, be familiar with the current status of the company, the company's strategy, its board and its management,
- Stay informed by reading company announcements (on the exchange website, newspapers, annual report, attend Annual General Meetings).
- Read research reports.
- Make use of financial advisers.
- Alternatively, investors can invest in a collective investment

- Read research reports.
- Make use of financial advisers.
- Alternatively, investors can invest in a collective investment undertaking, where the investor buys into a fund which holds a diverse pool of securities, and a group of experts are tasked with selecting the appropriate securities that the fund should hold.

Question: Does the exchange or NBFIRA guarantee that I will get a positive return on my investment?

Answer: Nobody knows for certain which direction the share price will move, and nobody knows for certain that the company's strategy will make it profitable, therefore just like any other investment such as farming or opening a tuckshop, there is a risk that investors may incur losses.

Question: In what ways can a Stock Exchange facilitate economic Growth and diversity?

Answer: An exchange can help a country position itself as a financial centre and attract foreign investment, assisting in diversifying the economy.

- An exchange provides an alternative source of funding for companies, which are then able to expand and contribute towards increased employment and GDP.
- There opportunities to use capital markets to grow economic industries such as infrastructure, energy (solar) and agriculture.
- The returns that are made on investments can be used towards something that will contribute to economic growth.

Question: What is market capitalisation?

Answer: Market Capitalization provides a measure of the value of a company. It is calculated by multiplying the number of shares held by all shareholders (outstanding securities) by the market price.

Question: What is the role of NBFIRA in the Capital Markets?

Answer: NBFIRA regulates the various participants of the Capital Markets including the securities exchange, securities brokers, financial advisers, central securities depository, collective investment undertakings, asset managers and custodians.
The licensed entity's Board of Directors and Senior Management are assessed on whether they are fit and proper to be a controller of a public interest company. The non-bank financial institution is licensed by NBFIRA and monitored for compliance with the relevant laws, regulations and rules, off-site through reporting requirements and on-site through inspections.
NBFIRA ensures that there are legal frameworks to provide guidance to licensees on how to operate in a manner that it transparent, minimises risks, where clients are treated fairly.
NBFIRA then takes action for non-compliance matters in order to restore licensees to compliance status, failing which the licence can be cancelled.

Question: What kind of protection am I given as an investor?

Answer: Disclosure requirements make it mandatory to publish price sensitive information so that investors can make informed decisions.

- Rules and regulations prohibit unfair market practices.
- Institutions are required to have a professional indemnity cover in order to be able to
- The Exchange has a Security Fund in order to in the case of dishonesty by a broker.
- A client may request NBFIRA to intervene where their complaint has not been adequately addressed by the licensed company.
- NBFIRA has several enforcement tools to deter and mitigate effects of non-compliance. This ranges from monetary penalties, warnings, directions to take certain actions, suspension of the company, introducing a statutory manager to restore the business to good condition, variation and cancelation of licence.

Question: How are Capital Markets regulated to ensure compliance and the integrity of the financial system to protect the economy?

Answer: Through the establishment and enforcement of regulatory frameworks, for non-bank financial institutions, which allow for prudential and market conduct supervision.

- NBFIRA is a member of various International Standard Setting Bodies such as the Committee of Insurance, Securities and Non-Banking Financial Institutions, Associate Members of the International Organisation of Securities Commissions, wherein challenges that are common to the market are interrogated in order to issue recommendations, and lessons can be learnt from other regulators.

Question: What are the Challenges in our Capital Markets industry?

Answer: The local stock exchange is relatively small with not much participation from diverse selection of local industries.

- Low Liquidity issues due to the buy and hold strategy of companies, who are the dominant investors, as well as Low levels of participation and activity.
- Financial Education & Financial Literacy levels are still low. People will generally be reluctant to participate in something they do not fully understand.
- Limited investment Products

Question: What advice can you give to the public general about investing through Capital Markets?

Answer: Make sure that the entity is licensed prior to making an investment decision.

- Establish the amount of risk you are willing to make sure that the risks of the investment under consideration matches the risk you are willing to take.
- If you invest in shares, understand that dividends are not your only source of investment returns. You can benefit from capital gains if you sell your shares at a higher price than the one you bought them for.
- Understand Terms & Conditions before investing. Read all the disclosure documents you are given and ask questions. Before you sign anything, make sure you understand what it is you are signing for. Make sure that you have a written agreement that also stipulates what would need to happen when you want to get out of the investment, and what conditions can restrict you, if any.
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Question: How can the public escalate their concerns or grievances to NBFIRA?

Answer: Follow the reporting channels within the licensed company in writing.

- If you fail to get a response or are not satisfied with the response, submit all communication you had with the entity to NBFIRA to investigate.

Asset Management And Major Risks

– By Sriram Gade

This article examines the risks of investment in financial markets. It is never advisable to dream about returns without understanding the related risks. I remember that when Botswana Telecommunications Corporation (BTC) shares were issued, there was a mad rush as people thought they can make quick money through this investment. Though investment advisors must have advised about related risks people bought the shares with excitement due to possible returns. However when the share price of BTC went down up to 90 thebe implying 10% loss to issue price that too just within four months of the issue, some people advised me that they regretted buying the stock as they never knew about the risks and as a result suffered losses. Fortunately BTC share price has since recovered getting back smiles to the investors. The point to remember is that investments are prone to risks and people should not be swayed away by allurement of returns without understanding the related risks. I intentionally decided to discuss the risks of investment in more detail so that the readers will be clear about all the aspects of investments.

Investments carry several risks which can emanate from the very types of investments, from the infrastructure related to investments or from the intermediaries involved in the investment. The risks which could result from the types of investments are discussed below.

Price Risk:

The reason why people fear stocks and similar investments is price risk which means the risk of loss resulting from the movement in market prices of the assets. The prices of assets depend on a number of factors starting from company specific factors, industry specific factors, country specific factors or international factors. Decline of over 50% in price of a security during a very short period of time is not uncommon in international markets. This shows that even major part of principal amount of investment could be at stake due to price risk. While sharp market price declines are the result affecting the investors, the immediate reason is the fear factor influencing investor psychology which triggers a panic sale. The ultimate cause for the price risk could be any other risk discussed hereinafter. Occurrence of any of these risks will result in triggering fall in prices.

Interest Rate Risk

The prices of bonds are directly influenced by the interest rates and remaining tenor of the bond in addition to credit risk of the issuer. The prices of the bond are normally inversely related to the interest rates meaning thereby the bond prices fall when interest rates rise and bond prices rise when interest rates fall. If after investing in bonds the interest rates rise then bond prices will fall causing losses.

Credit Risk
Prices of all the investments are influenced by credit risk emanates from the credit worthiness, both actual and perceived, of the issuer. Credit risk causes default risk which means the risk of default by the issuer to pay its liabilities. Credit risk is often measured by the investors based on the credit rating of the issuer. Higher the credit rating lower the credit risk. International markets have witnessed sudden fall in credit rating and consequent crash in share and bond prices. The author remembers how the bond and share prices of WorldCom crashed when its credit rating declined sharply due to an accounting scandal.

Currency Risk
When some investments are placed outside a country or denominated in a currency other than domestic currency then the investor assumes currency risk. When there is currency risk, there is a possibility of loss resulting from movement in exchange rates. For example, if investments are funded by Botswana pula but invested in another currency by converting Botswana pula then whenever Botswana pula appreciates against the other currency there will be loss to the investor. For a numerical example if BWP 100,000 is converted to USD 10,000 at an exchange rate of USD 1=BWP 10 and stocks worth USD 10,000 are bought, then there will be currency loss if exchange rate moves to USD 1 = BWP 9 because the investment is now worth only BWP 90,000 implying a 10% loss assuming no movement in the share price. If there is also loss resulting from decline in the price of shares, the total loss will be bigger resulting from both currency risk and price risk.

Country Risk
Country risk arises from a set of risks related to investing in the markets of a country. The set of risks varies depending on the country and comprises political risk, credit risk, currency risk, repatriation risk, economic risk etc. which are unique to the country. Political risk depends on the degree of political stability, policies of the Government and economy condition. The country risk includes the risk that country may default which is credit risk. Similarly its policies and economy may cause exchange rate fluctuations which is currency risk. Credit risk and currency risk have already been discussed in my previous article. Another important factor of country risk is the permissibility and ease of repatriation of investments when desired. All these factors determine the country risk which influences the investments by foreign investors of the country. The asset managers normally look to the sovereign credit ratings of a country given by international rating agencies to assess the level of country risk. Another country risk indicator is the index of Black Stone Risk index of various countries which is published quarterly. However both these are important tools but in practice choice of country takes into consideration the convenience of investing and the depth and width of the financial markets in the country coupled with a SWOT analysis of that country. For example Germany's position at 9 in Black Stone current Risk Index is six positions higher than that of US which is at 15. Again credit rating of Germany from two international rating agencies is equal to that of US while from Standard and Poor the rating of Germany is higher than that of US. Still US is a more favoured destination of the asset managers because of the depth and width of its financial markets and vast opportunities at the country. US is the more favoured destination for even Botswana's offshore assets.

Reinvestment Risk
Reinvestment risk is the risk that the periodic returns from the payment of principal and interest have to be reinvested at a lower rate than that of the original investment. Investments like bank deposits, bonds, floating rate notes periodically pay interest. Further these investments repay the principal at maturity. Even stocks pay dividends periodically while rentals are received periodically. All these periodic payments and those payments received at maturity need to be reinvested at market interest rates unless spent for the purpose other than investments. If market interest rates have fallen from the levels those prevailed at the time of original investment, then the investors face impact of reinvestment risk and are forced to reinvest these funds at lower returns. In Botswana since last several years interest rates have been falling and investors have seen the impact of reinvestment risk.

Operational Risk
Operational risk to the investors arises from the operations of the entire infrastructure in which investments take place from the beginning to end. It includes risks resulting from failure of people, systems, procedures and controls governing the various parts of the cycle of investments. An investor deals, directly or indirectly, with several parties/intermediaries in the process of effecting investments, like banks, retirement funds, insurance companies, stock brokers, asset managers, stock exchange etc. Operational risk to the investor is caused by the failure of operations at any of these intermediaries. The operational risk gets multiplied because of numerous intermediaries in the journey of funds from original investors to ultimate destinations, the operational risk gets multiplied. Higher operational risk often results from system issues related to data and technology, high reliance upon service providers and weak oversight over service providers. Another critical factor is the fraudulent activities at any of the intermediaries.

Liquidity Risk

Liquidity risk is the risk of inability of the investor to liquidate the investments when required for meeting the needs. It stems from the lack of marketability of the investment and resulting absence of buyers for the investment. As a result the investor is stuck with the investment. Illiquidity of an investment can arise from various factors like the investment in unlisted instrument or lack of trading even if the investments are listed. If the asset is property then illiquidity results from reasons like it is located in a remote area or in a troublesome area. Illiquidity of shares sometimes is because the issue or issuer size is small. Similarly, private equity has low liquidity.

Concentration Risk

Concentration risk can be well understood from the saying "One should not put all his eggs in one basket". When the investments are concentrated in one or few investments the investor may suffer losses due to concentration risk when the value of concentrated investments declines. Concentration may result in various ways. It could be (1) intentional concentration as the investor believes the investments chosen will outperform the market or actually outperformed the market (2) in correlated group of assets like an industry, a sector, a geography or a particular security class like junk bonds (3) concentration in illiquid assets like private equity or property in remote areas or untraded funds etc.

Horizon Risk

Investment horizon is the total length of time that an investor expects to hold a security or a portfolio. The investment horizon determines the investor's income needs and desired risk exposure. For example, a young new employee may plan for long term investments like equities because his horizon could be 30 years or more. For someone nearing retirement, however, preservation of capital becomes more important and fixed-income investments become more attractive. For a longer investment horizon, more risk can be taken, since the market has many years to recover in the event of a pullback. When the horizon suddenly changes due to factors like change in employment or change in medical conditions or other circumstances, horizon risk takes place because funds might have been locked in investments as per the original horizon and rebalancing might result in losses.

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