

# The Promotion of Regional Capital Markets In Africa

*By*

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# Why Regional Capital Markets

- Integration of African economies within the framework of AEC and Regional Economic Communities (RECS)
  - Abuja Treaty, June 3, 1991
  - RECs
    - Arab-Maghreb Union (AMU)
    - Central African Economic and Monetary Union (CEMAC)
    - Common Market of Eastern and Southern Africa (COMESA)
    - Economic Community of West African States (ECOWAS)
    - East African Communities
    - Southern Africa Development Cooperation (SADC)

# ACE Requirements on Financial Markets

- Harmonization of monetary, financial and payments policies
- Enhancement of monetary cooperation
- Promotion of regional and sub-regional money markets
- Monetary Union
- Regional integration of RECs converge to African Integration

# Economic Reasons for Regional Integration of Markets

- Drying up of official sources of external capital
- Limited domestic pool of savings
- National stock markets too small
- Facilitation of foreign direct and portfolio investment

# **Stock Markets and Economic Growth**

# The Role of Capital Markets

- Price discovery
- Liquidity
- Reduction of Transaction costs
  - Search Costs
  - Information costs
- Transferring of Risk

# Diversification of Financial System

- Banking system is dominant mode of finance in developing countries
- Financial markets reduce dependence on crisis-prone banking systems
- Substitutes and supplements
  - Unit trusts
  - Corporate bonds
- Well-developed financial system is diversified and less crisis-prone

# Stock Markets and Economic Growth

- Research indicates that stock markets can give a big boost to economic activity.
- Impact on economic activity occurs through creation of liquidity
- Over the period 1976-94, countries that had relatively liquid markets tended to grow much faster than countries with illiquid markets
- Countries with liquid markets enjoyed faster rates of capital accumulation and general productivity gains over the 18-year period

# Improving Liquidity

- Supply Side
- Demand Side
- Trading Arrangements
  - Well-capitalized dealers
  - Continuous Trading
  - Automated trading
- Larger market are better able to provide needed liquidity

# **Models of Capital Market Integration**

# Two Dimensions of capital Market Integration

- Reduction of policy barriers to capital mobility
- Reduction of barriers to trade in financial services (fair market access for cross-border participants)
- Both are important and complement each other
- Market integration does not mean a single stock market!

# Integration possibilities

- **Cross-Border Alliances**
  - Link-up of trading, clearing and settlement systems
  - Dual listings (direct and Depository receipts)
- **Regional Market**
  - Disappearance of national stock exchanges
  - Serious constraints
    - Uniform regulatory and accounting standards
    - Restrictions on capital transfers
    - Lack of currency convertibility

# Benefits of Integration

- Size
- Insulation from shocks
- Increased efficiency and price discovery
- Reduction in transaction costs
- Expansion of investment opportunities for African Investors
- Reduction in risk through diversification of country-specific macro economic risks

# **African Stock Markets**

**Table 4: Saharan-Africa Stock Market Statistics, 1998**

Country	YEAR OF ESTABLISHMENT	Market Capitalization to GDP	Turnover (%)
Botswana	1989	14.3%	10.5
Côte d'Ivoire	1976	17.7%	2.5
Egypt	1898	31.2%	22.2
Ghana	1990	20.1%	4.8
Kenya	1954	19.8%	4.1
Mauritius	1989	42.0%	5.8
Morocco	1929	49.1%	9.9
Namibia	1992	12.5%	2.3
Nigeria	1960	7.2%	4.9
South Africa	1887	131.9%	29.1
Swaziland	1990	5.8%	0.0
Tunisia	1969	12.85%	8.2
Zambia	1994	8.3%	na
Zimbabwe	1896	14.7%	10.1

Source: Stock Markets Fact Book, 1999, IFC  
Investor's Guide to the African Stock Markets, 1999

# A Look At the BRVM

- World's first Regional Stock Exchange
- Serves 8 UEMOA countries (Benin, Burkina Faso, Ivory Coast, Mali, Niger, Senegal, Togo, Guinea Bissau)
- Opened in September 1998

# Corporate Basis

- Limited Liability Company owned by:
  - Governments of UEMOA States (13%)
  - Sub-regional institutions (e.g. West African Development Bank) (23%)
  - Chambers of Commerce of UEMOA (11%)
  - Brokerage Firms (28%)
  - Private businessmen (25%)

# Institutional Basis & Trading

- Conseil Regional (Regulatory Agency)
- Central Depository and Settlement Bank
- Brokerage Companies (Societe de Gestion et d'Intermediation)
- Trading
  - Buy and sell orders are received and transmitted by satellite to head office in Abidjan
  - Trading occurs 3 times a week with one daily price fixing
  - Trading results available online in all countries

# Some Lingering Problems

- Market illiquidity, low transaction volumes
- Harmonized Tax Code has been ratified but not implemented
- AGMs are difficult to hold; postal services in region are poor; voting by distance difficult

# Lessons from BRVM

- Unity of Purpose
- Harmonization – Common Business Code (OHADA)
- Integrated trading platform
- Common Currency and Central Bank
- Model may be difficult for other RECs

# European Integration

- Minimal harmonization
- Principle of Mutual Recognition
- Reflected in:
  - Investment Services Directive
  - Capital Adequacy Directive

# Lessons from European Integration

- Multilateral agreements are not enough. Clear commitment to allowing offshore financial institutions is needed
- Formal legal harmonization can be kept to a minimum
- “Mutual Recognition” + “Home Country Control” works
- Single currency is key

# The African Integration Record

- ECOWAS
  - Limited Integration
  - Fast track process to lead to monetary union in 2003
- SADC – most advanced
  - Committee of SADC Stock Exchanges
  - Committee on Insurance, Securities and non-Banking Authorities (CISNA)

# Market Integration Constraints

- Disparities in size
- Currency inconvertibility
- National Pride and sovereignty
- Low technological base

# Policy Implications

- Capital Market Integration not an end in itself but part of comprehensive economic Integration
- Not necessary to achieve complete harmonization of rules
- Cross-border alliances with cross listings is fastest route
- A regional stock exchange is not necessary to achieve integration