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AFRICA'S FINANCIAL MARKETS: A REAL DEVELOPMENT TOOL?

Despite their limits can financial markets really contribute to private sector financing?
What can they provide to firms and individuals?
How can governments and development partners improve their performances?
These issue compares experts' views on these questions.

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Editorial

By Luc Rigouzzo, *Chief Executive Officer of Proparco*

African financial markets have been experiencing spectacular growth since the early 1990s. Their number has since risen from roughly a dozen to 23 and they now provide continent-wide coverage. Market capitalization has risen ninefold and over 2 000 businesses are now listed. There has been a sharp increase in initial public offerings (IPOs) in recent years which have allowed some banks or businesses to raise sizeable amounts of capital – this gives a clear sign of the depth of local savings and domestic investors' interest in stock markets. For instance, since 2000 nearly USD 4 billion have been raised locally on the Lagos Stock Exchange in Nigeria alone. Thanks to privatization programs, hundreds of thousands of Africans have become shareholders of major companies in their countries. Yet the size of these markets remains small – both on a global scale and in terms of African economies. Liquidity is often totally lacking and this deters foreign investors that are still not sufficiently active on these stock markets. Businesses are reluctant to conduct an IPO and very seldom manage to finance themselves through bond issues.

This fifth issue of the magazine Private Sector and Development makes a comprehensive review of developments (recent and future) on Africa's financial markets. It also highlights their utility and their impacts on African economies and poses the questions: Is the continent not at a too early stage on its "development path" to invest in the creation of financial markets? What do stock markets really bring to businesses that decide to conduct an IPO? What is the popular base of these markets? And how do they link up with banking markets – which themselves are in their infancy in many countries?

True to its editorial line, the magazine Private Sector and Development has once again decided to compare the ideas of researchers, development actors and private operators, investors or listed businesses. I would like to thank all the contributors for the originality and diversity of their points of view and for having managed to go beyond the often oversimplistic vision that we have of African realities. Yet such a topic could have become completely bogged down in ideological positions and recent debates on the crisis. This has not been the case. The authors tell us about just how important financial markets have become for Africa and the extent to which the stock market tool - with its limitations and weaknesses – has now become a local reality.

Proparco has been supporting the development of Africa's financial markets alongside other funders for 15 years now. This choice has become a cornerstone of our strategy. It is important to assess the impact and relevance of these operations and this issue of Private Sector and Development clearly contributes to this. The articles, which I hope you will read with pleasure and interest, underscore our aim to pursue our operations to support these markets while, of course, remaining aware that they are just one element among all the physical and financial infrastructure required for the development of the continent. ●

AFRICA'S FINANCIAL MARKETS: A REAL DEVELOPMENT TOOL?

Enko Capital Management LLP is an Africa-focused asset management firm with offices in London and Johannesburg. It manages two funds, an open-ended fund investing in listed securities across Africa and a closed-end, pre-IPO private equity fund that will invest in fast-growing African companies wishing to list on an African stock exchange. Founding member, Cyril Nkontchou, will analyse recent evolution of African financial markets and observe their increased role in providing capital to the private sector.

Recent Evolution of the African Financial Markets

Financial markets play an increasingly important role in financing Africa's private sector. Their recent growth in strength is unquestionable – despite the sudden standstill caused by the 2008 crisis: sixfold increase in capital flows in 10 years, opening of stock markets, initial public offerings by public and private companies, etc. If these markets are to continue to develop, it is essential to free up African savings – which are trapped by low-return assets and the lack of quality products – and to learn to attract higher portfolio investment flows.

By Cyrille Nkontchou, ***Managing Partner of Enko Capital Management LLP***

Cyrille Nkontchou
Enko Capital

Cyrille Nkontchou is the founder and managing partner of Enko Capital Management LLP, an Africa-focused asset management firm with offices in Johannesburg and London. He is also the founder and executive chairman of LiquidAfrica Holdings Limited. He started his career as a consultant with Andersen Consulting (now Accenture) in France, and worked as a banker with Merrill Lynch in London. He holds a degree in Economics from Institut d'Études Politiques de Paris and an MBA from the Harvard Business School.

The first decade of the 21st century has seen a sixfold increase in private capital flows in Sub-Saharan Africa. Foreign direct investment in Africa has traditionally been dominated by large multinationals mainly investing in resources projects, but the second half of this decade has witnessed the emergence of financial markets as a major source of finance for investments. Between 2007 and 2009, USD 10 billion of equity capital was raised on local African stock exchanges. Many first-time issuers such as Gabon and Ghana successfully raised debt sovereign bonds on the international market.
The financial markets are playing an increasingly important role in providing capital for the private sector in Sub-Saharan Africa, particularly in the financial services and telecommunication sectors. They are also playing a pivotal role in providing alternative investment opportunities for local savings, as seen in Nigeria where the bulk of the recapitalisation of the banking sector was achieved by channelling local savings into the stock market. However, despite recent successes, the development of African financial markets is hindered by a lack of accurate data, preventing both governments and development institutions from implementing adequate policies.

The rise of financial markets in Sub-Saharan Africa

The second half of this decade has witnessed a remarkable growth in African financial markets. The number of stock exchanges has risen from a dozen in the early 90s to over 23 today, including two regional stock exchanges. Over two-thirds of African countries are covered by a local or regional stock exchange.

With less than 2000 listed companies across all African markets (compared with 3500 for India alone, and 1700 for China), the number of companies that have tapped into the capital markets to fund their growth remains relatively small. However, over the past three years, we have witnessed an acceleration in the number of African companies going public. Between 2007 and 2009, over USD 10 billion of share capital was raised across 18 stock exchanges, mostly thanks to the listing of 170 new companies. The market capitalisation of the 10 largest markets grew from USD 222 billion to over USD 700 billion between 2002 and 2008, a compound annual growth rate (CAGR) of 18%. In Nigeria, the recapitalisation of the banking sector between 2005 and 2008 attracted over USD 4 billion of new investment through the stock market, mainly from local investors. The strong aftermarket performance of initial public offerings (IPOs) in Africa drew even more investors into pre-IPO investments. In Nigeria alone between 2007 and 2009, over USD 8 billion of equity capital was raised in such pre-IPO private placements[1].

Increased investor appetite for shares in utility companies such as Kengen and Safaricom in Kenya and banks such as Zanaco in Zambia allowed African states to benefit by successfully offloading large stakes in these companies. They also took advantage of the renewed investor appetite for African sovereign credit to raise bonds on the international market. The Government of Ghana raised USD 750 million in debt sovereign bonds, while the Republic of Gabon successfully raised a USD 1 billion 10-year bond on the international market. The Government of Seychelles raised a USD 230 million three-year bond. In effect, these flows enhance governments' financing capacities and constitute fresh money for public investments.

The rise in African financial markets was underpinned by improved macroeconomic fundamentals in the region, but also by a stellar performance of African stock markets during that period. ...

[1] *Pre-IPO placements refer to initiatives from investors to acquire capital shares of firms before their introduction on the stock exchange. These transactions are aimed at benefiting from a substantial upside by selling the acquired shares after the IPO (resulting from oversubscriptions and an increase in share prices).*

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... One of the most visible positive impacts of the rise of African financial markets in the past few years has been the recapitalisation of the banking and insurance sectors in Nigeria. On the other hand, the sector recently experienced troubles as the newly recapitalised banks aggressively started to provide loans to finance the purchase of shares in an inflated stock market. The global market meltdown in 2008 clearly put a brake on the exuberance of African financial markets. New issuance decreased dramatically as local stock markets indices collapsed. Foreign portfolio investors shied away from African markets and began returning cautiously in 2009, but only in the most advanced and liquid markets, such as South Africa and Egypt. The recent successful IPO of the CFAO group[2] in Paris however suggests that there is a renewed appetite for quality African assets among emerging market investors.

Unlocking trapped African savings

The rise of financial markets in Sub-Saharan Africa over the past few years has uncovered the importance of the often underestimated role of African investors eager to invest in financial assets. Among the sources of funds available for investment on African stock exchanges – some of which are not well utilised at present – are the following: (1) individual savings (for example, wealthy Nigerians), (2) funds collected by institutional investors (insurance companies and pension funds) and (3) funds deriving from loans given by banks to their clients for helping them to invest on the markets (margin loans).

The recapitalisation of the financial sector in Nigeria was a case in point. The decision in 2004 by the governor of the Central Bank of Nigeria to raise the minimum capital requirement for banks licensed in Nigeria to USD 250 million by December 2005 was initially met with scepticism. But most observers underestimated the pool of local African savings trapped in sub-optimal investment products[3] as a result of a relative lack of available assets in African financial markets. ...

Table 1: Subscription levels of African IPOs, 2009

Company	Sector	Country	Issue Size (USD million)	Subscription Level
Compagnie Generale Immobilier	Real Estate	Morocco	426	142x
Taalat Moustafa	Real Estate	Egypt	688	41x
Maridive	Oil Services	Egypt	278	31x
Alliances Development Immob.	Real Estate	Morocco	275	29x
Delta Holdings	Construction	Morocco	129	22x
GB Auto SAE	Automobile	Egypt	213	7x
Dangote Flour Mills	Food	Nigeria	146	6x
Kenya Reinsurance	Insurance	Kenya	34	4x
Safaricom	Telecom	Kenya	786	4x
AccessKenya	IT	Kenya	11	4x
Stanbic Bank	Banking	Uganda	39	3x
Celtel	Telecom	Zambia	174	2x
National Microfinance Bank	Banking	Tanzania	53	1x
Dangote Sugar	Food	Nigeria	404	1x

Safaricom's IPO was successful: the subscription level of 4 x means that subscribers proposed to acquire four times more shares than the number of shares that Safaricom was selling.
Source: Enko Capital research, 2009

[2] *The Compagnie française de l'Afrique occidentale (CFAO), a subsidiary of the Pinault-Printemps-Laredoute group, is the leader in specialised distribution in Africa and the French Overseas Collectivities (Collectivités d'outre-mer). The English translation for CFAO is French Occidental Africa Company.*
[3] *Such products are sub-optimal because they can provide relatively low returns for investors and/or low impacts on the local private sector. Examples of these are sight deposits, treasury bills (short-term), funds to be invested abroad, etc.*

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... Between 2005 and 2008, the banking sector recapitalisation was successfully achieved thanks to a combination of both private and public, primary and secondary issues mainly on the local market. These issues were mostly subscribed to by local institutions and individuals. There is evidence that many wealthy private Nigerian investors repatriated some of their offshore investments to participate in this recapitalisation.

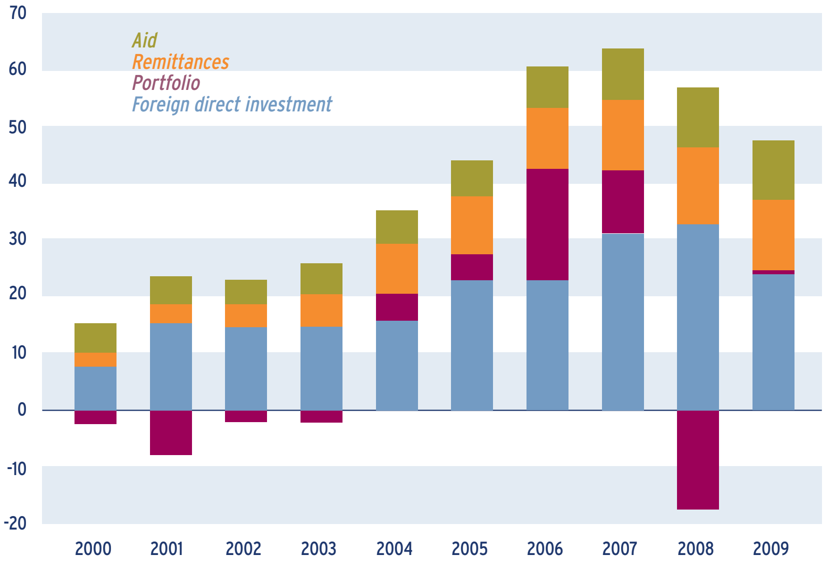
The importance of African savings available for quality financial assets is further evidenced by the level of oversubscription observed for many recent new IPOs on African stock markets (Table 1). This data indicates that apart from real estate and local government paper such as treasury bills, African investors have very few investment opportunities available. Moreover, local institutional investors such as insurance companies and pension funds are typically restricted from making investments outside of their home countries or monetary zone. As a result, a large pool of savings ideally suited to investment in financial markets is trapped. This increased appetite of African savers for local financial assets was further fuelled by local banks that in Nigeria, Kenya and Zambia provided personal loans to invest in the stock market (*e.g.* margins loans in Nigeria).

Attracting emerging market portfolio flows

Until the global market meltdown in 2008, African financial markets – particularly the more developed ones – have seen a steady rise in emerging market portfolios flows[4] (Table 2). In part, abundant global liquidity was responsible for the surge of private capital flows into Africa, but investors were also attracted by Sub-Saharan Africa's recent solid macroeconomic performance, more stable political environments, and high expected returns, given increasing commodity prices. With the exception of South Africa, Egypt and to some extent Nigeria, emerging market portfolio flows have played a limited role as a source of investments in the local capital market. Investors of emerging market portfolio flows have been more actively investing in African debt securities, buying securities issued by many first-time sovereign issuers (Gabon, Ghana, Seychelles).

The combined African equity markets account for about 12% of global emerging markets, but attract less than 2% of portfolio equity flows. This under allocation is mainly the result of a relatively poor liquidity in African markets and difficult access to quality financial information and research on many African companies and issuers. Despite their volatility, emerging market portfolio flows remain a vast untapped potential source of capital for frontier African markets.

Table 2: Financial flows in Sub-Saharan Africa 2000 – Q1 2009 (USD Billion)



Source: IMF, 2009 (2009 data are estimates)

Supporting the development of African financial markets

The importance and the impact of financial markets in Africa are often underestimated, if not overlooked. This is the result of a relative lack of understanding of African financial markets among governments and multilateral institutions, making it difficult for them to design appropriate and effective policies. The lack of timely and accurate data and the relative weakness of market participants is a major impediment to attracting emerging market portfolio flows. Governments should lead the way by further promoting the sale of state-owned assets through financial markets[5], create sovereign benchmarks to provide reference points for private sector borrowings and create fiscal incentives for investing in financial assets. Development agencies could also play a key role by investing in strengthening the capacity of market participants and by subscribing to and exiting from more investments *via* the financial market, in order to improve their liquidity. There needs to be a proactive approach to promoting the creation of more financial assets, including listed companies, corporate bonds issues, collective investment schemes, among others, to offer a broader investment spectrum to local savers. ●

[4] Emerging market portfolio flows refer mainly to the investment holdings of international investors in local securities (listed equities and long- and short-term debt) as opposed to direct investments by international investors in local assets, which are recorded as foreign direct investments.

[5] On this subject, see Laurent Demey's article on the political use of stock markets to promote privatisation programmes.

AFRICA'S FINANCIAL MARKETS: A REAL DEVELOPMENT TOOL?

Popular shareholding in Africa – which could have failed due to the weakness of financial systems – has today become a local reality. It has been led by the political will of States to include the population in their privatization programs and has also given the public access to long-term savings products. Laurent Demey, Deputy CEO of Proparco, takes a look at these developments. Some of them – such as the promotion of employee savings – have been supported by Proparco.

Popular Shareholding in Africa, both a Political and Financial Tool

Popular shareholding in the context of Africa would seem doomed to failure, yet it has now become a major development area for African financial markets. This type of equity ownership seems to have met with real popular success, particularly with urban executives. But it has especially been a success for governments who see it as the tool they require to implement privatizations. By promoting the participation of the population in a company's initial public offering it is possible to reach both economic and political targets – to gain long-term popular support and, at the same time, develop new savings products.

By Laurent Demey, ***Deputy Chief Executive Officer of Proparco***

Laurent Demey
Proparco

Laurent Demey graduated from the École Centrale de Paris and holds a postgraduate diploma in development economics from the École Normale Supérieure. He held several positions at Société Générale before heading the Group's brokerage firm in Abidjan. He joined Proparco in 2000 as an investment officer and went on to become head of the Banks and Financial Markets Department. In 2004, he set up an AFD agency in Bangkok and a regional Proparco office for East Asia. He was Investment Director from 2006 to 2008. Laurent Demey is now Proparco's Deputy Chief Executive Officer.

Today, Africa continues to remain poor with an extremely low level of access to banking services. If popular shareholding is to be developed, there must be relatively sophisticated financial markets, but the population must also have high savings capacities. Any attempt to establish it in Africa would consequently seem doomed to failure. And yet despite this difficult context, popular shareholding is for most governments and stock market authorities in developing countries a key area for strengthening their financial markets. It is also used as a real communication tool to promote privatization programs. Very few studies have aimed to study popular shareholding in this context and yet it would appear essential to analyze its importance. To do so, its political dimension must not be neglected and it is necessary to show how it may possibly – in various ways – foster the development of the poorest countries.

An African reality: little resemblance to preconceived ideas

The recent study conducted by Grout *et alii* (2009) gives a comprehensive overview of popular shareholding in developed and developing countries. Although individual results are surely questionable – due to the lack of reliable data in many countries – the overall analysis is relevant. Stock market penetration rates among populations range between 10 and 20% in developed countries, between 2 and 8% in emerging countries (or Eastern Europe) and between 0 and 3% in poor countries. The situation in Africa – as shown by the study – is generally difficult, but bears little resemblance to preconceived ideas: a country like South Africa has proportionately more shareholders than Spain, and the figures for Ghana (1.5% of the population) are quite honorable compared to those for middle-income countries (Table 1). These figures are made even more interesting by the fact that they apply to countries where there are extremely high wealth gaps and where investment *via* funds or collective investment entities – the main vehicles for stock market investment in developed countries – is made difficult or even impossible by the low level of market sophistication. In addition, correlation studies show – in a rather counterintuitive manner – that most macroeconomic determinants have little influence on the success of popular shareholding in a country: this is particularly the case for the Gini coefficient that measures income disparities. The only influential criterion is GDP *per capita* which is shored up in rich countries by the extremely high levels of shareholding.

A "bond-oriented" vision

The phenomenon of popular shareholding in Africa – although it does still remain limited – has therefore become a reality. This shareholding has developed in a difficult context: these emerging stock markets have little liquidity and by nature carry risks. The level of savings in these countries is also very low[1] – even though the level of informal savings, which is difficult to estimate accurately, is high. Unfortunately, here again very few studies exist on the behavior of individual African shareholders. Data from field experiments does however provide some indications on their identity; they are mainly urban executives from the middle – or wealthy – classes and work in both the public and private sectors. This investment is seen by the vast majority of them as a long-term investment that will provide regular income in the form of dividends and will consequently build up a nest egg for their retirement. This almost "bond-oriented" vision of investment in shares is reflected in some of the main features of Africa's stock markets: extremely high returns on dividends (three to four times higher than in Europe), often higher than the money market, and the very low level of liquidity. ...

[1] *For example, the rate of access to banking services in Burkina Faso is below 10%.*

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By Laurent Demey, *Deputy Chief Executive Officer of Proparco*

Table 1: Popular shareholding by country

Country	% population	Number of shareholders
DEVELOPED COUNTRIES		
France	14.7	9 000 000
United States	21.2	62 880 000
Spain	2.2	954 348
EASTERN EUROPE		
Poland	2.7	1 000 000
Hungary	0.4	40 000
MAJOR EMERGING COUNTRIES		
China	5.9	76 700 000
Brazil	1.6	3 100 000
Russia	0.14	204 000
Turkey	5.9	4 300 000
SUB-SAHARAN AFRICA		
South Africa	2.6	1 200 000
Kenya	0.37	110 000
Zambia	0.25	29 000
Ghana	1.5	345 000

Source: Grout et alii (2009)

... These shareholders have a much stronger attachment to the companies than in Europe – this can be seen by the extremely high attendance rates at shareholder meetings. This conception of shareholding has, however, tended to evolve over the past few years and has fostered the development of margin loans (loans to buy shares) that are widely available in Nigeria. This type of financing naturally promotes a "short-term" logic and behavior and can cause a major systemic risk in markets that have low liquidity levels. The recent stock market crisis in Nigeria was widely caused by margin loans and should, moreover, make regulators take more rigorous measures. Be that as it may, generally speaking stock market investment in Africa remains an attractive long-term savings product that is adapted to the characteristics of the continent and a financial environment which offers small savers very few choices.

Popular shareholding serves political targets

The development of popular shareholding in Africa mainly stems from political targets – particularly the one that in the 1990s and 2000s led to the implementation of privatization programs inspired by the major donors. Following the example of countries like France at the end of the 1980s, a large number of African governments used the stock market as a tool to promote their privatization programs and allow the population to participate in them. In the 1990s, Côte d'Ivoire made around 20 such operations; Senegal, Kenya, Nigeria, Zambia and Ghana are implementing similar operations. This explains why there is such a high level of shareholders in Ghana. The amounts raised may be modest – proportionate to the size of these economies – but the target remains the same: the general public.

The initial public offering (IPO) of ONATEL[2] in Burkina Faso at the beginning of 2009 is a good example of the reasons for which authorities in these countries support popular shareholding so much. ONATEL, a national telecommunications company that enjoyed a monopoly, was partly sold to Maroc Telecom (Vivendi Group) in 2006 in the framework of a privatization operation. This profitable and renowned company – a flagship for the public sector – was the ideal candidate for an IPO, but its sale to a foreign group caused intense political debate in Burkina Faso. The authorities consequently envisaged the IPO as much as a ...

[2] ONATEL, the national telecommunications office, is the traditional operator in Burkina Faso's telecoms sector. In 2006, 51% of its capital was sold – following an international bid invitation – to Maroc Telecom, a 53%-owned subsidiary of Vivendi Group.

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... financial operation (the State sold 20% of its capital *via* this method) as an operation of political communication and to promote national identity. It was supported by a vast audiovisual campaign mainly targeting the general public which aimed as much to justify the privatization operation as to promote ONATEL. The public was offered preferential price conditions ("ONATEL for the people of Burkina Faso") and priority access to shares.

The operation aimed to raise 29 billion CFA francs (44 million euros). It was, of course, managed by the country's only brokerage firm – SBIF[3] – and was a success: the oversubscription rate reached 140% and 73% of funds raised came from investments made by 3 300 local shareholders in Burkina Faso. This figure may seem low in a country of 14 million inhabitants, but it does become respectable if it is compared to the number of people in Burkina Faso that have a formal job – only 200 000 people, most of whom have a monthly salary that is only slightly above the price of an ONATEL share (80 euros). The target was therefore fully reached: ONATEL was once again a "national company" in the minds of the population. Quite a considerable number of wealthy city dwellers that had become shareholders will consequently feel they are involved in the success of the company. No classic promotional operation could have obtained this result – the strong attachment to shareholding (and dividends) means the message will be exceptionally sustainable.

Creating employee savings

The stock market can also be used as an instrument to promote the participation of a company's employees in its privatization. SONATEL[4] in Senegal followed a path that was very similar to ONATEL. Its IPO in 1999 gave rise to an even greater alliance between economic targets (mainly for savings) and socio-political targets. In a profitable and highly unionized institution such as SONATEL, the privatization would only be accepted if it was accompanied by active employee participation in the company's earnings – this participation was implemented in two phases. In 1999, the State – which was selling the shares – initially granted reductions that allowed 1 470 employees to purchase 10% of the company's capital, valued at 32 million euros at the time. The payment was spread out over time and was withdrawn from the paid-up dividends. This participation today represents some 90 million euros, *i.e.* 40 000 euros per employee, in a country where GDP *per capita* stood at USD 1 066 in 2009. In addition, in the second phase the company sought to both stabilize this shareholding and use this resource to solve the retirement problem – as the public system only left the retired with a very low income. Following an agreement with the unions, in 2004 practically all the shares were transferred to a corporate mutual fund. This type of product was completely new in the country. The mechanism guarantees a nest egg for employees when they retire and means they can top up their income and consequently keep it at the same level.

How to gain long-term popular support and simultaneously develop new savings products

The development of popular shareholding can consequently be fully justified by the simple need to support the series of privatizations that have been taking place in Africa for the past 20 years. These operations – which have widely benefited foreign and often European players – have often been perceived as having been imposed by donors. Moreover, they have often been accompanied by painful restructuring processes. They could therefore only be made with the agreement and participation of the local population and employees. This popular support was even more essential because the privatizations often coincided with a wider democratization movement which compelled governments to be more regularly accountable to populations.

The stock market is consequently a tool that has made it possible to meet several targets – both political and economic – at the same time: involve the population in privatization operations in order to gain its support and, of course, guarantee a high level of national investment in capital. But the main objective was to create a long-term link between the new private company and the local population by targeting the segment of the population that was most likely to influence future political choices – the emerging urban middle classes that are currently propping up the development of the continent. Beyond this socio-political aspect, share investment has also demonstrated its interest as a savings product in countries which often lack such products. The percentage of small investors in these poor countries which is, ultimately, high shows the extent to which the stock market is an instrument that has become a local reality. ●

[3] Burkina Faso financial intermediation company.
[4] The national telecommunications company was set up in 1985 and has traditionally been Senegal's leading telecommunications operator.

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Operating under the name Serena Hotels, the Aga Khan Fund for Economic Development is a major shareholder of TPS EA. They operate luxury hotels, lodges and resorts throughout Africa and Asia. Operations in Kenya began in the 1970s, and the company was floated on the Nairobi Stock Exchange (NSE) in 1997. The group then expanded operations, and in 2006 the holding TPS EA was listed on the NSE. The author explains how opening the shareholding structure through public listing was positive but also restrictive.

Listing on African Stock Exchanges: Many Advantages and Few Drawbacks

The international hotel group TPS EA's listing on the Nairobi Stock Exchange enhanced its visibility and reputation and fostered its commercial development. Moreover, by opening its capital to the general public it has also met the targets set by the main shareholder – the Aga Khan Fund. However, the listing does not only come with advantages. The company must provide a high and regular level of profitability and cannot afford to take too many risks. There are also a whole host of costly requirements in terms of accounting, reporting and corporate governance.

By Mahmud Janmohamed, ***Managing Director of Serena Hotels Africa***

Mahmud Janmohamed
Serena Hotels Africa

Mahmud Janmohamed is Managing Director of Serena Hotels Africa where he is responsible for 31 hotels, lodges and resorts. He is also head of tourism and executive committee member of the Aga Khan Fund for Economic Development (AKFED), founding chairman of the Kenya Tourism Federation, director on the Corporate Governance Board East Africa, and board member on the East Africa Association and Kenya Land Conservation Trust. Mahmud Janmohamed was instrumental in placing Tourism Promotion Services Limited (TPSL, Serena Hotels, Kenya) on the Nairobi Stock Exchange (NSE) and in expanding operations in Africa and Asia.

Tourism Promotion Services (TPS) is an international hotel group that currently owns and manages 31 hotels, lodges and resorts in nine countries under the Serena name[1]. This success is mainly due to expansion, as the group's Kenyan operations, initially named TPSL[2], began operations in hotels and tourism in the early 1970s. Being the first major player to enter Kenya's tourism industry, it played a pioneering role.

The Aga Khan Fund for Economic Development (AKFED) has always been the major shareholder of the group, initially holding 66.7% of TPSL shares, but now holding 60.4% of TPS EA capital. It launched its initial project in collaboration with the Kenyan government, which contributed 33.3% to TPSL capital through the Kenya Tourist Development Corporation (KTDC)[3].

The TPSL group initially assumed investment and business risk through privately funded equity and debt, the ultimate objective being to spread ownership to the broader public once the business reached maturity. This strategy has been applied throughout the East African region. Success was achieved in Kenya by listing TPSL as a public company on the Nairobi Stock Exchange (NSE) in 1997. The group then expanded its operations in Tanzania and Zanzibar and in 2006[4], was restructured under the name TPS EA and listed on the NSE as a public company (TPSL was de-listed), with TPS (Kenya), TPS (Tanzania) and TPS (Zanzibar) as its fully owned subsidiaries.

With its experience in African financial markets, TPS EA is, to date, able to draw up a detailed assessment of the performance of its listing. While listing has certainly provided TPS EA with many benefits, it has also resulted in some drawbacks. Both the benefits and negative implications will be discussed in the following section.

Brand awareness

Among the benefits, the listing has significantly improved the brand awareness of the company, making it easier to expand its activities.

With its enhanced status, market visibility, brand awareness and improved financial standing after floatation on the NSE, the company has expanded and investor confidence among private owners has increased. By creating public awareness of the NSE listing, exposure in both local and regional markets has increased, and business performance and public perception of products and services have improved. Given that shareholders tend to support their own companies, business performance has improved even further. In other words, when suppliers and customers share ownership of the company, business opportunities increase.

However, brand awareness not only expanded business activities, but provided the company with other benefits too. For instance, as a true market leader, the company is well represented in stakeholder groups, and along with other players, provides leadership in articulating the industry's concerns. Therefore, this industry recognition creates a competitive advantage and reinforces the company's position as a good corporate citizen. Due to the prestige and positive company image, TPS EA is able to attract and retain some of ...

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... the most qualified human resources in the industry. In addition, management and staff realise that they have a much larger constituency in terms of stakeholders, which results in increased commitment and dedication. Finally, an indisputable advantage has been the increased publicity and improved perception of the group through the media and analyst reports.

Wider ownership and fund-raising

Interestingly, the case of TPS EA is unique as the company did not initially approach the market for capital increases. Rather, the ultimate objective of the TPSL listing was to spread ownership to the wider public. In 1997, TPSL was floated on the NSE through an offer for sale made by KTDC as part of the Kenyan government's privatisation programme. In the offer, shares representing 23.3% of the issued share capital of TPSL were made available for the public to purchase. Listing thus creates an opportunity for small investors to buy the number of shares they can afford. This enables locals to share in the success of a company through dividends and stock price increases that may result in capital gains.

In just a few years, efforts to further promote public participation within the group have been increased. When TPS EA was floated on the NSE, all AKFED companies and other shareholders, like IFC and CDC, waived their pre-emption rights in order to enable the local Kenyan population to acquire shares. As a result, public citizens are now among the major stakeholders of TPS EA, owning 26.87% of the shares.

Being publicly listed provides companies with vehicles for raising funds by means of issuing new shares and other securities (rights, bonds, etc). In the case of TPS, raising funds was not part of the initial objective of listing, but being listed has provided the company with important financing opportunities. As an illustration, TPS (Kenya), a subsidiary of TPS EA, is currently pursuing the option of issuing long-term private bonds in Kenya for an amount of USD 12.8 million.

It is also important to note that listing not only provides opportunities to raise funds through issuing bonds or shares, it also makes it possible for a company with a good track record to benefit from recognition from financial institutions when it comes to sourcing cheaper funding, and to have access to more competitive interest rates than non-listed companies.

However, while opening shareholding capital to a wider public can be useful for a company to improve its access to funding, it can also be restricting. Companies listed on the stock exchange are expected to maintain dividend payout and profit growth trends year on year. This is seen as 'the success criterion' and can stifle dynamism, unlike non-listed companies that may take priority when re-engineering products and committing funds for expansion, and will accept lower profits and dividend pay-outs in view of the 'bigger' picture.

Increased corporate governance

By having a wide range of stakeholders, the company is continuously under pressure to comply with corporate governance legislation, the various regulatory bodies and best standards, to improve and to be totally transparent in terms of policies, procedures, standards, systems and reporting. The disclosure requirements of the NSE and the Capital Markets Authority (CMA) have led to the development of best practices in board and management processes and activities. In this context, the company adopted triple-bottom-line accounting, which incorporates not only expanding the traditional company reporting ...

[1] Kenya, Tanzania, Zanzibar, Uganda, Rwanda, Mozambique, Pakistan, Afghanistan and Tajikistan.
[2] Renamed TPS Eastern Africa (TPSEA) during restructuring operations, which started in 2004.
[3] At the time, TPSL also obtained a loan from the International Finance Corporation (IFC) to construct lodges and hotels.
[4] Investment partners for this project included IFC, CDC Group Plc (formerly Britain's Commonwealth Development Corporation) and the National Social Security Fund (NSSF) of Tanzania.

Listing on African Stock Exchanges: Many Advantages and Few Drawbacks

By Mahmud Janmohamed, *Managing Director of Serena Hotels Africa*

... framework to take financial outcomes into account, but also environmental and social performance. Moreover, as the company is partially held by the public, there is increased accountability from these shareholders, meaning that additional obligations and reporting requirements of the company and its directors have to be met.

Although, at first glance, the listing seems to provide benefits in terms of corporate governance, several drawbacks can be identified. One drawback is that important and sensitive information, useful to competitors, is available through the reporting of business disclosures. Another is that compliance with the higher level of reporting requirements, as per the regulations from the governing bodies, is a costly exercise. These requirements include providing all shareholders with a physical copy of the annual report, having an AGM once a year and paying annual fees to the various governing bodies and managing share registers.

Challenges still to overcome

In view of the abovementioned TPS EA growth and development philosophy and long-term strategy, it was important, before implementation, for TPS EA management to weigh up the pros and cons of being listed on the stock exchange, from both a micro and macro perspective. The decision to list the company provided a competitive edge and met the objectives of AKFED, which allows East African populations to share in the success of the company.

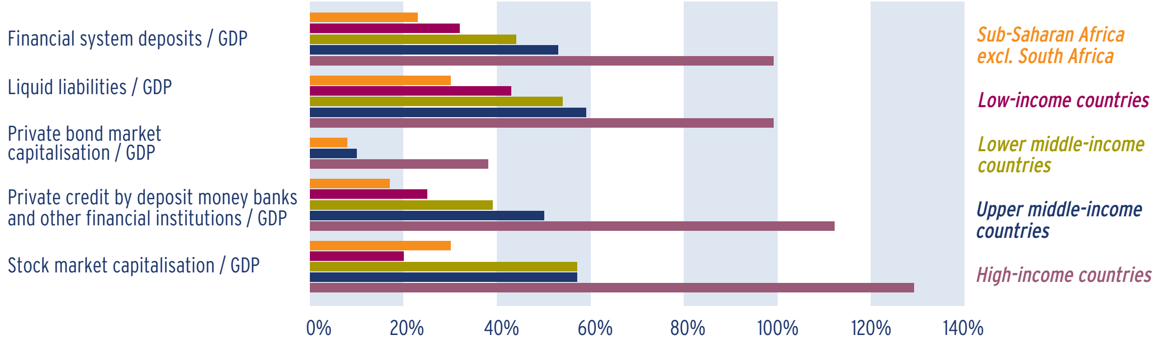
Despite the numerous benefits of listing, it must be kept in mind that this operation is not lacking in drawbacks. In addition to those cited above, the low level of organisation and regulation of African financial markets must also be taken into consideration. For a quoted company, market forces driven by various factors affect the price of the stock. Given that stock exchanges in developing countries are generally less well regulated and organised than in developed countries, governing bodies have no mechanism in place to control share price and price fluctuations. Hence, the true value of a company is not always evident, as at times, it may be grossly under- or overvalued. ●

AFRICA'S FINANCIAL MARKETS: A REAL DEVELOPMENT TOOL?

Key data

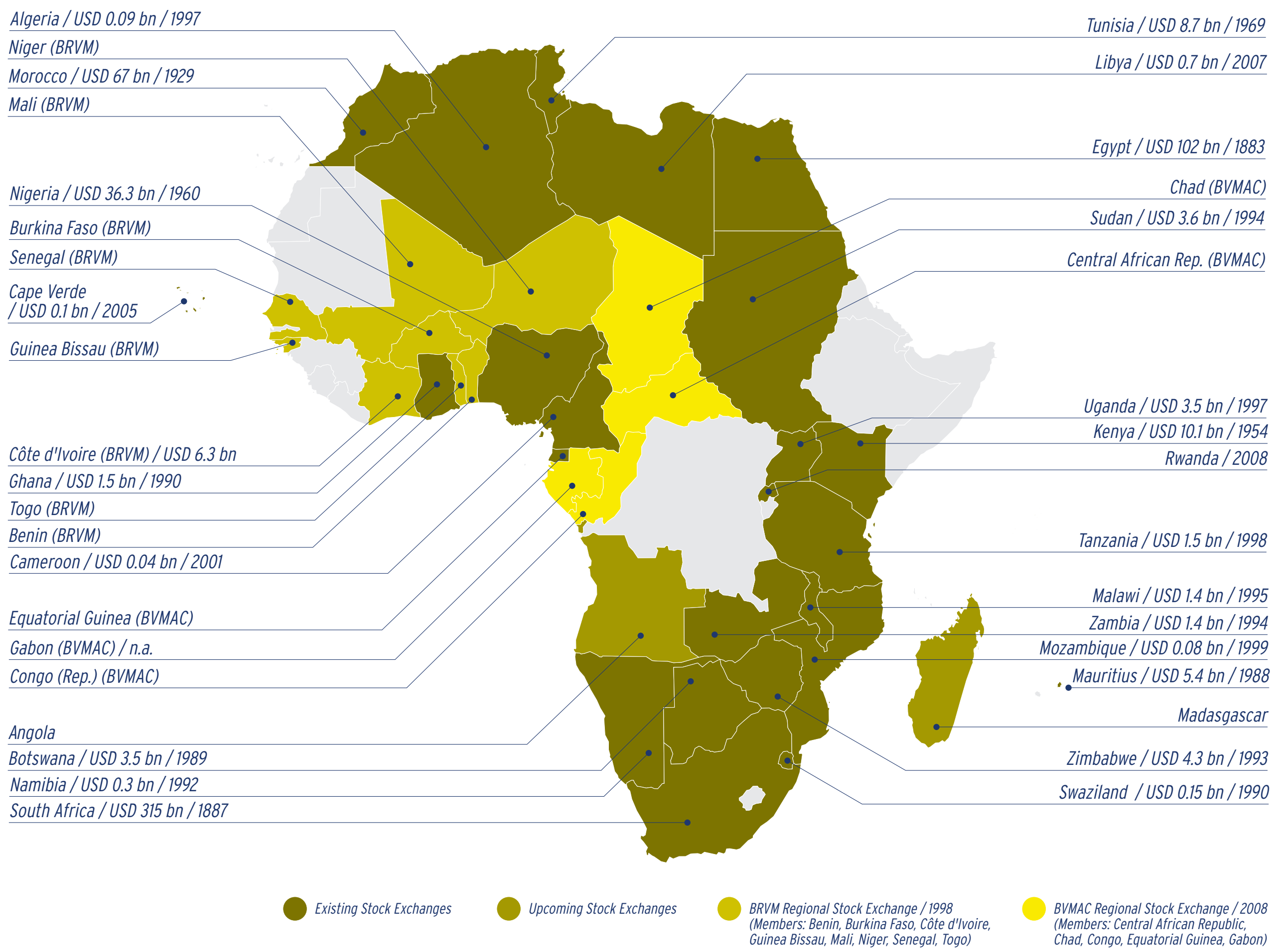
Sub-Saharan Africa's financial sector may be relatively underdeveloped compared to other continents, yet its stock market issues have recently achieved encouraging performances in both numbers and volumes. Indeed, since the late 1980s national and regional stock markets have been increasingly established in Africa and today there is practically continent-wide coverage. However, great disparities still exist between the handful of major markets like South Africa or – to a lesser extent – Nigeria and newer markets that remain very small and lack liquidity. These figures provide an overview of the development of Africa's financial markets whose rapid expansion is closely correlated with economic development and the size of local banking systems.

Financial system size indicators - average values in 2007



Source: World Bank Financial Structure Dataset, 2009

African stock exchanges and their market capitalisations (excluding debt)

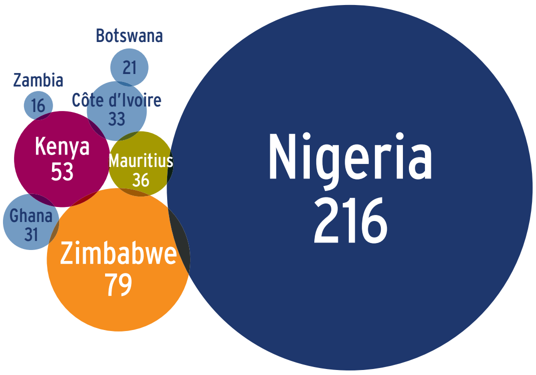


For each country the date refers to the creation of the stock exchange.
Source: Figures are based on calculation made by Private Sector and Development on the basis of IMF, National stock exchanges, DB research; Enko Capital research

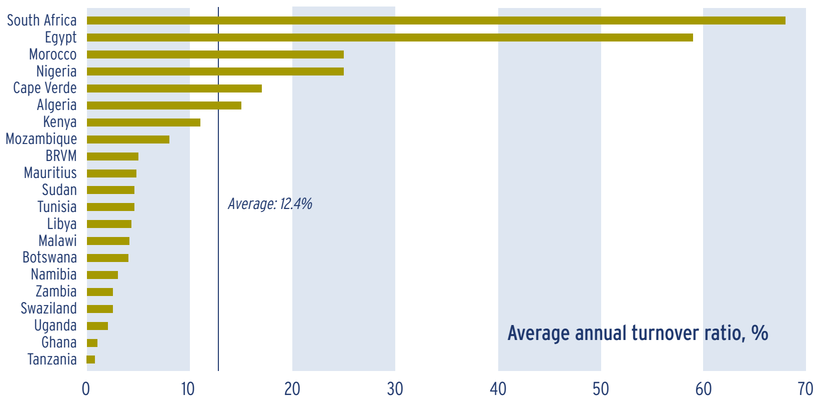
Correlation between GDP, market capitalisation and turnover on African stock exchanges (2007)

The bigger the disc the higher the market capitalisation. Source: S&P, IMF, African Union, stock markets websites

Number of listed domestic companies in 2008



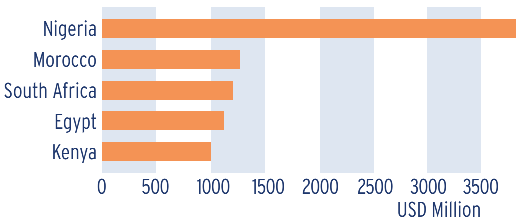
African financial markets' liquidity in 2008



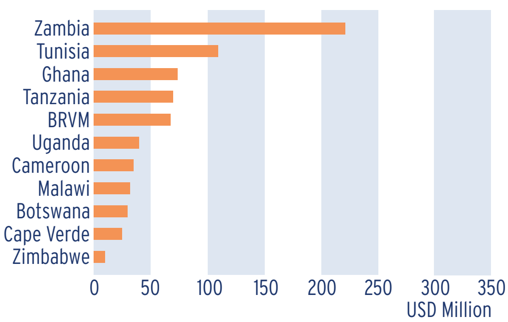
Turnover ratio: annual volumes traded divided by market capitalisation.
Turnover of Swaziland and Algeria based on 2007 figures.
Source: Enko Capital research

Value of new issues on African stock exchanges between 2007 and Q3'2009

TOP FIVE MARKETS

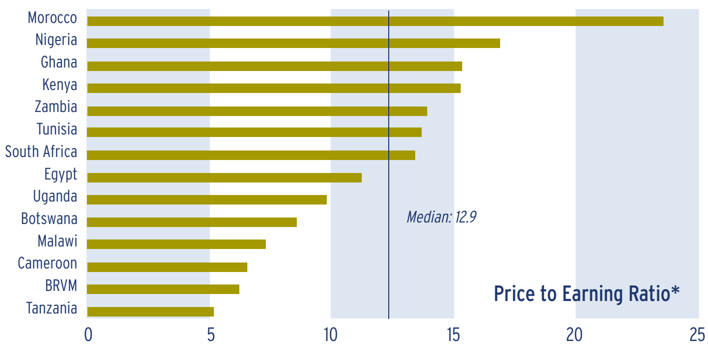


OTHER MARKETS



Source: Enko Capital research

Average price to earnings ratio on different financial markets in Africa between 2007 and Q3'2009



**The Moroccan P/E of 23.2 means that shares are traded, on average, at a price that is 23.2 times equivalent to the net earning per shares of the concerned firms.*
Source: Enko Capital research

In the 1980s, creation of the Ecobank Group was promoted by the Federation of West African Chambers of Commerce and supported by the Economic Community of West African States, so as to build a private Pan-African bank that would contribute to Africa's development. In 2006, the group's holding (ETI) undertook the first simultaneous listing on three stock exchanges in West Africa, a move that has implied, beyond the challenges, many advantages for both the group and the markets.

Motives for a Multiple Listing on African Stock Exchanges: The Ecobank Experience

In 2006, Ecobank Transnational Incorporated launched a simultaneous public offering operation on three African stock markets. This exceptional listing gave the group greater financial flexibility, a diversified, popular and truly pan-African shareholding and enhanced its reputation and financial rigor. Moreover, such operations promote regional integration and improve the depth and liquidity of markets which also benefits shareholders. Despite heavy administrative constraints, this type of multiple public offering should consequently be promoted in Africa.

By Arnold Ekpe, *Chief Executive Officer of Ecobank*

Arnold Ekpe
Ecobank

Mr. Arnold Ekpe holds degrees in mechanical engineering with first class honours from Manchester University and a Business Administration degree from Manchester Business School. Mr. Ekpe has been the Group Chief Executive Officer of Ecobank Transnational, Inc. since 2005. Prior to that, he was the Managing Director and Chief Executive Officer of United Bank for Africa. Mr. Ekpe has more than 28 years of African and international banking experience and has executed landmark trade and corporate finance deals in West and Southern Africa.

In 1985, under a private sector initiative spearheaded by the Federation of West African Chambers of Commerce and Industry (FEWACCI) with the support of the Economic Community of West African States (ECOWAS), Ecobank Transnational Incorporated (ETI) was established in Togo as a bank holding company with a dual mandate: firstly, to build a world class African bank; and secondly, to contribute to the economic integration and development of Africa. Today, the Ecobank group has operations in 29 countries with 800 branches and offices and a staff complement of more than 11 000 professionals. It generates more than USD 1 billion in gross revenues and has a balance sheet of approximately USD 9 billion. Ecobank's performance to date, along with that of other banks in Africa, confirms that Africa is a good investment destination despite perceived risks.

ETI was incorporated as a public limited liability company with an authorised capital of USD 100 million. ETI's initial paid-up capital of USD 32 million was raised from more than 1 500 individuals and institutions from West African countries. The largest shareholder was the ECOWAS Fund, the development finance arm of the ECOWAS.

In 2006, for strategic reasons, the Ecobank Group undertook the first and only simultaneous multiple listing of its shares on all three stock exchanges in West Africa: the Ghana Stock Exchange (GSE), the Nigerian Stock Exchange (NSE) and the BRVM, the regional stock exchange for Francophone West Africa.

Multiple listing provides financial flexibility for Ecobank's future capital needs

The multiple listing provided financial flexibility for the group's future capital needs and it was paramount for Ecobank, as a truly Pan-African Bank, to have access to available and suitable capital markets in West Africa. This was exemplified by the raising of more than USD 550 million on the three exchanges in the middle of the financial crisis in 2008. ETI share capital has thus remained very diverse. Institutions, individuals and the group's staff constitute the shareholding base. There is no majority shareholder. Today, ETI's paid-up capital amounts to USD 775 million owned by about 175 000 shareholders, most of whom are African, and of which more than 170 000 are individuals. Geographically, the shareholding base spreads across Africa and Europe. Moreover, since its listing, ETI's share price has performed reasonably well in spite of the downturn in the capital markets, mainly thanks to the solid financial performance of the group (Figures 1 and 2).

Transparency and brand awareness

Raising the standard of transparency about the group's operations has also been a motivating factor for listing. Along with the fact that the group reports according to IFRS[1], providing information on the group's operations and financial results to meet the requirements of the different stock markets ensures that the group maintains a high level of financial discipline and rigor.

Ecobank brand awareness is strong across Africa and this, as a tool for business development, is obviously an advantage that the group has derived from the ETI multiple listing. 2006 and 2008 Initial Public Offerings (IPO) campaigns have proven to be efficient vehicles to raise and to strengthen awareness of the Ecobank brand. In Ghana for instance, Ecobank is fast mobilizing deposits as investors prefer to use the bank given its listing and membership of a pan-African banking group. This improving awareness of the brand ...

[1] *International Financial Reporting Standards*

Motives for a Multiple Listing on African Stock Exchanges: The Ecobank Experience

By Arnold Ekpe, ***Chief Executive Officer of Ecobank***

has also made it easier for the group to expand its footprint through acquisitions of other structures. Indeed, the requisite level of transparency and financial discipline associated with its listings means that it is easier to convince central banks to consider acquisition proposals.

Multiple listing generates liquidity to shareholders

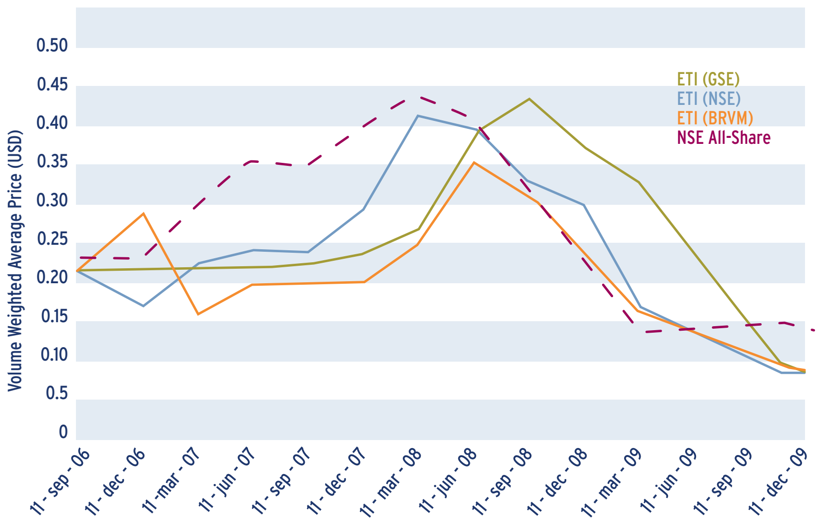
Enhancing the liquidity of ETI shares was also one of the objectives of the multiple listing. Stock markets in West Africa have limited depth and liquidity and listing Ecobank on any one of these markets alone would have limited the liquidity of the shares. The triple listing provided convenience to shareholders in terms of the ability to easily trade the shares. Multiple listings also expose the bank to a wider investor base, especially retail investors, as it helps to improve investors' choices relating to preferred sale points. The different markets have actually provided convenience for shareholders of the various regions to sell in their respective markets. For example, it would have been difficult for retail shareholders in Nigeria to sell their shares if ETI shares were listed only in Ghana or vice versa. As a consequence, ETI is now one of the most actively traded stocks on the BRVM and the Ghana Stock Exchange, which has in turn helped to improve the liquidity of these exchanges (Table 1).

Building an integration tool and deepening financial markets

There was also an important developmental objective in deepening and integrating the economies and capital markets of the countries in which the group operates. This motivation is grounded in Ecobank's belief that the financial sector is central to meaningful economic development, especially in the current globalised world. A strong financial sector can provide the capital needed for other sectors of Africa's economy.

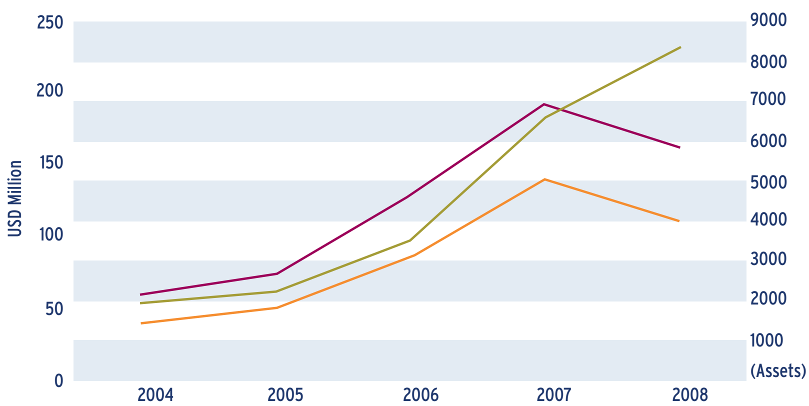
An exciting benefit is the platform the group has offered participants in different markets to use alternate neighbouring markets. The stocks were listed at the same price but with time there were arbitrage opportunities because of market imperfections. Arbitrage opportunities have thus been possible, for the sole benefit of investors. Investors can actually monitor price ...

Figure 1: ETI price evolution since listing



Source: Ecobank Development Corporation/Country Stock Exchanges, 2009

Figure 2: Evolution since listing: profits and assets



	2004	2005	2006	2007	2008
PBT (USD mn)	60	74	129	191	162
PAT (USD mn)	40	51	86	139	111
Assets (USD mn)	1 910	2 199	3 504	6 550	8 306

Source: Ecobank Transnational Inc. Annual Reports, 2009

Table 1: ETI volumes traded since listing (USD million)

	GSE	*NSE*	*BRVM*	*Total*
2006	45.45	204.66	13.63	263.74
2007	320.71	1 245.02	47.03	1 612.76
2008	314.05	891.72	63.42	1 269.18
2009*	6.22	869.88	23.50	899.60

**As at November 23, 2009*
Source: Ecobank Development Corporation/Country Stock Exchanges, 2009

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... movement on the various markets and use the information on where to buy or sell to their advantage. This helps to identify the bottlenecks in executing cross border transactions and as such, resolution of trading inefficiencies has been greatly enhanced. This will aid in the regional integration efforts of the three markets. Ultimately, as information feeds through the various exchanges, the market imperfections will get corrected and the simultaneous listing will enable regional markets to become more efficient.

Multiple listing: an experience to be replicated despite the challenges

Multiple listing does have its drawbacks. Audit and compliance costs are higher compared to single listing because of the different requirements of each stock market. Administrative issues including accounting disclosures, prospectus disclosures, financial formats, and governance requirements are all subject to multiple securities laws. Moreover, transaction costs, such as brokerage, listing and other costs are higher. Finally, market imperfection and arbitrage opportunities also have to be dealt with.

However, Ecobank believes that the benefits of multiple listing outweigh the costs and challenges and that early positioning and involvement in the capital markets of Africa will enhance the group's chances of tapping into the development of these countries in the future. As an illustration, ETI managed to raise more than USD 550 million through a retailled public share offer in 2008, despite the global financial crisis when the offer was launched. The challenges and drawbacks of multiple listing may deter many companies from cross border listing. Thus, measures should be implemented to reduce such costs, by harmonizing procedures to get listed on the different African stock exchanges. •

AFRICA'S FINANCIAL MARKETS: A REAL DEVELOPMENT TOOL?

For decades, the IMF has actively supported African financial markets with both financial and technical assistance. Much data and structural information have thus been collected through their Financial Sector Assessment Programme (FSAP). In order to further improve understanding of financial sectors, the IMF will dedicate greater attention to research. Scott Standley identifies the different determinants of financial market development, identifying market integration initiatives as essential.

What Are the Determinants of Financial Market Development in Sub-Saharan Africa?

Sub-Saharan Africa's financial markets are generally immature and are widely characterized by their low level of activity and the domination of the banking sector. However, if a market and its economy have proportional sizes, it is possible to go beyond the constraints of scale by promoting regional integration. Here again, nothing is simple and it would certainly seem necessary to go slowly. Immediate reforms can however be envisaged, first by improving banking services and implementing stronger legal and regulatory structures.

By Scott Standley, *Senior Research Officer at the Independent Evaluation Office of the International Monetary Fund*[1]

Scott Standley
International Monetary Fund

Scott Standley is a Senior Research Officer in the Independent Evaluation Office of the International Monetary Fund. He was previously a researcher at the Center for Global Development, where he worked on private sector and financial market development in Sub-Saharan Africa. He holds a Master's in Public Policy from Harvard University's Kennedy School of Government and a B.A. in Economics from the University of Pennsylvania.

The benefits of deep financial markets have been extensively documented. Efficient, well-regulated markets mobilise capital and channel resources into productive investments. They also help better manage and diversify risk, mobilise savings and monitor the corporate sector. With this in mind, increasing attention has been paid to developing and deepening financial markets in many Sub-Saharan African countries over the last decade. National development strategies have included plans to create new markets or augment existing ones, and both multilateral and bilateral donors have supported such efforts.

Despite these trends, most financial markets in Sub-Saharan Africa remain underdeveloped and are not yet effective tools for improving economic prospects. The character of each domestic financial sector – and indeed all aspects of each economy – varies across countries, but many have immature domestic capital markets and rely on relatively shallow banking sectors. Outside of South Africa, equity markets in Sub-Saharan Africa are small and illiquid, and few countries operate viable domestic bond markets.

However, according to a large number of studies, the low development level of financial markets is not surprising. Increasing evidence suggests that the size of a financial market is related to the size of its economy. Given the small size of the majority of Sub-Saharan African economies, efforts to further integrate capital markets, in particular by promoting cross-border listings and sharing of technologies, are relevant, in addition to reforms to improve the efficiency of the banking sector and the legal and regulatory environments.

African financial sector: dominant banking sectors and immature financial markets

Banks still dominate the financial systems of most African countries, as few operate efficient capital markets and most tend to rely primarily on commercial banks for finance. The banking sectors of most African countries, however, do not yet have sufficient depth to play a catalytic role in promoting the development of a deep financial sector. Most standard indicators of banking sector depth are low compared to the rest of the world: credit to the private sector is limited, assets are highly concentrated in a small number of banks, and the total volume of assets is low (Table 1). Legal and regulatory structures have also been insufficient in many countries, with property rights poorly defined, contract enforcement weak and creditor protection deficient.

Most Sub-Saharan African countries, meanwhile, do no yet operate a viable stock market. Although there are at least 18 stock exchanges in the region[2], several of these have been largely inactive while others have grown considerably over the past decade – at least until the onset of the global financial crisis. With few exceptions, however, these markets can be described as having few company listings, low market capitalisation and low liquidity (Table 2). The Johannesburg Stock Exchange (JSE) in South Africa is the obvious exception, and in 2008, the JSE accounted for nearly 85% of Africa's total market capitalisation. Although the size of the other African exchanges varies, in general they are small relative to markets in the rest of the world. As an illustration, the total market capitalisation of all Sub-Saharan exchanges, excluding South Africa, was USD 90 billion at the end of 2008 – less than the size of ...

[1] The views expressed in this article are those of the author and should not be attributed to the IMF, its Executive Board or its management.
[2] Including the regional Bourse Régionale des Valeurs Mobilières (BRVM) based in Cote d'Ivoire that lists companies from eight west-African countries.

What Are the Determinants of Financial Market Development in Sub-Saharan Africa?

By Scott Standley, *Senior Research Officer at the Independent Evaluation Office of the International Monetary Fund*

... the Thai exchange (Table 2). Most African exchanges are also relatively illiquid compared to those in other regions; Sub-Saharan exchanges had an average turnover ratio of 10% in 2008 compared to 50% in emerging Asian economies. Such low levels of activity make it difficult to attract the volume of participation necessary to enlarge and deepen markets. Whereas efforts have been made by many exchanges to update their market infrastructures[3] (seen as an obstacle to their expansion), the actual number of trades is still very low. While there are several million trades each year in larger emerging markets such as Brazil, there are fewer than 100 in some larger African exchanges.

If Sub-Saharan African equity markets remain underdeveloped, domestic bond markets are even more so. Few countries in Sub-Saharan Africa have a mature domestic bond market, and existing ones are shallow and inefficient. This can be partly explained by the fact that during the last two decades many African countries relied on easy access to concessional finance – access which impeded the development of domestic bond markets and led to debt profiles dominated by foreign currency. To date, African domestic bond markets are mostly not major channels of capital, as issues are few and erratic and most have short-term maturities of less than a year (Blommestein and Horman, 2007). These characteristics have constrained the establishment of reliable yield curves and pricing benchmarks, and have also limited growth of the investor base.

Determinants of financial market development

Developing efficient financial markets is not a short-term project. Much of the evidence suggests that the main drivers of financial market depth are the policy and institutional environments in which these markets operate – a finding that does not lend itself to quick fixes to prop up markets. Achieving deep and efficient financial markets will likely be difficult in the absence of corresponding policies that promote economic stability and stimulate investor confidence.

While transparent macroeconomic management and general political stability is necessary to attract investment, some specific reforms can be undertaken in the medium term. The legal and regulatory frameworks underpinning the financial system, for example, have consistently been shown to influence the depth of financial markets. To date, both banking sector and capital market development have been constrained by relatively weak regimes. Stronger legal structures and regulatory bodies to better define property rights, enforce contracts and protect investors are needed before financial systems can operate effectively.

The sequencing of reforms is also important, and a strategy may start with initiatives to improve the efficiency of banking services, given evidence that countries with well-developed capital markets also generally have deep banking sectors (Andrianaivo and Yartey, 2009). Financial institutions and markets may grow simultaneously, but a focus on developing capital markets may be premature in countries lacking a sufficiently deep banking sector and adequate demand from firms for alternative financing instruments. An initial focus on improving banking services – such as through upgrading collateral registries and creditor rights protection – may be appropriate (Beck *et alii*, 2009; Gulde *et alii*, 2006).

Financial market size is also strongly related to the size of the economy – a finding that is true for both equity and debt markets – with the size and activity of most exchanges aligned with each country's level of economic development. This suggests that some countries may be too small to develop viable capital markets even with appropriate macroeconomic policies and institutions, leading to calls for regional equity markets and ...

[3] *Most exchanges now have automated trading and a central depository system. The frequency of trading has also increased, with most exchanges trading equities five days a week–though some trade for only a few hours a day.*

Table 1: Banking indicators in 2008

	Credit to the private sector (% GDP)	Bank concentration (% of assets owned by three largest banks)	Deposit money bank assets (% of GDP)
COUNTRY AVERAGE OF DEVELOPING AND EMERGING ECONOMIES BY REGION			
Sub-Saharan Africa	20.9	81.2	23.3
Latin America and the Caribbean	46.0	66.8	50.6
Europe and Central Asia	45.1	64.6	40.0
East Asia and Pacific	57.3	64.4	53.6
South Asia	40.2	53.2	45.3
Middle East and North Africa	46.7	70.1	64.3
COUNTRY AVERAGES BY INCOME GROUPE			
High-income	117.8	73.6	117.4
Upper middle-income	50.9	67.5	54.8
Lower middle-income	40.7	64.7	40.3
Low-income	18.8	79.5	21.2
WORLD AVERAGE	**60.0**	**71.1**	**62.3**

All data is from 2008 where available. Data from 2007 is used for countries where 2008 data was not available. Data on bank concentration, deposit money and bank assets is from 2007. Source: IMF International Financial Statistics; World Bank World Development Indicators; and Beck et alii, 2009

What Are the Determinants of Financial Market Development in Sub-Saharan Africa?

By Scott Standley, ***Senior Research Officer at the Independent Evaluation Office of the International Monetary Fund***

… regional bond issues to help overcome scale constraints. The most prominent regional initiative to date has been the Abidjan-based Bourse régionale des valeurs mobilières (BRVM), although its ability to overcome problems that plague small exchanges has been limited[4]. Establishing functional regional exchanges is complex, requiring significant technological investment and the surmounting of non-trivial administrative and political barriers. For example, participating countries need to harmonise their trading systems, legal regulations, reporting standards and taxation schemes. Stock markets are also potent national symbols, and political resistance may arise in countries joining a regional exchange based elsewhere[5].

The launch of regional exchanges may thus be unrealistic in the short term. Initiatives to partially integrate markets, however, may be constructive alternatives. In particular, smaller exchanges may profit by capitalising on existing systems of more advanced exchanges in their region. Such efforts include cross-listing stocks, harmonising listing requirements and regulations, and jointly using automated systems. Some efforts are already underway. Firms from several countries for example, have already cross-listed stocks both domestically and on the JSE. Exchanges in the Southern African Development Community (SADC) have also tried to integrate more deeply by harmonising their company listing requirements based on the JSE systems. In East Africa, several Kenyan companies have cross-listed in Tanzania and Uganda, and the three exchanges have also established a common Securities Regulatory Authority and initiated a joint automated trading platform. Such efforts should be encouraged more widely alongside strategies to strengthen legal frameworks as constructive steps to help develop financial markets. •

Table 2: Indicators for selected stock exchanges at the end of 2008

	No. of listed domestic companies	*Market capitalization (USD bn)*	*Value traded (USD bn)*	*Turnover ratio (%)*	*Market capitalization (% of GDP)*
Botswana	19	3.6	0.14	3.1	27.4
Côte d'Ivoire	38	7.1	0.32	4.1	30.2
Ghana	35	3.4	0.15	5.2	21.1
Kenya	53	10.9	1.44	11.8	31.6
Malawi	14	1.8	0.06	3.9	41.5
Mauritius	41	3.4	0.40	8.9	39.8
Nambia	7	0.6	0.02	2.8	7.2
Nigeria	213	49.8	19.95	29.3	23.5
South Africa	425	491.3	401.49	60.6	177.5
Swaziland	7	0.2	0.00	0.0	7.8
Tanzania	7	1.3	0.01	2.1	6.3
Uganda	6	0.1	0.01	5.2	0.8
Zambia	15	2.3	0.07	4.1	16.4
Zimbabwe	81	5.3	0.81	5.1	n.a.
SSA sum	**961**	**581.1**	**424.9**	**...**	**89.5**
SSA sum excl. South Africa	**536**	**89.9**	**23.4**	**...**	**24.1**
REGIONAL AND GLOBAL AVERAGES					
Sub-Saharan Africa	69	41.5	30.3	10.4	33.2
Sub-Saharan Africa excl. South Africa	41	6.9	2.3	6.6	21.1
Latin America and the Caribbean	91	78.6	75.4	14.1	33.2
Europe and Central Asia	354	109.0	52.0	34.1	19.6
East Asia and Pacific	534	413.0	714.0	50.5	56.7
South Asia	1 249	137.0	223.0	72.6	25.0
Middle East and North Africa	166	36.4	19.8	37.6	61.7
High-Income OECD	982	947.0	2 530.0	124.4	48.4
OTHER EMERGING MARKETS					
Kazakhstan	74	31.1	3.4	11.7	23.5
Peru	199	55.6	5.1	6.3	43.7
Thailand	476	102.6	116.8	78.2	39.4

Data for Zambia and Zimbabwe is from end-2007. Market capitalisation data for Swaziland is from end-2007 and for Uganda, end-2006. Value traded data for Swaziland, Tanzania and Uganda is from end-2006. Data for Cameroon, Cape Verde, Mozambique and Rwanda is not included due to low levels of activity. Turnover ratio: annual volumes traded divided by market capitalisation.
Source: S&P Emerging Market Database, World Bank World Development Indicators

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[4] The BRVM has branches in each participating country and trading takes place through satellite links with a centralized settlement and clearing system. While the exchange has grown, it still suffers from size and liquidity shortcomings. Activity has also been mostly limited to Ivorian firms and companies in smaller member countries have not benefited substantially.

[5] An announced regional exchange for central Africa never got off the ground after disagreement about the host country. Competing exchanges in Gabon and Cameroon have been essentially inactive.

One of the main stumbling blocks to the development of Africa's capital markets is the fact that taken as a whole the financial systems lack structure. Donors can help them develop; IFC has been operating in Africa for decades and one of its priority areas is to strengthen markets. Thierry Tanoh, Vice President of IFC, explains in this article how development agencies could do more to promote the expansion of financial markets.

How Can Development Partners Support the Financial Sector in Africa?

Although Africa's financial sector was not severely affected by the 2008 crisis, the latter did however reveal its structural weaknesses – including the narrowness of markets and the low level of credit allocated to the private sector. It would consequently appear to be particularly difficult to develop capital markets in this context. Yet it is not impossible: international organizations, by working closely with local authorities, can support this development by providing their advice and expertise. Beyond this, they can have a very direct impact on increasing financial market depth and liquidity.

By Thierry Tanoh, ***Vice President for Africa, Latin America and Europe at International Finance Corporation***

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Africa can be pleased that its financial sectors were not significantly affected by the first-round impacts of the financial crisis in 2008, and this despite a high degree of foreign ownership in the banking system in general. While this is a plus for stability, escaping the contagion of the sub-prime lending crisis that originated in the US also highlights several weaknesses within the African financial sector, as well as low levels of integration and development within the global financial system.

Weak banking sector base

Most African countries' financial sectors consist mainly of banking sectors; only in the more advanced countries is there significant development of corporate bond and equity markets, insurance, etc. The main exception is South Africa with its highly developed financial markets, which will be excluded from this discussion.

The first point to note is that the size of African financial sectors is small, even when looked at in relation to GDP. When it comes to deposit mobilisation and provision of credit to the private sector, Africa lags significantly behind the low-income country average. Of particular concern is the low rate of credit extended to the private sector (below 20% of GDP). Instead, most banks lend to governments through the purchase of treasury bills and other instruments. Figure 1 shows the composition of bank assets in Africa compared to other regions. It shows the much higher amount in direct government obligations and loans to state-owned enterprises than in any other region.

In terms of access to finance, fewer than 20% of Africans have bank accounts, including at registered microfinance institutions.

Banking in Africa, however limited, is nevertheless a profitable business. Banks in Africa tend also to be highly liquid, meaning they have plenty of deposits, typically held as reserves or in short-term money market (often government) instruments. So it may appear that African bankers have little incentive to expand their lending to businesses, especially small businesses, or make efforts to have bank accounts more accessible to the population.

These figures show how complicated it can be to build a sound capital market infrastructure on such a weak financial market base. On the other hand, it also shows that capital markets are needed in order to provide adequate financing to the private sector, new savings products for the population and uses for the high liquidity in banks.

Role of development partners

Development partners can provide a range of assistance to help African governments, financial institutions and markets overcome these barriers and expand financial services in a productive fashion. Support from development partners can take various forms, including, but not limited to, assisting governments to amend outdated or ineffective policies and regulations, providing capacity building to regulatory institutions to implement those changes and to oversee financial institutions, and directly assisting private institutions to improve their practice.

The World Bank and IMF, along with some bilateral donor agencies, are active in providing support to financial authorities to improve overall regulation and supervision of financial institutions and markets. The importance of a strong regulatory environment, backed by effective ...

How Can Development Partners Support the Financial Sector in Africa?

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... supervision, has been highlighted in the recent financial crisis, which exposed many weaknesses in the supervision of financial institutions in developed countries. The need for regulation is particularly important for capital markets. The specialist nature of equity, bond and other capital markets requires sophisticated regulation and oversight to ensure its development. Partner institutions are well placed to provide technical assistance, which must often come from outside Africa, to regulatory bodies. In particular, there is a need to improve efficiency and lower costs to make markets more attractive to firms for new issues. There is also a need for effective regulation of securities markets and application of appropriate standards to securities issued. African market regulators will require ongoing assistance as they develop and become more sophisticated.

In the African context, there is also potential to integrate financial markets further in order to address some of the issues related to both the size of the markets and the quality of regulation. For example, this has been done effectively in the CFA[1] zone through initiatives to establish regional securities markets, and should be promoted further. Partners can assist by bringing their experience from other regions to help address regional policy and institutional issues.

Apart from regulation and supervision of the financial sector, other measures can be supported by multilateral and bilateral agencies. For instance, following the financial crisis, risk management and corporate governance have become even more important in assuring sound management of financial institutions. Partners can provide advisory assistance to help banks establish stronger risk-management systems and improve their corporate governance to ensure that the interests of all stakeholders are being served.

In capital markets, new institutions or functions are also often required for the development of markets. External partners can help address the risks of greenfield institution start-ups by participating as shareholders and providing advisory assistance during the start-up phase. The IFC has invested directly in several market-making financial institutions, such as investment banks and discount houses.

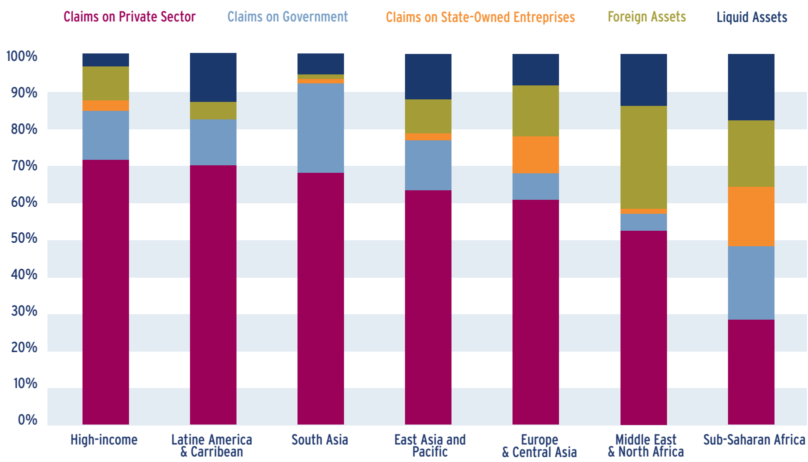
Initiatives to support African financial markets

The IFC, the private investment arm of the World Bank Group, has been actively involved in supporting the development of African financial institutions and markets for several decades. Recently, IFC interventions have been specifically focused on direct assistance to bond and equity markets.

As part of these initiatives, the IFC launched the Efficient Securities Market Institutional Development (ESMID) advisory programme in 2006, designed to work with leading national and regional bond markets to improve their attractiveness to issuers. The objective was to increase transparency and disclosure in bond-market offerings, decrease time requirements and lower costs to promote increased issues. The programme focused on Nigerian and East African bond markets, working with regulatory authorities to improve processes for bond issuance. The first phase of identifying and designing the needed reforms was completed and advisory assistance to regulatory ...

[1] *CFA refers to Communauté financière africaine (African financial community in English).*

Figure 1: Composition of bank assets by region



Source: World Bank Financial Structure Dataset, 2009

How Can Development Partners Support the Financial Sector in Africa?

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... authorities on designing these reforms was provided. In Kenya, for instance, the Capital Markets Authority (CMA) recently unveiled draft laws and regulations that will overhaul the securities industry.

Since the 1980s, the IFC's support of emerging-market development has included issuing local currency bonds. As countries liberalise markets to international issuers, they often prefer a first listing with a supranational to establish an international, risk-free benchmark. In addition, the issues help the IFC diversify its funding base and provide long-term local currency for support of infrastructure and other non-exporting projects in the region. In 2007, the IFC became the first international issuer in the West African regional stock exchange (BRVM) with its CFAF 22 billion (USD 40 million) 'kola bond' issue, earning an emerging markets deal-of-the-year award. This was followed in 2009 in Central Africa with the 'moabi bond' worth CFAF 20 billion (USD 43 million). These issues have helped deepen these fledgling markets and should help attract further issues.

The IFC's investment can also help pave the way for an Initial Public Offering (IPO) on local equity markets. This may take the form of an IFC investment at the time of the IPO, where the IFC's involvement helps reassure other institutional and retail investors of the quality of the issue. For example, the IFC invested alongside the IPO for Onatel[2], the national telecommunications operator in Burkina Faso, and the first Burkina-based IPO on the regional Bourse. The IFC may also invest equity in major companies, with the intent of supporting a broad-based IPO at a later date, in which the IFC may then also participate by selling some of its shareholding. In general, the IFC seeks to exit *via* options such as public listings on local securities markets to help expand the depth and liquidity in those markets. IFC investment in a company can also help serve as a 'stamp of approval' to help pave the way for a subsequent public offering.

Given their significant growth in recent years, stock and debt markets appear to be increasingly relevant tools for firms willing to finance their development. Despite recent growing efforts made by the IFC in these markets, much action is still needed to equip Africa with efficient financial markets. From this perspective, pursuing close financial and technical cooperation between bilateral and multilateral partners, as well as local authorities, seems relevant. ●

[2] See in this issue Laurent Demey's article on the political reasons for the IPO of ONATEL as a public company.

AFRICA'S FINANCIAL MARKETS: A REAL DEVELOPMENT TOOL?

After attaining a PhD in economics from the University of Virginia, Thorsten Beck joined the Research Group of the World Bank where he focused on financial sector development strategy. Today, Thorsten Beck is a professor at the University of Tilburg where he continues his research, focusing on various financial topics. In this article, the author attempts to determine whether it is relevant for a financial system to rely more on banks or financial markets.

Financial Development and Economic Growth: Stock Markets *versus* Banks?

Economic theories diverge radically on the role that banks and markets play in the development of a financial sector – and the link they have with economic growth. It is essential to answer these questions in order to provide concrete orientations for economic policies. Indicators make it possible to link economic growth to the financial system, but there is however no evidence to justify supporting banks to the detriment of markets – or the other way round. From a "service-based logic", it is more the complementarity between these two players that will be a determining factor.

By Thorsten Beck, ***Professor of Economics at Tilburg University and Chairman of the European Banking Centre***[1]

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Economic historians and theorists have provided conflicting opinions on the importance of financial intermediaries and markets for economic development. Joseph Schumpeter (1912) argued that financial intermediaries play a decisive role as they decide which firms have access to society's savings. Joan Robinson (1952), on the other hand, argued that finance follows growth and that the process of economic development needed to be explained by other factors. Lucas (1988) asserts that the role of finance in economic development has been significantly overrated.

Economic history and theory also provide conflicting opinion on the different roles of financial intermediaries and markets. Some arguments have been in favour of a financial system in which intermediaries provide most financial services, while others have focused on the superiority of financial markets.

Across countries, much variation in the development of financial intermediaries and markets can be observed. Variation in the degree to which financial systems are based on these intermediaries and markets can also be observed. Theoretical debate and empirical observation give rise to several questions: Is the development of financial intermediaries and markets related to economic growth performance? Do markets and intermediaries provide the same, substitutable financial services, or are their services complementary?

These questions are especially important in the context of the development policy debate for Africa: given the limited resources and implementation capacities in most African countries, should financial sector policies top the reform agenda? If yes, should there be emphasis on banks or stock exchanges? This paper reviews the theoretical literature and provides empirical evidence on these policy-relevant questions.

Financial development and economic growth

While significant information and transaction frictions prevent savers from easily entrusting their savings to entrepreneurs and firms, banks and markets can, in theory, help overcome these frictions.

Firstly, banks can reduce the cost of acquiring and processing information about firms and potential projects by specialising in the assessment of potential borrowers, thereby possibly increasing saving and capital accumulation in the economy. Furthermore, by identifying the most worthy projects and firms, banks foster innovation and efficient resource allocation. Secondly, banks can lower liquidity risk by pooling savings and investing in both short-term securities and long-term investments. Thirdly, banks allow individual investors to share risk, thus allowing a shift to higher -return, higher-risk projects.

When it comes to stock markets, their increased liquidity gives investors more incentive to invest in the acquiring and processing of information, since they are more likely to realise a return by trading in the market. Stock markets can also improve corporate control and resource allocation by facilitating takeovers and compensating managers according to performance. Furthermore, ...

[1] *This article is based on Beck (2003). Also see Beck and Levine (2002) and Beck and Levine (2004).*

Financial Development and Economic Growth: Stock Markets *versus* Banks?

By Thorsten Beck, ***Professor of Economics at Tilburg University and Chairman of the European Banking Centre***

... markets can ease liquidity risk by allowing investors to sell rapidly in more liquid markets. In light of this, we would expect both the banking sector and stock market development to foster economic growth.

To analyse the link between stock market development, bank development, and economic growth, a sample of 40 countries is used[2], with data for each country averaged over the period 1975-98. To assess stock market development, the 'turnover ratio', a measure of market liquidity[3], is used. To measure banking sector development, 'bank credit', which equals deposit-taking bank claims on the private sector divided by GDP, is used. To assess the relation of banks, markets, and economic growth, real *per capita* GDP growth rates over the period 1975-98 is averaged.

Table 1 represents ordinary-least-squares regressions of the average *per capita* GDP growth rate for the period 1975-98 on bank credit and turnover ratio. Even when including other factors influencing economic growth, such as human capital accumulation, macroeconomic stability and trade openness, the results provide evidence for a robust statistical relationship between banks, stock markets and economic growth.

These results imply an economically significant relationship as well, illustrated by the following examples. Mexico's annual average growth rate during 1975-98 would have been 1.4 percentage points higher than the actual rate of 1% if its level of banking sector development was equal to the sample average of 44% instead of 13%. Similarly, Chile's growth rate would have been 1.2 percentage points above the actual rate of 4.2% if that country's stock markets had shown the liquidity of the sample average of 37% instead of the actual 7%.

Bank-based *versus* market-based financial systems

While the previous section focused on the positive role that both banks and markets play in economic growth, this section emphasises the relative advantages of both. It will examine whether financial structure, *i.e.* the degree to which a financial system is based on markets or banks, influences economic growth.

According to proponents of bank-based financial systems, financial markets do not provide sufficient incentives against free-riding small investors. Since well-developed and liquid markets promptly reveal information to all investors, small investors do not have incentive to invest in the acquiring and processing of information. It is also argued that banks are better exercisers of corporate control, mainly due to the fact that insiders typically have better information about the firm than outsiders. Finally, proponents of a bank-based system argue that banks are better at providing intertemporal risk diversification options.

Proponents of market-based financial systems focus on the problems that powerful banks pose for the efficient delivery of financial services, and thus, resource allocation. Firstly, powerful banks can negatively affect incentive of firms to undertake innovative, profitable projects, as they have inside information, allowing them to extract rents from these firms. Secondly, it is often claimed that banks, due to their insider status, are ineffective corporate controllers. They could become influenced by firm management, colluding against the interests of shareholders. Finally, while banks offer only limited and standard hedging products, markets offer a richer and more customised set of risk diversification and hedging instruments.

At the heart of the debate about banks *vs.* markets is the question of whether one system outperforms the other in efficiently mobilising and allocating savings, thus generating growth. While economic reasoning does not provide enough argument for the superiority of either view, this paper statistically tests the importance of financial structure. **...**

Table 1: Regression of economic growth on bank credit and turnover ratio

Explanatory variables	*(1)*	*(2)*	*(3)*
Bank Credit	1.808 (0.001)		1.185 (0.079)
Turnover Ratio		0.96 (0.008)	0.73 (0.068)
R^2	0.518	0.554	0.608
Countries	40	40	40

Some explanatory variables are not included in this table.
P-values in parentheses. The lower the p-value, the more "significant" the result.
Source: Beck, 2003

[2] *Including 18 developed countries (Australia, Greece, Norway, Belgium, Italy, Portugal, Canada, Japan, Sweden, Denmark, U.S., Austria, Finland, France, Netherlands, Germany, New Zealand and Great Britain) and 22 emerging and developing countries (India, Pakistan, Israel, Bangladesh, Indonesia, Peru, Philippines, Brazil, Jamaica, South Africa, Colombia, Jordan, Taiwan, Chile, Korea, Thailand, Egypt, Malaysia, Mexico, Uruguay, Venezuela and Zimbabwe).*
[3] *As shown by Levine and Zervos (1998) and Beck and Levine (2004), it is the liquidity, not the size of a stock market, that is related to economic growth.*

Financial Development and Economic Growth: Stock Markets *versus* Banks?

By Thorsten Beck, ***Professor of Economics at Tilburg University and Chairman of the European Banking Centre***

... Two indicators to measure the structure of a financial system are used. The first, named 'structure-activity', measures the relative importance of stock markets vis-à-vis banks in a country's financial system. The second, called 'restrict', measures regulatory restrictions on banks' activities[4]. To test the impact of the level of financial development, an aggregate indicator called 'finance-activity' is constructed to account for the development of both financial intermediation and stock markets.

Table 2 presents the results of regressions of economic growth on financial structure. Neither the 'structure-activity' nor the 'restrict' variable has a statistically significant impact on real *per capita* GDP growth. There is, therefore, no evidence in favour of either the market-based or the bank-based hypotheses. By contrast, the 'finance-activity' indicator for financial development enters the regressions significantly. This is strong evidence that cross-country variation in financial development explains cross-country variation in growth performance.

While the theoretical literature has provided many arguments on the relative advantages of both bank-based and market-based financial systems, there is no empirical evidence in favour of either view. Cross-country growth regressions show the importance of the overall level of financial development, rather than the composition of the financial system. This is consistent with the financial services view where emphasis is placed on the services that financial intermediaries and markets provide, rather than on who provides them.

The financial services view also emphasises the complementarity of intermediaries and markets. Well-developed and liquid stock markets can, for instance, offset the negative effects of powerful banks. Furthermore, intermediaries and markets provide funding to different segments of firms, with only the larger and older firms accessing equity finance through stock markets. The importance of markets in relation to intermediaries might increase with the development of an economy. In other words, the structure of an economy's financial system might become more market oriented as the economy develops[5].

All these findings have important policy implications. For one, they are not supportive of policies that favour either financial intermediaries or markets, and thus caution against trying to tilt the playing field in favour of either banks or markets. Also, the results stress the importance of creating conditions for the efficient provision of financial services. For African policymakers, this implies focusing on the policy environment for financial service provision, rather than on establishing stock exchanges where little demand exists. ●

[4] *'Restrict' focuses on the policy environment that determines the structure of the financial system, specifically, the activities of banks relative to other financial institutions and financial markets.*
[5] *On this point, see Scott Standley's article in this issue.*

Table 2: Financial structure and development, and economic growth

Explanatory variables	*(1)*	*(2)*
Structure-Activity	-0.234 (0.674)	
Restrict		0.108 (0.201)
Finance-Activity	0.923 (0.003)	0.914 (0.003)
R^2	0.581	0.603
Countries	40	35

Some explanatory variables are not included in this table.
P-values in parentheses. The lower the p-value, the more "significant" the result.
Source: Beck, 2003

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Lessons-learned from this issue

By Arthur Foch and Anne-Sophie Kervella

Africa's financial systems in general and the banking system in particular – except for those in South Africa – are today among the least developed in the world. For example, the value of loan portfolios allocated by banks and financial institutions to private sectors in Sub-Saharan African countries accounted for nearly 18% of their GDP in 2007, whereas it stood at 26% in the other low-income countries and exceeded 100% in developed countries. Sub-Saharan Africa's financial systems remain widely dominated by banks, yet the banking sectors in this region are generally small – low number of establishments – and their penetration rates in the economy and among the population remain limited. Businesses find it difficult to access banking services and less than 20% of the general public has a bank account.

Financial markets obviously have a role to play in this context, particularly by offering private businesses an interesting alternative to raise the funds they require in order to implement their projects. For example, in Ghana the local stock exchange financed 12% of the increase in the assets of listed businesses between 1995 and 2002. Sub-Saharan African financial markets have also been playing a much more important role in recent years, which can be seen by the increase in their total capitalization excluding debt – from USD 300 billion in 2003 to USD 965 billion in 2007. This went hand in hand with a rise in the number of stock exchanges – which today practically provide continent-wide coverage – and in the number of businesses listed on them. However, debt markets – including public markets – are still in their infancy. However, in all cases, recent developments in Africa's financial markets are promising.

Surprisingly, these evolutions have not only come about as a result of government economic policies seeking to develop the financial sector. They are also due to political strategies aiming to include populations in the privatization programs implemented under the impetus of international financial institutions (IFIs) right from the late 1980s. Indeed, the initial public offerings made by national public companies aimed to gain the support and involvement of the population (traditionally hostile to privatizations that mainly benefitted foreign groups) by promoting African shareholding. This also made it possible to broaden the investor base at the same time. Fourteen stock exchanges were consequently established between 1988 and 1999.

Although the financial markets were initially prompted by political will, they very soon proved to be powerful economic tools for governments, the general public and businesses alike. Listing requirements lead to greater transparency and financial rigor and enhance corporate governance – this consequently helps structure the private sector. In addition to the financial flexibility that stock markets bring them, listed companies also benefit from a better reputation. Moreover, the debt resources that governments can raise on markets provide them with a relevant alternative to the concessional financing they previously had at their disposal. Finally, by offering local savers better quality investment products with a higher level of profitability, financial markets mobilize huge amounts of African savings that are generally tied up in low-productive investments. All these reasons explain why popular shareholding in Africa has now become a local reality and could be further strengthened: African savers increasingly view their investments on financial markets as long-term investments that aim to provide regular income (particularly to prepare their retirement). By capturing private saving and enhancing the financing and structuring of businesses, financial markets contribute to a better allocation of resources and a greater diversification of risks. They consequently actively participate in economic growth. The scale of these positive impacts does, however, differ depending on their level of maturity. It is clear that the bigger the markets are, the greater their liquidity and effects on economic growth will be.

Yet most African countries do not have mature markets. Markets continue to be small. The exceptions are countries like Nigeria or South Africa which count over 100 listed businesses (on average, African stock exchanges generally do not top the 20 mark). In addition, although in 2008 the volume of trade on Sub-Saharan African markets stood at USD 581 billion, 85% of these deals took place in South Africa. Similarly, the average turnover in Sub-Saharan African countries stands at 7% when South Africa is excluded (60%), while the figure reaches 50% in Asia-Pacific countries and 124% in OECD countries. This low level of liquidity makes African markets less attractive and limits their expansion. Moreover, there are inherent ...

Lessons learned from this issue

By Arthur Foch and Anne-Sophie Kervella

... weaknesses to the way African markets operate: the relatively high cost of a listing, (numerous administrative, regulatory and financial constraints, etc.), the scarcity of collective investments, etc. In practice, only a handful of players consequently benefit from these markets: salaried employees in urban areas and businesses with a sizeable financial base.

Governments and donors can help reduce the weaknesses of Africa's financial markets and foster their development. Measures have, moreover, already been taken. Governments have especially sought to increase the number of existing stock exchanges and have promoted the listing of public companies. Donors, for their part, have focused on market regulation by supporting the creation of regulatory institutions and strengthening their capacities. Several initiatives aim to boost regional integration: the creation of the West African Regional Stock Exchange (BRVM) in 1998 and the Central African Stock Exchange (BVMAC) in 2008 are good examples of this target. Although these results are still far from the initial objectives, regional integration does provide an effective solution to the narrowness of African markets.

However, an increasing number of studies affirm that the development of financial markets is more a result of economic growth than one of the vehicles for it. Financial markets must consequently not be seen as a panacea – they are instead powerful tools that can support economic growth. Recent research shows that there is a close correlation between the scale and efficiency of financial markets and that of the banking sector. It would consequently seem that a prerequisite to the emergence and expansion of a financial market is to have a well-developed banking sector; it would therefore appear useful to promote their necessary complementarity as much as possible. •

In our next issue

How to boost the clean energy sector in emerging countries?

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