



**A REVIEW OF BOND MARKET STATUS IN SUB-SAHARAN AFRICA
– 5 BOND MARKETS**

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1.0 INTRODUCTION

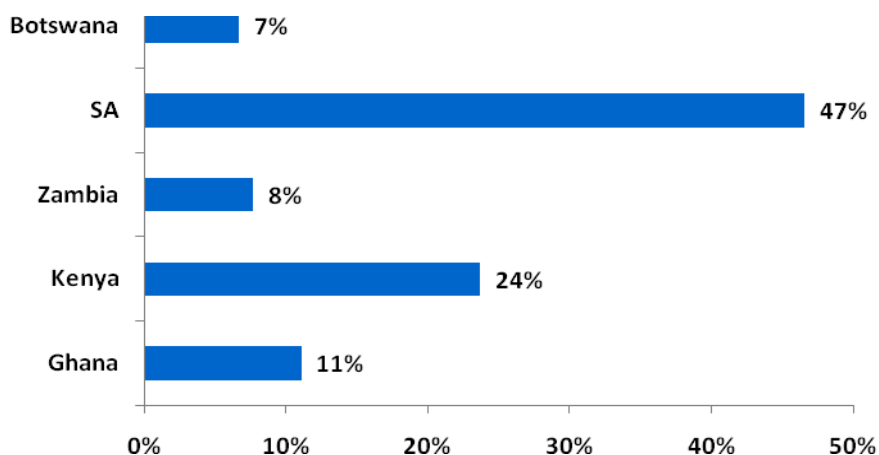
This paper reviews the status of bond markets in five Sub-Saharan African (SSA) countries with specific focus on the trading venues, trading processes, trading methodologies, clearing and settlement infrastructure, fee structure and market transparency. The paper also gives an illustration of the institutional arrangements and the interaction between bond market players in each market. This review helps to show how Botswana's bond market can be benchmarked so as to improve market efficiency and achieve an optimal market structure. The countries reviewed are Botswana, Kenya, South Africa, Zambia and Ghana.

Bond markets in Botswana and Ghana, unlike others under review, have remained shallow, illiquid, inefficient, ineffective and not very transparent. South Africa, Kenya and Zambia's infrastructure developments are at advanced stages while Botswana and Ghana do not have Automated Trading Systems (ATS's). However, it is noted that the Botswana Stock Exchange is in the process of implementing an ATS for equities, bonds and other listed instruments. All the markets have a Central Securities Depository (CSD) system but the extent of involvement of the CSD in clearing and settlement of bonds varies across the markets.

The ATS and CSD are key milestones for bond market development and are crucial in establishing a central order book that will enable market participants to see prices and transactions in real-time. This will improve price discovery and efficiency of the bond market. It also improves regulatory infrastructure and creates a "market". Kenya operates a central order book and the South African bond market is in discussions to move towards establishing a central order book. Botswana and Ghana operate fragmented trading platforms.

Most Sub-Saharan African bond markets are small relative to the sizes of their economies as depicted in Figure 1.

Figure 1: Bond Market as % of GDP as of December 2010



The size of the global bond market reached \$95 trillion as at December 2010, (Knowledge For Markets, 2011) and this was much larger than the global equity market capitalisation of \$55 trillion as at December 2010.

A wide range of economic studies have shown that economic growth is positively correlated to the growth in the size of bond market as the latter is the platform for raising investment capital.

Countries like South Africa and Kenya, with robust investment spending, have much more developed bond markets. In some other countries, such as Botswana, there was either surpluses or had access to substitute capital, hence raising money through bond issuances was less compelling. Comparatively, the markets under review compare poorly with the Association of South East Asian Nations (ASEAN-5) Bond Markets consisting of Singapore, Malaysia, Indonesia, Philippines and Thailand. In the ASEAN-5 Bond Markets, the smallest country's bond market accounts for close to 15% of GDP and the largest accounts for over 90% of GDP, as of December 2010.

Most of ASEAN-5 Bond Markets trade and settle electronically. Even the ASEAN-5 Bond Markets OTC platforms fare well in transparency vis-a-vis international best practices (Knowledge For Markets, 2011). The pre and post-trade transparency requirements are well developed. The post-trade obligations are clearer and beneficial to the market in all ASEAN-5 markets.

The sizes of the 5 SSA bond markets studied vary, with South Africa being the largest.

Figure 2: Size of the Bond Market as of December 2010 ('000,000)

	Market Cap (Domestic Currencies)	Market Cap (USD)
South Africa	1,257,725.6	189,919.9
Kenya	538,600.0	6,684.5
Botswana	6,716.0	1,043.0
Zambia	5,715.4	1.2
Ghana	2,858.4	4,153.7

Figure 3 depicts the number of listed bonds shown by issuer profile.

Figure 3: Number of bonds listed as at December 2010

	Government Bonds	Corporate Bonds	Total
Botswana	12	26	38
Ghana	105	1	106
Kenya	67	16	83
South Africa	134	943	1,077
Zambia	200	7	207

The following section focuses on each of the SSA country's trading venues, trading processes, trading methodologies, clearing and settlement infrastructure, fee structure and market transparency. It also gives an illustration of the institutional arrangements and the interaction between bond market players in each bond market.

2.0 BOTSWANA

2.1 Trading Venues, Processes and Methodology

Trading of government bonds is executed in the over-the-counter (OTC) market via licensed primary dealers. Primary dealers receive orders from clients by telephone or email. After execution (inter-dealer transactions), the primary dealers report the trades (by Reuters) to the central bank, Bank of Botswana (BoB), by latest end of business day. The BoB in turn reports the trades (by email) to the Botswana Stock Exchange (BSE) before close of business or the day that follows and at times after a few days. Sometimes, trade prices are reported after settlement. This is as a result of lack of time limits for trade reporting to the BSE. Trades between primary dealers and institutional clients are not reported to the central bank.

For corporate bonds, clients submit their orders to the brokers over the phone or by email. The brokers then match the trades manually on the floor of the BSE by way of open cry. Some of the trades (book-overs) are booked but still matched by way of open cry on the floor of the stock exchange during trading. The Exchange publishes all the trades in the daily market report. Primary Dealer trades reported to the BSE have a 1 day lag and are sometimes several days behind due to late trade reporting by the BoB. Primary Dealers are special members of the BSE, meaning they are allowed to trade bonds (government bonds only) on the floor of the BSE. This, however, has not been utilised by primary dealers.

2.2 Clearing & Settlement

	Government Bonds	Corporate Bonds	CSD for Bonds*	ATS for Bonds
Botswana	T+3	T+3	Yes	No

*The CSDB has recently commenced transferring bonds into the CSD

- The Bank of Botswana (BoB) is the settlement bank of the government bonds (trades are reported directly to BoB)
- BoB performs securities clearing and settlement of government bonds
- Cash settlement of government bonds is done through commercial banks, who liaise with BoB
- The BSE commenced dematerialization of corporate bonds in mid 2011 to enable corporate bond trades to be settled in the BSE's Central Securities Depository (CSD)
- Corporate bonds settlement is undertaken by the CSD for bonds that are dematerialized
- The CSD has seven participants, being four Brokers and three Custodians (commercial banks with custodial services)
- The CSD also liaises with Nominated Transfer Secretaries (NTS) who maintain both the electronic and manual bond registers and administer securities dematerialisation and transfer
- The BSE's CSD has a single settlement bank which is currently one of the commercial banks

2.3 Fee Structure

	Exchange Fees (%)	Brokerage (%)	CSD Fees (%)	Regulatory (%)
Botswana	N/A*	Max 0.25	N/A*	N/A

Broker commission is on a sliding scale and is dependent on the value of the trade: 0.25% (BWP0 –BWP499, 999) and 0.10% (from BWP500, 000 and above). The sliding scale commission structure is also common in other exchanges.

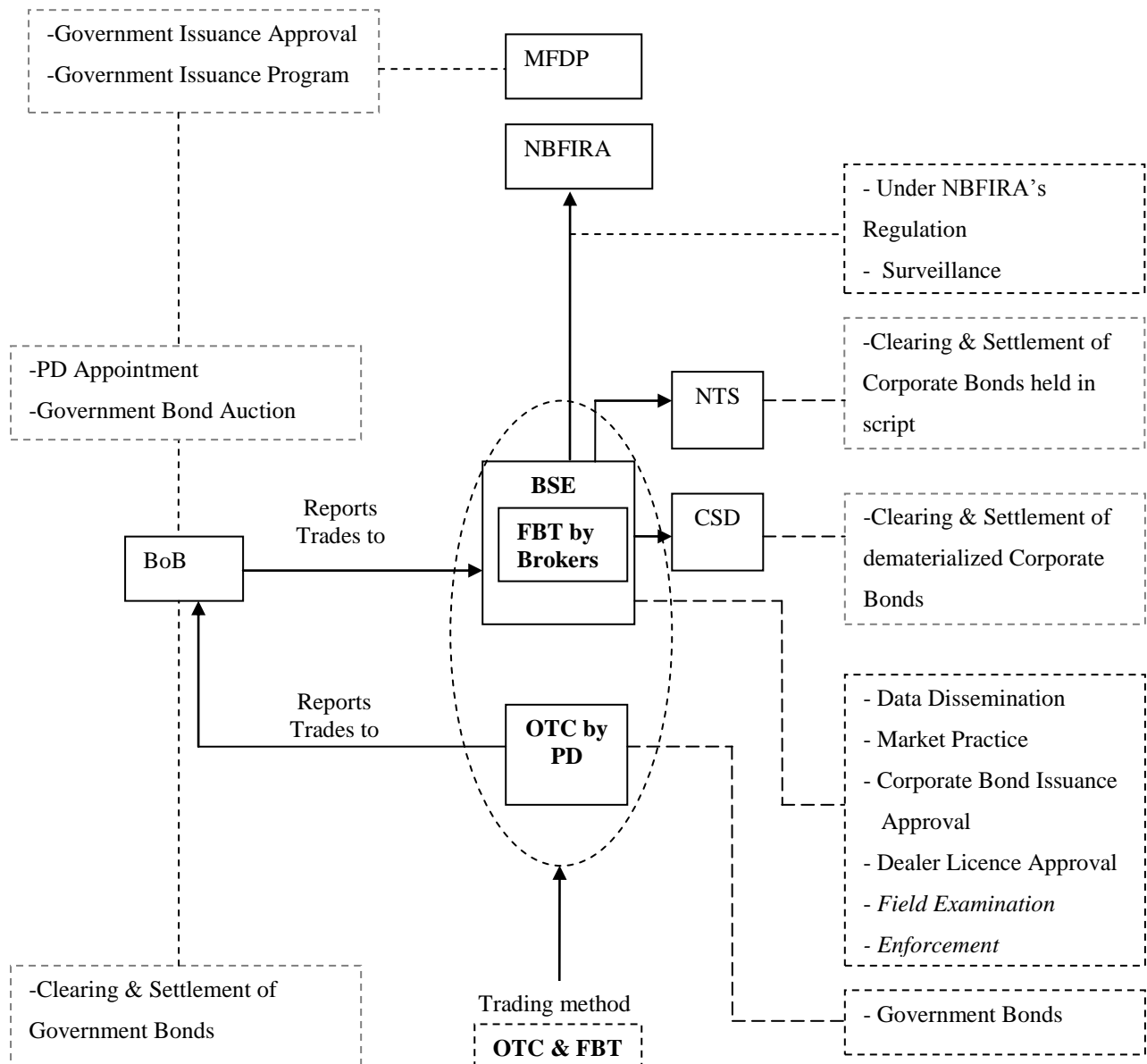
N/A*: Currently, no fees are paid to the BSE and CSD although the proposal is being discussed to introduce these fees as bonds are dematerialized.

2.4 Market Transparency

The OTC market culminates in inefficient price discovery and market opaqueness. Pricing of government securities in the secondary market is unsystematic with clients having to phone each dealer for a price, and each dealer trying to phone the other for the same before reverting to the client. At times bond yields are not updated daily as some primary dealers do not submit quotes daily. Given that primary dealers only report inter dealer transactions, the rest of the trades (which are transactions between primary dealers and the other market participants such as fund managers) are not disseminated to the market. This undermines activity in the bond market and inhibits price discovery.

Corporate bonds enter the market through private placements. No systematic pricing of corporate bonds in the secondary market exists as yields are not monitored on a daily basis. There are no time limits for trade reporting and there seems to be two markets for bonds in Botswana, i.e. for government bonds by primary dealers and for corporate bonds by brokers. There is no central reporting or trading venue.

2.5 Institutional arrangements in the Botswana bond market



Abbreviations

MFDP	Ministry of Finance and Development Planning
BoB	Bank of Botswana
CSD	Central Securities Depository
OTC	Over-the-counter
FBT	Floor Based Trading
BSE	Botswana Stock Exchange
NBFIRA	Non Bank Financial Institutions Regulatory Authority
PD	Primary Dealers
NTS	Nominated Transfer Secretaries

The Ministry of Finance and Development Planning (MFDP) issues government bonds through its appointed agent, the Bank of Botswana (BoB). The Non Bank Financial Institutions Regulatory Authority (NBFIRA) is responsible for regulating capital markets.

The primary dealers, appointed by BoB, are the five Botswana commercial banks. The primary dealers are classified as Tier 1 and Tier 2 primary dealers, based on a number of factors such as clearing facilities and bank capital. Tier 1 primary dealers are allowed to participate directly in the Government bond auction by equally taking up the bonds in auction, being market makers and promoting secondary bond trading. Tier 2 primary dealers also participate in the government bond auctions but are limited in terms of the sizes of bonds they can bid for. However, all banks can participate directly in money market instruments auctions such as those of Bank of Botswana Certificates of deposits (BoBCs).

3.0 KENYA

3.1 Trading Venues, Processes and Methodology

The Nairobi Stock Exchange's (NSE) operates the trading platform, Automated Trading System (ATS), for both government and corporate bonds. The ATS has the central order book. The ATS is accessible to the members of the NSE from their offices but is not accessible to the clients. Orders for both government and corporate bonds are captured through brokers. Brokers receive client orders by telephone or email. For government bonds, the client's order (SELL) is first sent to the Central Bank of Kenya (CBK) for verification with their Central Depository System (CDS) and then captured in the ATS for execution. The BUY order is captured in the ATS and later forwarded by the NSE to the CBK for clearing in the CDS after execution.

Trading in the ATS is done through four trading sessions: Pre-open session where brokers submit orders into the ATS. This is followed by the Open Auction session where the system temporarily closes the order book and starts matching orders. The Regular Trading follows where new orders are continually matched to existing orders and executed. The final session is the Close Session where the order book is closed to allow for the posting of trades and the subsequent generation of market statistics. The market statistics is visible to the clients via data vendors, the daily market report and the brokers. Kenya is in the process of introducing the primary dealer system (by end of 2011). The proposal in terms of trade reporting is for the trades to be reported to the ATS by primary dealers within 10minutes. Currently, trade reporting is immediate, thanks to the ATS.

3.2 Clearing & Settlement

	Government Bonds	Corporate Bonds	CSD for Bonds	ATS for Bonds
Kenya	T+3	T+3	Yes	Yes

- Central Bank of Kenya (CBK) is the settlement bank of the government bonds
- CBK has its own Central Depository System (CDS) for settlement of government bonds
- The CBK's CDS undertakes both cash and securities clearing and settlement

- The NSE's ATS is linked to the CDS of the CBK and the Central Depository & Settlement Corporation (CSDC) of the NSE. In essence, there are two settlement systems in Kenya.
- The CSDC also undertakes both cash and securities clearing and settlement of corporate bonds
- The CSDC has its own single settlement bank which is currently one of the commercial banks but is considering including other commercial banks
- All bonds listed on the NSE are dematerialized

3.3 Fee Structure

	Exchange Fees (%)	Brokerage (%)	CSD Fees (%)	Regulatory (%)*
Kenya	0.0035	0.024	0.0002	0.04

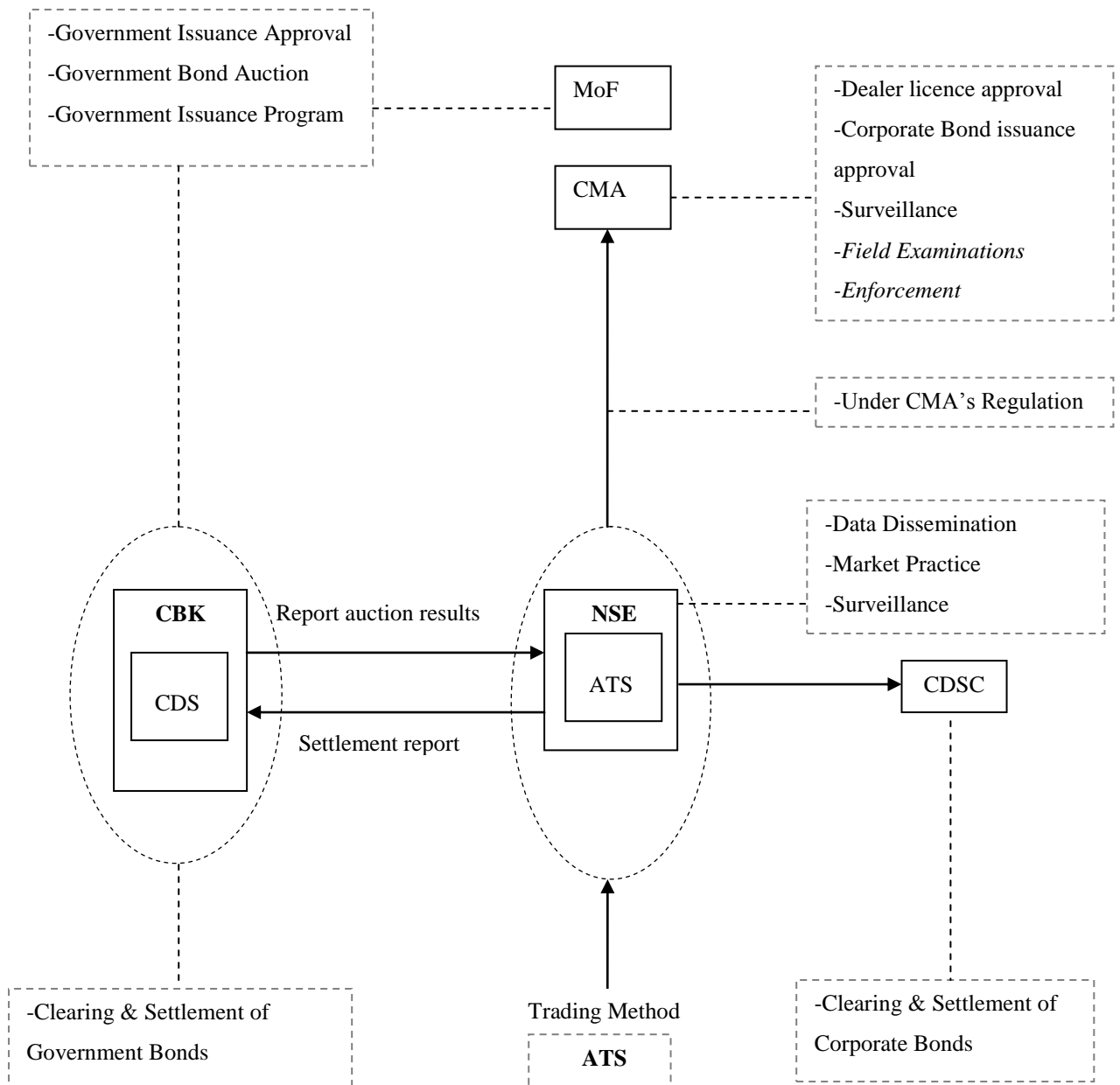
*Investor Compensation Fund

3.4 Market Transparency

Kenya is by far the most transparent and the most developed (in terms of infrastructure) bond market in Sub Saharan Africa amongst the five markets in this review. All government and corporate bonds are dematerialized and trade in an end-to-end automated platform, right from the placement of orders to matching and finally clearing and settlement. Pre and post-trade transparency is very high. Price discovery is highly enhanced during the Open Auction session. Orders are displayed to the market (via the ATS accessible to brokers) before, during and after trading on a real-time basis. Orders are also visible to the market through data vendors such as Bloomberg, otherwise clients can call to enquire on orders.

By introducing the primary dealer system the expectations are that liquidity will improve as uptake of government bonds (through underwriting and market making) also improves. The primary dealers will be connected to the ATS. Thus concerns about price distortions, price discovery and untimely trade reporting are less pessimistic.

3.5 Institutional Arrangements in the Kenyan Bond Market



Abbreviations

MoF	Ministry of Finance
CBK	Central Bank of Kenya (agent for government)
ATS	Automated Trading System
NSE	Nairobi Stock Exchange
CMA	Capital Markets Authority
CDS	Central Depository System
CDSC	Central Depository Securities Corporation

The Ministry of Finance (MoF) issues government bonds through its appointed agent the Central Bank of Kenya (CBK). The Capital Markets Authority (CMA) is the regulator of capital markets.

4.0 SOUTH AFRICA

4.1 Trading Venues, Processes and Methodology

Trading is mainly conducted over the telephone and through Inter Dealer Broker (IDB) systems. Government and corporate bonds are traded by both primary dealers and brokers in the secondary market. The deals are negotiated by parties involved and then reported to the Johannesburg Stock Exchange (JSE) where trades are matched and settled. The JSE operates a trade reporting system called Nutron or the Report-Only System for reporting, booking and matching of deals. There is mandatory reporting of trades to the JSE. The deals must be reported to the JSE within 30 minutes.

In essence, trading occurs in the OTC market since there is no central order book for bonds but the JSE is lobbying for the creation of a central order book. The use of the IDB system affords the rest of the dealers the opportunity to see market orders and trades on a real-time basis and the opportunity to participate in such. The Exchange publishes the trades on the daily market report.

4.2 Clearing & Settlement

	Government Bonds	Corporate Bonds	CSD for Bonds	ATS for Bonds
South Africa	T+3	T+3	Yes	No

- Clearing and Settlement is centralised and conducted through STRATE, the South African Central Securities Depository (CSD) system
- The South African Reserve Bank (SARB) only undertakes cash settlement of government bonds and the RSA Retail Savings bonds
- There are five STRATE settlement banks (CSD Participants), being the four main commercial banks and the SARB
- The CSD Participants handle the cash settlement and scrip settlements for all debt market participants
- Some bonds are held in electronic form through the STRATE whilst some bonds in the market are still held in paper form

4.3 Fee Structure

	Exchange Fees (%)	Brokerage (%)	CSD Fees (%)	Regulatory (%)
South Africa	N/A	0.005	N/A	N/A

N/A: In South Africa, the fee structure is the least cumbersome. Clients only see the brokerage commission on the contract note whilst the dealer absorbs all other trading costs levied by the JSE and STRATE. These costs are lumped and paid monthly.

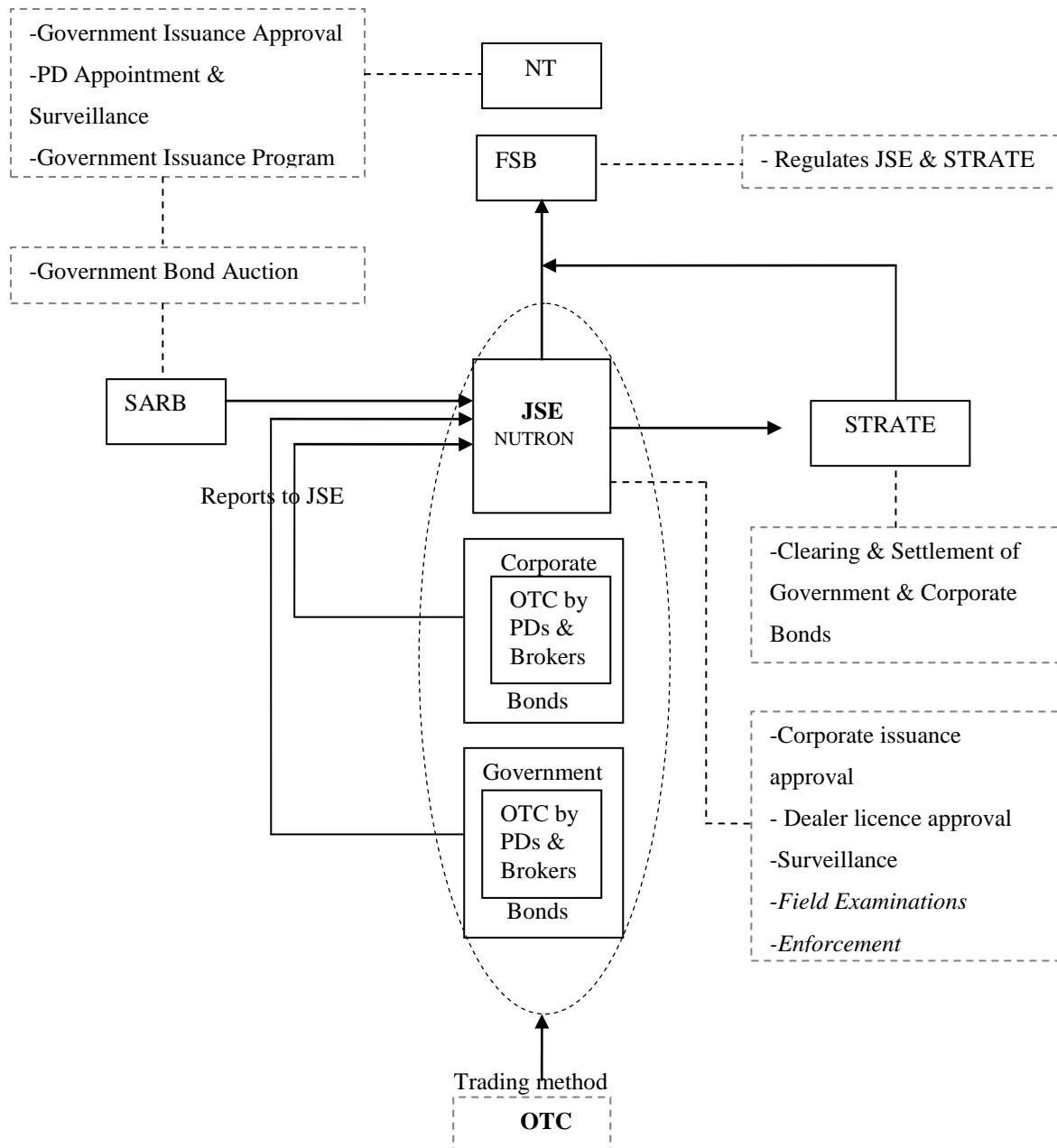
4.4 Market Transparency

The South African bond market is the deepest and broadest in Sub Saharan Africa. However, the existence of primary dealers is perceived as evading transparency, price discovery and also potentially inducing market manipulation, especially in the

secondary trading of government bonds. Nevertheless, primary dealers don't act collusively (they do not necessarily agree on and fix quotes) and they sometimes rely on inter-dealer brokers to act as intermediaries that carry information on prices and deal sizes between them and the buy side.

Such information is deemed confidential and is transmitted via phones, instant messaging, Reuters screens, and voluntarily through IDB screens. The lack of the central order book means trades are only visible to the market post execution.

4.5 Institutional Arrangements in the South African Bond Market



Abbreviations

NT	National Treasury
SARB	South African Reserve Bank (agent for government)
STRATE	South African Central Securities Depository System
OTC	Over-the-counter
JSE	Johannesburg Stock Exchange
FSB	Financial Services Board
PD	Primary Dealers

The Ministry of Finance (MoF), through the National Treasury (NT) issues government bonds through its appointed agent, the South African Reserve Bank (SARB). The

Financial Services Board (FSB) is the regulator of self appointed regulators such as the JSE and STRATE.

The primary dealers, appointed by the National Treasury, are mandated to perform the role of market making for government bonds. Furthermore, all listed bonds are traded in the secondary market through all members of the JSE including banks, primary dealers, asset managers, brokers, inter dealer brokers and issuers.

5.0 ZAMBIA

5.1 Trading Venues, Processes and Methodology

Secondary trading of both government and corporate bonds is executed in the OTC market (via Primary Dealers and Brokers) and alternatively through the Automated Trading System (ATS) at the Lusaka Stock Exchange (LuSE). Primary Dealers and Brokers receive orders from clients by telephone or email. If the Dealer/Broker has both the buy and the sell side, he is permitted to match the trade at his desk and then report it to the Exchange for publication in the daily market report and for clearing and settlement by the LuSE Central Securities Depository (CSD).

However, if the order is not pre-matched it is submitted to the ATS thereby becoming visible to the entire market to match. Trading on bonds happens between 1100hours and 1300hours. So, trades must be reported to the LuSE not later than 1300hours. The dealers do not report any trades to Bank of Zambia (BoZ) which is the central bank, even government bond trades. The clearing and settlement of bonds (delivery from the seller to the buyer), including trades with/between primary dealers, is conducted electronically through the LuSE's CSD which is linked to the ATS. Settlement reports are generated by the LuSE CSD and sent to the BoZ for the BoZ to adjust their holdings of government bonds. The Exchange publishes all the trades in the daily market report.

5.2 Clearing & Settlement

	Government Bonds	Corporate Bonds	CSD for Bonds	ATS for Bonds
Zambia	T+1	T+1	Yes	Yes

- Clearing and Settlement is centralised and conducted through the LuSE CSD, a subsidiary of the LuSE
- The Bank of Zambia is the settlement bank for the Government bonds
- The Bank of Zambia only undertakes cash settlement of government bonds
- All bonds have been dematerialized into the CSD
- The LuSE's ATS is linked to the CSD, facilitating end-to-end trading and settlement for bonds traded through the ATS
- The LuSE CSD Participants are the Brokers and Commercial Banks
- The LuSE CSD has one settlement bank which is currently one of the commercial banks

5.3 Fee Structure

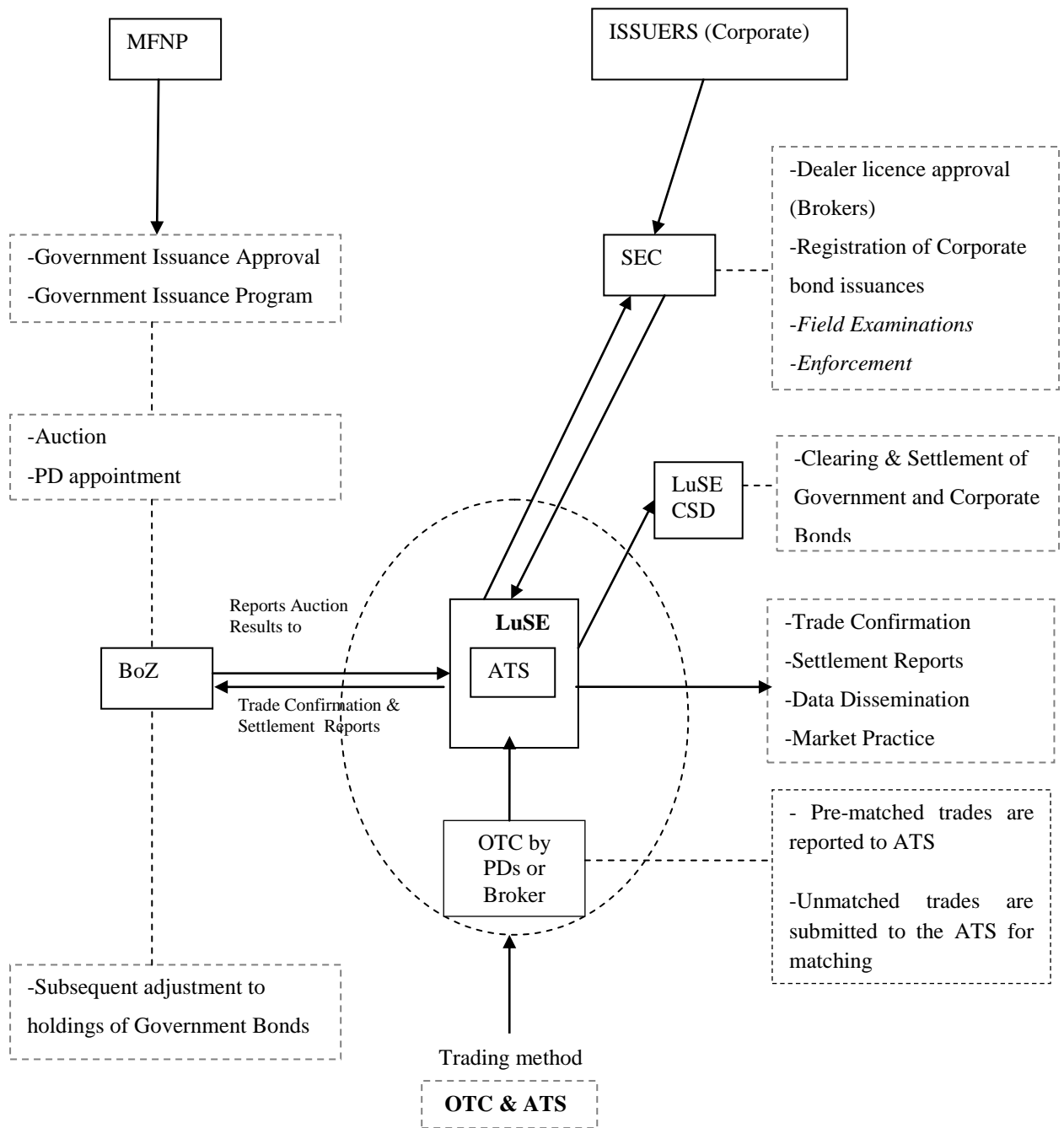
	Exchange Fees (%)	Brokerage (%)	CSD Fees (%)	Regulatory (%)
Zambia	0.10 - 0.060	0.10-0.035	N/A	N/A

N/A: This means the fee is not passed directly onto the client but is rather incurred by the members of the Lusaka Stock Exchange

5.4 Market Transparency

Pre-trade information is available to the market only if the broker or primary dealer was not able to pre-match the order, thereby compelled to submit the order and quotes to the ATS. Sometimes, brokers get to know of transacted orders after trading closes since trades can be pre-matched manually. This limit participation of other Agents if the order was done manually and not submitted to the ATS before trading. The trades are publicised in the daily market report by the exchange at the end of each trading day, without a lag.

5.5 Institutional Arrangements in the Zambia Bond Market



Abbreviation

MFNP	Ministry of Finance and National Planning
BoZ	Bank of Zambia (agent for government)
OTC	Over-the-counter
ATS	Automated Trading System
LuSE	Lusaka Stock Exchange
CSD	Central Securities Depository
SEC	Securities and Exchange Commission
PD	Primary Dealers

The Ministry of Finance and National Planning (MFNP) issues government bonds through its appointed agent, the Bank of Zambia (BoZ). The Securities and Exchange Commission (SEC) is responsible for regulating capital markets. The primary dealers are the commercial banks and are appointed by the BoZ.

Once the bonds are issued they are automatically listed on the Lusaka Stock Exchange (LuSE). Upon the receipt of each bond auction results the BoZ immediately release these results to the LuSE for dissemination through the ATS. After every bond auction, results are sent from the BoZ to the LuSE Central Securities Depository (CSD). On receipt of the auction results the LuSE CSD credits the accounts of successful bidders with the appropriate amount of bonds allotted to them in the auction. The BoZ does not handle secondary market transactions in GRZ bonds. It only gets involved to an extent of debiting and crediting current accounts of Agents (Brokers and PDs) and also adjusting their holdings as per the CSD report generated by the LuSE CSD.

Half yearly interest and maturity money will be paid to the respective bond holders' settlement bank's current accounts at Bank of Zambia. To facilitate interest and maturity payments the LuSE CSD produces a full schedule (a list) of all bond holders and submits this record (called Holders of Record Report – HOR) to the Bank of Zambia. The HOR is released to BOZ 5 working days before the interest payment/maturity (redemption date).

6.0 GHANA

6.1 Trading Venues, Processes and Methodology

Trading of both government and corporate bonds is executed in the OTC market. Government bonds can be traded by both primary dealers and brokers whereas corporate bonds can only be traded by brokers. Primary dealers and brokers receive orders from clients by telephone or email and match the trades outside the floor of the Exchange. Corporate bonds trades by brokers are reported (by email) to the Ghana Stock Exchange (GSE) for publication and to Ghana Securities Depository (GSD) for clearing and settlement.

Government bond trades by brokers and primary dealers are reported (by email) to the Ghana Stock Exchange (GSE) for publication and to the Central Securities Depository Corporation (CSDC) at Bank of Ghana, the central bank, for clearing and settlement. Trades must be reported latest one day after the trading date. The GSE publishes all the trades in the daily market report, usually with a 1 to 2 days lag depending on the time of the day the trades were reported to the GSE.

6.2 Clearing & Settlement

	Government Bonds	Corporate Bonds	CSD for Bonds	ATS for Bonds
Ghana	T+1	T+1	Yes	No

- The Bank of Ghana (BoG) is the settlement bank of the government Bonds
- BoG undertakes cash and securities clearing and settlement of government bonds through the CSD Corporation (CSDC), which is a subsidiary of BoG
- The CSD Corporation is interfaced with the Real Time Gross Settlement System (RTGS)

- The CSD Corporation has 28 settlement banks who undertake cash settlement of government bonds (the 28 banks comprise 27 commercial banks and 1 bank which is a representation of a rural bank)
- The GSD, a subsidiary of the GSE, undertakes corporate bonds cash and securities clearing and settlement
- The GSD has a single settlement bank which is one of the commercial banks. The GSD participants comprise two custodian banks and all the brokers.

6.3 Fee Structure

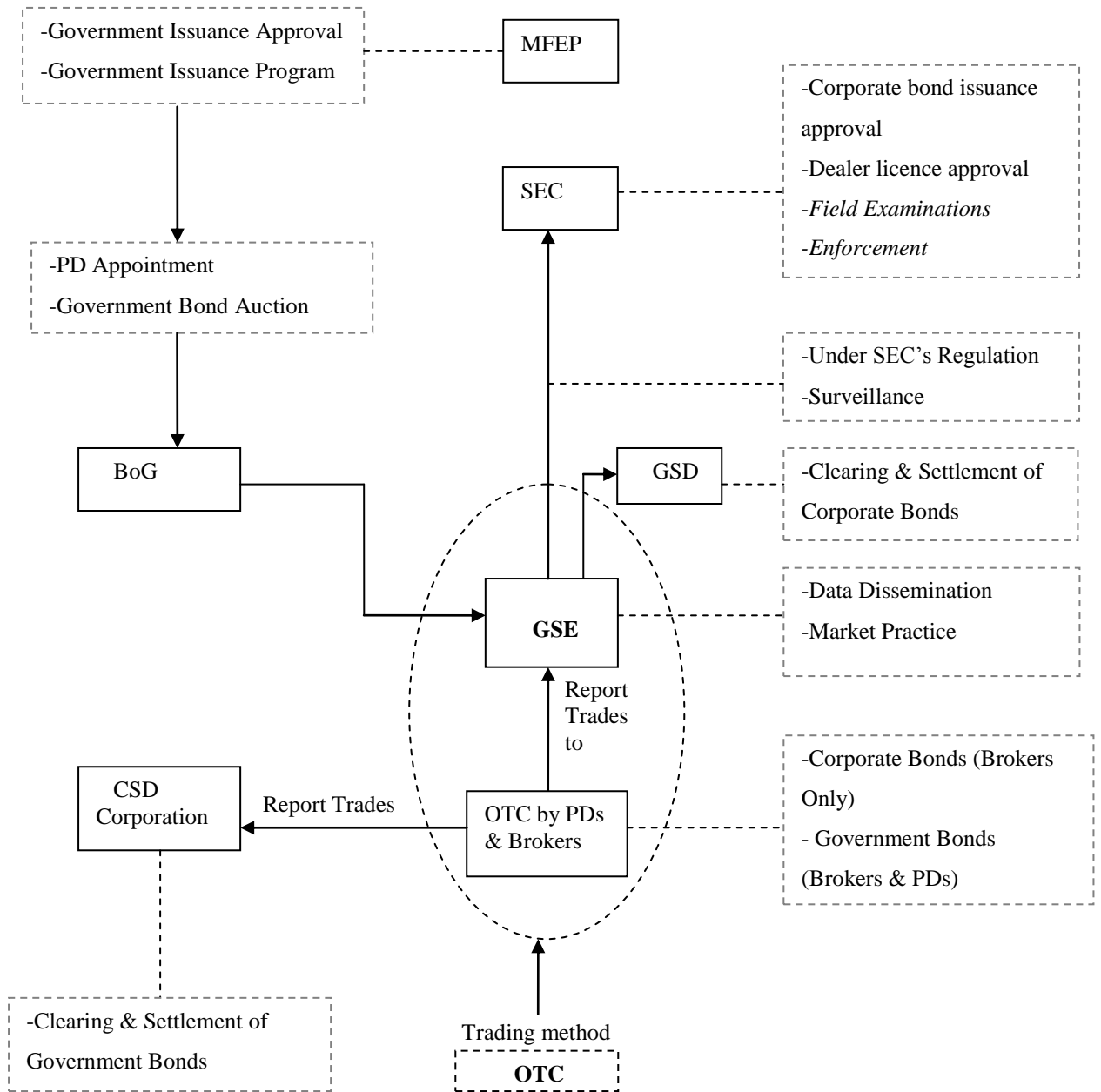
	Exchange Fees (%)	Brokerage (%)	CSD Fees (%)	Regulatory (%)
Ghana	0.022*	Max 0.105	0.009	0.009

*The Exchange Fee above includes a Market Development Fee of 0.002% which is paid to be GSE

6.4 Market Transparency

The OTC market potentially results in inefficient price discovery and market opaqueness mainly because yields are not submitted to a central place (since trades are executed off the floor of the exchange) and are not updated regularly (given the 1 to 2 days lag in trade reporting). Bonds trade over-the-counter with no pre trade orders displayed and this closes out participation by other dealers and brokers and inhibits competitiveness and information efficiency. Trade information is available after execution. Corporate bonds hardly trade and are few so price discovery is highly inefficient.

6.5 Institutional Arrangements in the Ghana Bond Market



Abbreviations

MFEP	Ministry of Finance and Economic Planning
BoG	Bank of Ghana (agent for government)
OTC	Over-the-counter
CSDC	Central Securities Depository Corporation
GSE	Ghana Stock Exchange
SEC	Securities and Exchange Commission
PD	Primary Dealers

The Ministry of Finance and Economic Planning (MFEP) issues government bonds through its appointed agent, the Bank of Ghana (BoG). The Securities and Exchange

Commission (SEC) regulates the capital markets. The Bank of Ghana appoints both the brokers and primary dealers.

7.0 SUMMARY

It is widely known that a mature domestic bond market offers funding opportunities for government and private sector and government bond markets create ideal opportunities for other issuers. They provide a benchmark yield curve and facilitate establishment of overall credit curve. Therefore, the role of government bonds in the domestic bond markets is vital.

In both developed and developing countries, efficient bond markets are characterised by a competitive market structure, low levels of fragmentation, a high level of heterogeneity among market participants, a robust and safe market infrastructure (ATS and CSD) and low transaction costs (IMF, 2001). Botswana bond market should strive to achieve the above by re-assessing the current state of the domestic bond market.

The move towards an optimal market structure for Botswana bond market will be beneficial. Therefore, trading and disclosure practices must become significant factors in bond market development in Botswana. The importance of price discovery, information transparency and efficiency (centralized distribution of market information, e.g. centralised and transparent price dissemination from a central platform), extended market reach, fair price execution (facilitated by centralised pool of liquidity) and efficient settlement and clearing channels are the issues that Botswana bond market has to address.

The issues stated above are also important for attracting and developing a heterogeneous investor base with differing time horizons, risk preferences, trading motives and ultimately improved liquidity.

8.0 RECOMMENDATIONS

Trading Venues, Processes and Methodology

The current trading arrangement in the Botswana bond market which comprise two trading venues, the BSE and the primary dealer system, needs to be harmonized into a single centralised platform at the Botswana Stock Exchange. Regulations already embrace primary dealers as special members of the BSE. Therefore, it will be ideal for primary dealers and BSE brokers to trade at a single centralised BSE trading and/or reporting platform. The envisaged benefits of centralising trading are that late trade reporting will be minimised and transparency will be expected to improve as all deals become visible to the market to price and match. Moreover, market activity will be correctly represented as all trades are executed and captured from a single platform. The transition could optimise these benefits if it coincides with the implementation of the Automated Trading System.

By centralising trading, primary dealers will be compelled to update or avail quotes on a daily basis, thus aiding price discovery and such prices will be sufficiently disseminated through a centralized platform.

Market data compilation and dissemination needs to improve so that information about trades could reach investors on a timely basis and centralising bond trading and reporting will significantly improve this. Moreover, Bank of Botswana (BoB) and primary dealers could be offloaded of current role of reporting trades in government bonds and minimise late trade reporting to the BoB and BSE.

The centralising of trading or trade reporting will facilitate the calculation of an accurate and up to date bond index. This will further enhance portfolio management by fund managers.

A centralised trading platform will also provide for strong regulation and solid surveillance. The present structure presents a challenge as to adequate surveillance of a market in which trading happens in many screens and platforms. It is very susceptible to price manipulations. It will also be conforming to IOSCO principles for secondary markets.

The BSE plans to implement a “dual screen” trading mode whereby certain minimum threshold trades have to compulsorily be traded through the Exchange and any amounts beyond can be traded in “negotiated mode” or traded in Exchange and be reported within a stipulated time.

Clearing and Settlement

The BSE is following convention and international best practise in dematerializing bonds into the CSD. This certainly improves risk management and also eliminates hurdles that could hamper the conventional T+3 turnaround time in clearing and settlement. By settling through the CSDB, the participation of retail investors in the government bond market could be efficiently harnessed. The trend in other markets is that clearing and settlement takes place at a central depository and the Central Bank handles cash settlement of government bonds and in other cases even corporate bonds. The movement of cash is done after the CSD sends settlement schedules to the Central Bank. Therefore, the CSDB should be utilised to carry out settlement of debt instruments even for OTC traded bonds.

Pricing structure

The BSE needs to establish and advertise a bond pricing formula and calculator (for vanilla bonds and variable rate bonds). This initiative will be helpful in resolving disputes where market participants dispute considerations resulting from different, and mostly their own, bond calculators. In most cases, illiquidity is directly linked to an inability to price a bond efficiently through lack of price transparency. Hence, a combination of efficient price dissemination and reliable bond calculators will also help in addressing liquidity problems in the bond market.

Commission Structure

The Botswana bond market (BSE and Brokers) has to formulate a competitive commission structure conducive and relevant for bond trading divorced from the equity referenced commission structure.

Regulatory Issues

Surveillance is key in any market place. Currently, surveillance is based on post-trade information provided by market participants. Given the fragmented structure of our market, a regulated centralised trading screen would improve pre-trade transparency and therefore facilitate surveillance, end-to-end. It is also important that the regulatory environment takes into account progressive initiatives such as promotion of retail and foreign investor participation in both the government and corporate bond market. Their confidence in the market is required in order for them to be mobilized.

Therefore, the present fragmented market structure is not information efficient and it is not conducive to attract a heterogeneous investor base.

9.0 ACKNOWLEDGEMENTS

Contributions were obtained from bond market participants and stakeholders from the following institutions:

- a. Botswana Stock Exchange
- b. Capital Securities
- c. Ghana Stock Exchange
- d. Johannesburg Stock Exchange
- e. Lusaka Stock Exchange
- f. Nairobi Stock Exchange
- g. Renaissance Capital, Lusaka
- h. Stanbic Investments, Nairobi
- i. Standard Chartered Bank Botswana
- j. Thebe Securities, Johannesburg