

At the Heart of East Africa

The Nairobi Stock Exchange features a modern technology infrastructure, cost and tax incentives for investors and listing companies, and a friendly environment for foreign investors. With a regional character since inception, the NSE is committed to facilitating the creation of a regional exchange to serve the East, Central and Great Lakes region of Africa

Q: Could you provide some information about the background and the place within the economy of the Nairobi Stock Exchange?

A: Stock trading in Kenya dates back to the 1920s, but there was no formal market at the time. The Nairobi Stock Exchange was established in 1954 as a satellite of the London Stock Exchange. However, Africans and Asians were not permitted to trade securities until the independence in 1963, so the stock trade at the time was confined to the resident European community.

The first years of independence were marked by steady economic growth and improving confidence in the market, so the exchange handled a number of highly oversubscribed public issues. The oil crisis in 1972 hampered the growth as inflationary pressures depressed share prices. In 1975, a capital gains tax of 35% was introduced, leading to further losses. During the same period, the exchange also lost its regional character because Tanzania and Uganda started nationalizations and introduced restrictions. The East African Community dissolved in 1977.

In 1980, the Kenyan Government realized the need for reforms to achieve

economic development and a stable financial system. It's stated policy was aimed at enhancing the role of the private sector, streamlining the public sector, broadening the base of local ownership, and enhancing the development of the capital markets. In 1988, the government made the first privatization through the NSE as it sold 20% of the Kenya Commercial Bank.

During the 1990s, an extensive modernization included a move to new premises, a computerized delivery and settlement system, and a modern information centre. The restrictions on foreign ownership in local companies were relaxed, thus encouraging foreign investments. In 1996, the largest issue in the history of the NSE, the privatization of Kenya Airways, came to the market. In 1998, the government introduced further tax incentives and Kenya adopted the International Accounting Standards.

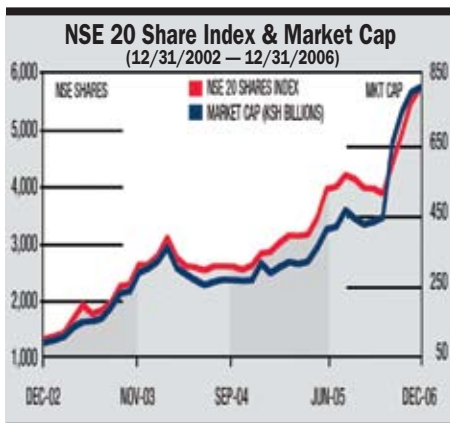
Since 2000, there has been a focus on facilitating the development of the collective investment schemes to encourage domestic savings. Collective investment schemes set up by employers on behalf of employees are now exempt from income tax. There is also an increasing focus on partnership



CHRIS MWEBESA is the Chief Executive of the Nairobi Stock Exchange Limited. During his two years at the helm of the NSE, Mwebesa has overseen the largest expansion in the history of the 52 year old bourse which culminated in a record breaking 2006. He was also responsible for the successful implementation of the Automated Trading System (ATS) of the NSE.

Mwebesa's experience transcends the banking industry, investment management services industry and the securities industry in the East Africa Region. Prior to his appointment as CEO of the NSE, Mwebesa was the Head of Business Development at AIG Global Investment Company (East Africa) Limited, and prior to AIG Global, he was the Chief Executive of Stanbic Investment Management Services (East Africa) Ltd, a subsidiary of Stanbic Bank Kenya Limited.

Mwebesa is widely consulted on issues affecting the Financial Services Sector by institutions such as the World Bank, International Finance Corporation, UNDP, Central Bank of Kenya, Monetary Policy Advisory Committee, Foreign Country Missions, Regional Securities Exchanges and Development Finance Banks to mention just a few.



and integration with other African exchanges and a move towards setting up a regional exchange. The goal of the East African Community, re-launched in 1999, is to have a fully integrated capital market with one regional stock exchange by the end of 2009.

Q: How large is the Nairobi Stock Exchange in terms of volume, brokers, and listed companies?

A: The number of stockbrokers has steadily increased through the years from six brokers at the inception to 19 brokers currently. There are 54 equities and 8 corporate bonds. 68 treasury bonds are listed on the fixed income segment.

Trading activity has been rising, especially after the implementation of the Automated Trading System in 2006. Last year the equity turnover increased by 160% to a record of Kshs. 94.95 billion. The volume of shares traded rose by 66% to 1,454.67 million, while the number of deals increased 239% to 598,301. The bond turnover grew even faster, up 257.42% for the year to Kshs. 48.58 billion

Q: What do you believe makes the NSE attractive? What is your strategy for attracting new investors?

A: We aim to position ourselves as an affordable cost-effective platform for local and regional companies to raise capital and enhance their public profiles. That is why keeping the expenses for brokers and investors low is a major strategy. The commission rates have been reduced considerably to between 2% and 1% on a sliding scale for equities and 0.0625% for all fixed interest securities.

There are also many tax incentives. The withholding tax on dividend income is 5% for local residents and 10% for non-residents. The capital gains tax was suspended in 1985, while the withholding tax on interest income

from listed corporate bonds and treasury bonds is 15%.

A newly listed company pays corporate tax at a lower rate of 20% for a period of 5 years, provided that these companies offer at least 40% of their shares to the Kenyan public. The companies that successfully apply for listing get a tax amnesty on their past omitted income, if they make full disclosure and oblige to pay all their future taxes. The IPO-related costs are tax deductible.

The law also encourages institutions to set up Special Purpose Vehicles (SPVs) for issuing asset backed securities, because the investment income of SPVs is exempt from income tax. Registered venture capital funds enjoy tax holidays of up to ten years on their income.

Q: Do you undertake any initiatives for the education of new investors?

A: We believe that an informed investor is a market's best friend, so we have programs for educating both investors and stock brokers. In collaboration with the Central Depository and Settlement Corporation, the NSE organized a series of workshops related to educating the market participants on the legal and regulatory issues, and market automation among others. We also organize seminars together with professional speakers from the stock broking community, investment banks, and investment advisors.

Last year, we facilitated more than 90 educational seminars, catering to secondary and tertiary institutions, professional bodies and institutional investors. We held four issuer workshops targeting the private sector and the state corporations in the tourism, IT, agro processing, and infrastructure sectors. These workshops aimed to clarify the listing process, the accessibility of the capital markets, and the

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incentives that the government has granted over the years.

One of the areas where we focus our educational efforts is the savings and credit co-operative societies (SACCOS) sector, with the idea to illustrate the investment and fundraising opportunities available through the NSE. Kenya's SACCOS is the most vibrant in Africa and accounts for approximately 8% of the GDP with over 3,000 registered SACCOS in Kenya. We also sponsor stands at industry events, especially agricultural and trade shows, to disseminate information on how to invest in listed securities, the rights of the investor and the role of the securities exchange, the Capital Markets Authority and the stock broker in the investment process.

We have also redesigned our website to provide up-to-date information. Key features of the site include market information from the trading floor that is updated immediately after the trading session, as well as updates of company announcements and news.

Q: The consolidation of exchanges is a global trend. What is the role and the future of the NSE in this environment?

A: We are deeply committed to the idea of creating a regional securities exchange for East Africa. We have been continually active in the regional developments through consultancy and partnerships. When Dar es Salaam Stock Exchange was established in 1996, the NSE was involved in a consulting capacity. The same also happened when the Uganda Securities Exchange was established in 1997. Rwanda is currently considering the establishment of a stock exchange as a satellite of the Nairobi Stock Exchange.

The harmonization of our rules and regulations and the close working relationships between the regulators

and securities exchanges of the three markets has culminated in the listing of Kenya Airways, East Africa Breweries and Jubilee Holdings on all the three securities exchanges. In 2006, we signed a memorandum of understanding with the Uganda Securities Exchange as a prelude towards moving to a merger. For 2007, we have budgeted Kshs. 500.0 million towards the establishment of a regional financial centre for market intermediaries engaged in stock broking, investment banking, trust and fund management and other financial services.

Q: What are the main challenges and benefits of a possible integration?

A: The integration provides many benefits. A regional capital market can facilitate economic development by providing deeper pools of capital and a broader range of listed securities. It has the potential to address the thinness and the illiquidity of the country capital markets. East African residents will have a single access point to all the securities listed in the region. Another benefit is that it will bring Rwanda and Burundi on line without them having to reinvent the wheel. For the listed companies, a regional exchange means access to a wider capital base and well as greater acceptance and recognition of the company brand.

Of course, the process requires the national authorities to harmonize stock trading systems and to permit the residents of each state to freely acquire and negotiate monetary instruments within the EAC. Another challenge is the difference in the key macro economic indicators of each country, such as the interest rates, inflation, and the currencies.

The multiplicity of regional trading blocks also acts as a hinderance. For example, while Kenya and Uganda are members of the Common Market of

Eastern and Southern Africa (COMESA) and the East African Community (EAC), while Tanzania is a member of the EAC and the Southern African Development Community (SADC).

Q: What types of listed companies dominate the NSE? Would you explain the main trends in new listings?

A: After a drought in new listings of almost 4 years the Exchange hosted 3 IPOs, one introduction to the official list and a secondary offering during the year. The IPOs of the Kenya Electricity Generating Company (through a Government privatization), Scangroup, and Eveready Batteries East Africa, the introduction of Equity Bank to the official list and the secondary offering from Mumias Sugar Company all served to create an unprecedented increase in public awareness of equity as an investment asset class. In 2007, Access Kenya Group and Kenya Reinsurance Corporation raised Kshs. 800 million and Kshs. 2.28 billion respectively.

Towards the end of 2007, the Government is expected to use the capital markets to offer a 25% stake in Safaricom. Safaricom is the leading mobile telephone operator in Kenya with a subscriber base of about 8 million and in 2006, was the most profitable company in East Africa. It was formed in 1997 as a subsidiary of Telkom Kenya and, later, Vodafone acquired a 40% stake and management responsibility.

Q: What has been the growth in the last three years in the Kenyan economy and the market?

A: The performance of most African capital markets has been stellar in the last three years. The demand for minerals and other commodities, political and economic reforms, and capital inflows were among the main drivers. The Kenyan economy is growing, with 2006 GDP growth in excess of 6%. The



Nairobi Stock Exchange

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Tel. No.	+254 20 2831000
Inception	1954

NSE INFORMATION

Members of the Exchange	20
Trading Sessions	10:00 - 13:00
Main Index	NSE 20-Share Index
Index Return - 2006	42.10%

INSTRUMENTS & SEGMENTS

Instruments Traded	Equities, Preference Shares
Secondary Market	Treasury Bonds, Corporate Bonds
Market Segments	Main Inv Market Alt Inv Market Fixed Inc Sec Market
Issues Listed	62
Equities	54
Corporate Bonds	8

MARKET INDICATORS

Market Cap - KES/US\$	KES745.54*/ US\$11.94*
Mkt Cap Change in 2006	33.86%
Equity Turnover - 2006	US\$1.52*
Turnover Change in 2006	159.98%
Equity Volume Shares - 06	1,454,667,044
Volume Change in 2006	66.40%

KEY EXECUTIVES

Chairman of NSE	Jimnah Mbaru
CEO of NSE	Chris Mwebesa
*billions	
Data through: 10/31/07	
Source: NSE	

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strongest economy sectors are agriculture, horticulture, manufacturing, telecommunications, construction, and tourism.

Q: Could you explain the change brought by the automated trading system that you recently implemented?

A: We started live trading on the Automated Trading System, or ATS, in September last year. The ATS is sourced from Millennium Information Technologies of Sri Lanka. The company is also the supplier of our Central Depository System (CDS) and of similar solutions to the Colombo Stock Exchange and the Stock Exchange of Mauritius.

The solution was customized to fit the specific requirements of the NSE. Besides trading equities, the ATS is also fully capable of trading corporate and treasury bonds. As a result of the change, trading hours and the daily volume increased. Another change is the removal of the block trades board and the introduction of the functionality for the trading rights in the same manner as equities.

There are many benefits of the new system for the market participants. Probably the most important one is the greater transparency in the placement of bids and offers. The system transmits information about the index and securities movements. Now there is more current information available to more stakeholders, which facilitates their decision making process and lowers the risk of participation in our market.

For us, the new system also means an opportunity to enhance the revenue stream with data vending to the shareholders. It also provides better control because our surveillance department can monitor the live trading session electronically, and any abnormal trad-

ing activity is investigated. With the switch to ATS, we became the first market in East and Central Africa to fully automate its clearing, settlement and trading systems.

Q: How do you see the future development of the exchange?

A: We plan to diversify our revenue stream through leveraging the ATS capabilities to roll out more information products. The real-time trading information data feed provides up-to-date market information including current market price, best bid and ask price, and transaction volumes. This information is available through the authorized vendors at a prescribed fee.

Cross-border operations should accelerate as the regional integration is now technologically possible. MIT, the vendor of our depository and trading system, has completed similar installations at the Dar-es-Salaam has been selected to implement an automated solution for the Uganda Securities Exchanges. The shared technological platform will increase the operational efficiencies and immensely aid the development of a regional market.

Another important development is our demutualization, which should be completed towards the end of 2008. It will transform the exchange from a members' association into a for-profit corporation, shortly followed by conversion into a public company. The segregation of ownership and trading rights of the members creates better corporate governance.

Going forward, we expect more IPOs because the market has strong absorptive capacity and the infrastructure is well enhanced and adequate. Overall, with the upcoming IPOs of Safaricom and other companies, the demutualization and the cross-border listings, the future of the NSE looks bright. **T**