REGIONAL CONFERENCE OF EMERGING SECURITIES MARKETS OF SOUTH AND SOUTH EAST ASIA

September 30 - October 3, 1992

Colombo, Sri Lanka.

A Conference Organized by

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REGIONAL CONFERENCE OF EMERGING SECURITIES MARKETS OF SOUTH AND SOUTH EAST ASIA

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INTRODUCTION

The Regional Conference of Emerging Securities Markets in South and South East Asia which was held in Colombo from September 30 to October 3, 1992 was an important step in discussing major issues and providing the basis for regional cooperation in the development of emerging markets. Fifty foreign participants from 15 countries attended with over one hundred local participants. Virtually all emerging markets in the region were represented. The role of Mr. L. Stanley Jayawardena, Chairman of the Securities and Exchange Commission of Sri Lanka, in helping conceive and organize this event was instrumental to its success.

The Conference Proceedings is a complete collection of all presentations and papers submitted by the participants and others unable to attend.

Section 1: Welcoming Address by the Prime Minister of Sri Lanka, Keynote Address and Conference Theme Papers

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This collection represents a significant amount of knowledge, thought and expertise not only from South and South East Asia but also from Africa, Latin America, the United Kingdom, Ireland and the United States. It is a valuable resource for future work. The readers of this proceedings will benefit from the balanced views expressed together with the lessons learned and successes shared.

The United States Agency for International Development (USAID) in Sri Lanka was the principal sponsor of this Conference and also facilitated the attendance of a number of participants through USAID Missions in the region. The Securities and Exchange Commission of Sri Lanka and the Colombo Stock Exchange, which among other activities hosted the receptions and financed the newspaper supplement on the Conference, are the other two sponsors.

the conference theme papers evoked lively discussion among the workshop groups and set the tone for much of the proceedings. A special not of appreciation is extended to Mr. Anthony Loehnis, Vice Chairman of S.G. Warburg, Dr. Mark Mobius, President of Templeton Emerging Markets Fund, Mr. Bill Gorman, Consultant on market automation and information systems, and Mr. Tom Healy, General Manager of the Irish Stock Exchange, for heeding the call to present papers at the conference.

Special appreciation is extended to Mr. Richard Brown, Director of USAID in Sri Lanka, and Mr. Talbot Penner. former Chief of USAID's Office of Private Sector Development, the Securities and Exchange Commission, the Colombo Stock Exchange, the Conference Committee and the Conference participants for making this event such a success. They made our job all that more pleasant. Particular note is made of the untiring efforts of Mr. Tilak Ranaviraja, Conference Coordinator, and Mr. Bradford A. Warner, Jr, ISTI's Chief of Party of the Capital Market Development Project in Sri Lanka, in making it all happen.

International Science and Technology Institute, Inc.
Washington, DC
October 1992

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CONFERENCE PROGRAM

Wednesday, September 30, 1992

12:00 Noon		Registration begins After registration participants are free to visit the city for sight-seeing, shopping on their own or join in the **City Tour.**
7:00- 9:30		**Welcome Dinner** Pre-dinner cocktails Welcome Speech
	Dr. Roland Silva **Director General** **Central Cultural Fund**	After Dinner Speech on the Cultural Heritage of Sri Lanka by Dr. Roland Silva.

Thursday, October 1, 1992

8:00		Tea/Coffee
		CEREMONIAL INAUGURATION OF CONFERENCE
8:50	**Hon. D.B. Wijetunge** **Prime Minister and** **Minister of Finance**	Arrival of the Chief Guest. Hon. D.B. Wijetunge Prime Minister and Minister of Finance
		Lighting of the traditional oil lamp
9:00	**Stanley Jayawardena** **Chairman** **Securities & Exchange** **Commission, Sri Lanka**	Welcome speech by Stanley Jayawardena
9:05	**Hon. D.B. Wijetunge** **Prime Minister and** **Minister of Finance**	Address by Chief Guest, Hon. D.B. Wijetunge
9:20	**Anthony Loehnis** **Vice Chairman** **S.G. Warburg & Co., Ltd.**	Keynote Address

CONFERENCE PROGRAM

9:55	**Ajit Jayaratne** **Chairman** **The Colombo Stock Exchange**	Vote of thanks
10:00		Tea/Coffee
		PLENARY SESSION I **Country Profiles -** **Recent Developments in Selected Share Markets**
10:30		**INDIA**
10:45		**THAILAND**
11:00		**NIGERIA**
		Conference theme presentations
11:15	**Stanley Jayawardena** **Chairman, SEC**	• The Regulator as a Capital Market development agency in partnership with the Securities Industry
11:45	**Tom Healy** **General Manager** **Irish Stock Exchange**	• The balance between oversight regulation by the Regulator and self regulation by the Stock Exchange
12:15- 2:00		**Lunch**
		WORKSHOPS
2:00 - 3:30		Workshop 1 Workshop 2 (Tea/Coffee will be served at the workshops)
		PLENARY SESSION II
3:30 - 4:10		Presentations by moderators of the workshops
4.10		Open Forum
		Conference theme presentation
4.30 - 5.00	**Mark Mobius** **Executive Director** **Templeton, Galbraith & Hansberger Ltd.**	• The Global Share Market - Foreign Investors and their emerging markets' expectations
7:00 - 9:30		**Conference Dinner** **After Dinner - Speaker Dr. Gamini Corea** **Cultural Performance**

CONFERENCE PROGRAM

Friday, October 2, 1992

		PLENARY SESSION III
9:00		Conference Chairman's review of day one
		Conference theme presentation
9:15	**Bill Gorman Consultant, Securities Trading, Settlement and Custody Systems**	• Automated Securities Market Systems- The path to the future?
		Country Profiles - Recent Developments in Selected Share Markets
9:45		**PAKISTAN**
10:00		**MALAYSIA**
10:15		**CHINA/MEXICO**
10:30 - 12:00		**WORKSHOPS** (Tea/Coffee will be served at the workshops) Workshop 1 Workshop 2
12:00 - 12:40		**PLENARY SESSION IV** Presentations by moderators of the workshops
12:40		Open Forum
1:00 - 2:30		**Lunch** **After Lunch - Speaker Richard Brown** Concluding remarks
2:30 - 4:00		Meeting of Chairmen of Securities and Exchange Commissions and Stock Exchanges to discuss possible action/strategies for the future

Saturday, October 3, 1992
Seeing a bit of Sri Lanka

Participants and accompanying guests have a choice between a visit to Kandy or relaxing in the sun at a beach resort in Bentota

Visit to Kandy:

The bus to Kandy will leave at 8:00 a.m. The tour includes visits to the Botanical Gardens, University of Sri Lanka, Peradeniya, and the Temple of the Tooth revered by Buddhists the world over. After lunch the group is expected to return to Colombo between 4:30 - 5:00 p.m.

WELCOMING ADDRESS

by

The Honorable D.B. Wijetunge
Prime Minister and Minister of Finance
Sri Lanka

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I consider it a singular honour and a privilege to be called upon by the organizers of the Regional Conference of Emerging Securities Markets of South and South East Asia to be Chief Guest at its ceremonial inauguration, and at the outset may I offer my sincere thanks to the organizers for their kind gesture.

Let me begin my short address observing that the theme of the Conference is very relevant to Sri Lanka as well as in other participating countries. In this continuously shrinking world, especially in the context of the global economy of which all of us are partners — whether willing or unwilling, no country can live in economic isolation. Countries are so interdependent economically that major changes or some times even minor ones in the economic structure of a country are bound to have immediate and sometimes far-reaching repercussions on countries in the region, and perhaps even on countries outside the region where at least their tremors would be felt.

In such a context hardly any country can be indifferent to questions pertaining to securities markets. This is more so because securities markets can play a pivotal role in the development process of a country. As regards Sri Lanka, her securities market achieved a very remarkable growth both in price appreciation and in number of transactions during the proceeding two year period, 1990 - 1991. Many other participant countries may have experienced similar or even better or vice versa growth rates.

Additionally, the recent developments in the socialist world have further demonstrated the fact that economic isolation is a distress attitude and that it is bound to fail. Therefore, I believe it is inevitable that countries will opt for an open economy and open up their markets to foreign investors. In this context a conference of this nature is very timely. Such a Conference will help to discuss and resolve the various problems faced by emerging securities markets of participating countries.

I am also happy to observe that this Conference contains a fine blend of delegates and participants representing a wide range of countries whose emerging securities markets are at different levels of development. This is bound to make the Conference mutually fruitful for all participating countries. This Conference will provide a very enlightened forum to express and exchange views on a variety of problems connected with securities markets and share each others experiences. The experts gathered at this Conference will certainly contribute to resolving problems and evolving effective goal oriented methods and strategies.

The Conference brochure points out the need for dynamic and time-targeted strategies. It notes that unlike the developed markets which took many years to evolve and grow, we have to make a quantum leap to reach our goals within just a few years. This sounds challenging but I am positive that this is the right approach to solve problems and evolve solutions, especially for counties with emerging securities markets.

I would like now to say a few words on the historical development of the stock market in Sri Lanka. Its origin dates to the latter part of the last century, in the late 1870s, due to economic necessity. This was the time when coffee — which till then was the main export commodity — was being replaced by tea. Long-term finance was needed to affect this transition, and in order to raise the required funds Public Limited Liability Companies were floated in both Colombo and London. Subsequently secondary market transactions resulted in the Colombo Share Market being organized in 1986 under the administration of the Colombo Share Brokers Association.

At the turn of the century, with the coming of rubber as an export commodity, once again long-term finance was required, and for this, too, shares were issued to the public. The development of the tea and rubber plantations led to the organization of a number of Commercial Companies which provided back-up services to this sector. A number of these Commercial Companies also raised their initial capital through share issues to the public.

Thus, prior to independence in 1948, the share market consisted of Plantation Companies, a handful of commercial companies and some foreign companies headquartered in London, Bombay and Singapore. However, the introduction of exchange control in June of 1948, transformed the Colombo market into a market for domestic companies only.

From independence to 1977, the Colombo Share Market was adversely impacted by economic policies which unfortunately retarded its development by thwarting private enterprise and eroding business confidence. Stringent import controls starved business and industry of its needs and stifled growth. The insurance industry was nationalized beginning in 1962. The Finance Act of 1963 imposed a 100 percent tax on property, including shares, purchased by non-nationalized companies. The Business Acquisition Act was introduced in 1971 with its ever-present threat of Government being able to take over any business undertaking. Finally, Plantations were nationalized in stages through the Land Reform Acts of 1972 and 1975. As a result of the nationalization of the plantations, 105 companies were eliminated at once from the share list representing a substantial portion of the market capitalization of the Colombo Share Market. As of the end of 1976, the share list had been reduced to 76 companies from 216 in 1965.

However, the advent of the United National Party government in 1977 espousing liberal economic policies and offering a hospitable climate for foreign investment contributed to the rapid revival of enterprise, business confidence and investment. By the end of 1983, the share list had expanded to 176 companies, despite the elimination of the plantation companies owning domestic properties. Several measures taken by the government since 1977 are particularly worthy of note as they helped directly to stimulate the growth of the share market. The first was the decision to pay compensation to the shareholders of plantation companies which had been nationalized. Next came the introduction of an income tax differential of 10 percent in favour of listed companies effective April 1, 1980. Third, the generous package of tax incentives and exemptions for new companies that went public. Fourth, the repeal of the Business Acquisitions Act in 1988. Fifth the announcement on June 5, 1990 that the 100 percent property transfer tax on listed shares purchased by foreigners from nationals (to the extent of up to 40 percent foreign ownership) was abolished, thus opening the market. Finally, the Peoplisation Program which commenced in 1989 and which is ongoing represents the most important source of supply of securities. The Government also put in place a package of tax exemptions per holders of listed securities and encouraged the setting-up of Unit Trusts in the amendments to the SEC Act in 1992.

In keeping with the new economic policies, the share market was reorganized in 1985 under the name. The Colombo Securities Exchange, which subsequently became The Colombo Stock Exchange. In 1987 the Securities Council Act was passed and this created a regulatory body responsible for ensuring orderly markets and safeguarding investors' interests in securities transactions of both debt and equity. This body was also charged with the responsibility of advising the Government on the development of the capital market.

Though the securities market in Sri Lanka has shown a remarkable growth in recent times, there is much more to be achieved. For example, the percentage of current market capitalization is still relatively low compared with the gross national product. Also, the number of listed companies is below expectations when compared with the total number of companies in Sri Lanka.

Though the saving habit is well established, the majority of people are not yet knowledgeable about the possibility and prospects of investing in shares. Therefore, they prefer to invest in savings deposits. However, recent market surveys reveal that there is an increased awareness among the public regarding what the share market is and how it functions. This is attributable, at least in part, to the extensive public awareness campaign recently completed by the Securities and Exchange Commission and the Colombo Stock Exchange. This campaign was part of the Capital Markets Development Project funded by USAID, and it would like to commend those organizations for their initiative.

It is clear that given the proper stimulus and infrastructure, the capital market can develop and make a major contribution to economic growth and employment opportunities. As this economy becomes more private sector-oriented, and with transfers of assets from the public sector to the private sector under the Peoplisation Program, the ability of the capital market to channel savings into investment will become of overriding importance to the economy's future. I can assure you that the government is keen to develop an environment conducive to achieving this goal and will always be willing to provide the necessary support.

Let me congratulate and thank the Organizers for holding this Conference and also for giving me this opportunity to participate in this ceremonial inauguration and to address a few words. I am confident that the Conference will provide a useful and stimulating experience and facilitate fruitful discussions.

SECTION 1

PAPERS PRESENTED BY SPEAKERS

THE ROLE AND DEVELOPMENT OF SECURITIES MARKETS IN DEVELOPING ECONOMIES

by

Anthony D. Loehnis
Vice-Chairman, S.G. Warburg & Co. Ltd.

INTRODUCTION

It is a great honor to have been invited to address this important and timely conference of the emerging securities markets of South and South East Asia. The very phrase "emerging securities markets" encapsulates a truth about the evolution of the economic development process which is wholly welcome. Twenty years ago or more the countries subject to that process tended to be lumped together under the title, *The Third World*. In the course of the 1970s and up to the early 1980's that title had mutated to less developed countries. You will recall that the international debt crisis which burst upon the world just over ten years ago was known as "the LDC debt crisis" over the past few years, however, there has been a tendency to talk less of LDC's and more of emerging economies or emerging markets. This last mutation is hardly coincidental: the debt crisis has been eased, if not overcome, in those countries whose economic policies have recognized the dynamic role which markets can play in economic development and which have encouraged their growth.

There are currently about 180 closed-end emerging market funds. No less than 10 Latin American funds were launched in 1991. The IFCs first Emerging Stock Markets Fact Book appeared as recently as 1987. 1987 was, of course, the year of Black Monday, when the bubbles in most of the developed world's stock markets burst, and since when global investors have had every incentive to widen their search for value and the prospect of capital gains. They certainly found it in emerging markets in 1991, where nine of the top ten performing stock markets in the world were emerging markets. It must be admitted that the four worst performing markets were emerging ones also! Since 1982 the total market capitalization of emerging markets was increased from 2.5 percent of that of developed markets to 6 percent by the end of last year. In an age of indexed fund management such a percentage begins to look significant.

Asian countries have been very much the focus of all this activity, notwithstanding last year's re-emergence of the much older markets of Latin America. At the end of 1991 the market capitalization of the East and South Asian markets included in the IFCs Emerging Markets Composite Index totalled nearly $390 billion, while those of Latin America reached only just over $200 billion. Including Hong Kong and Singapore, the Asian total would be increased by a further $170 billion, although their stock markets are counted as developed. These figures reflect the consistent economic dynamism of the economies of East Asia. It is in East Asia, too, that the most headline-catching and spectacular stock market crashes have occurred, such as those in Taipei and Indonesia in 1990, not to mention the market fever that has gripped the fledgling securities markets in the People's Republic of China. There are certainly lessons to be learned from a situation when members of the public can be crushed to death in crowds seeking not to buy stock, but to buy application forms for admission to a ballot in which those successful will be able to buy stock.

The development of stock markets in Asia has not only been driven by economic dynamism, it has also received a powerful impetus from the important shift of intellectual opinion in the 1980's in favor of reducing the share of the public sector and its accompanying bureaucracy in favor of the private sector and the development of markets. This has had an obvious manifestation in a number of privatisation programmes which have themselves both been stimulated by and stimulated the globalization of marketplaces. In this, of course, innovation in information and communications technology has played a key role.

These, then, are some of the reasons why I describe this conference as timely. There are delegates or observer participants here from countries all along the spectrum of development, from those where market evolution has hardly begun, to those trying to take off, to those who have taken off, to those whose market development is fully mature. This provides scope for a useful exchange of experiences and I am glad that the programme contains two sessions of country profiles when we will hear about recent developments in six very different countries.

The Conference themes also seem to me wholly appropriate. How can Government cooperate with the securities industry in the process of capital market development? What is the appropriate balance in the supervision of markets between the official regulator and self-regulation by practitioners actually operating in the markets? What are the consequences for the structure and development of domestic capital markets of the globalization of investment and the demands of global investors, and what contribution can this globalization make to the development of a domestic capital market? Finally, how can the advances of information and communications technology in recent years be applied to the structure and operations of emerging markets and how can you learn from the costly mistakes of mature markets as they seek to adapt their own long-established but out-dated systems? Without seeking to preempt what our expert speakers will say on those themes, I should like to proffer a few thoughts on them.

Before that, however, I should like to try to put stock market development and evolution into a slightly wider context. I was struck by what I took to be a *cri de coeur* in the letter from the Chairmen of the Sri Lankan SEC and Colombo Stock Exchange in the brochure describing the conference:

> "Though developed markets took many years to evolve and grow, we certainly cannot afford to take the same amount of time. We need a quantum leap to reach our goals within just a few years".

In this context, the conference themes I have referred to above are all posited on the assumption that securities markets are, and should be, an intrinsic part of the development process. But is this assumption, true, either in economic theory or in historical fact? Does economic growth depend on the development of stock markets? Capital and finance is certainly important, but must it or should it be equity finance? In the development of a sophisticated financial system what is the appropriate sequencing for the development of a stock market?

I shall argue — and I hope that my arguments may help rather than hinder the workshop discussions — that there is no generalized answer to the questions I have just posed. Much depends on the cultural and historical background of the developing country involved, whether and when emphasis should be placed on developing a stock market. I shall also argue that, contrary to popular mythology, equity finance plays a relatively insignificant role in the financing of the corporate sectors of developed countries. Furthermore, economic theory is ambivalent or negative as regards the significance of stock markets in the growth or development process.

This is not to suggest that one should be indifferent as to whether or not to develop a capital market. Clearly, security markets play an important role in the improvement of domestic resource mobilization and, under appropriate circumstances, in the efficient allocation of capital resources. The timely evolution of capital markets should go hand in hand with the development of institutional investors, such as life insurance companies or pension funds, not to mention mutual funds which provide a balanced spread of investment risk. A stock market is also very important for the process of privatisation, which itself is a significant means for increasing the supply of securities which in turn is an essential part of the growth process for stock markets. Open financial markets can also act as a macro-economic discipline on governments, through the role which capital flows have on the exchange rate and the current account balance. But stock markets are not a necessary condition for any of those functions.

The point I seek to make is that expectations should not be pitched too high about what establishing and nurturing a stock market will achieve. Nor can markets be expected to prosper in, or contribute to, the development process unless their evolution takes place in a balanced way, with encouragement to both the supply and demand for securities at the same time. Furthermore if stock markets are to encourage savings and to allocate them effectively among competing claims for capital resources, they must be seen to be efficiently organized and well-regulated.

THEORY AND HISTORY

This is certainly not the place, nor am I well qualified, to burden you with a detailed theoretical exegesis on finance or development economics. It does seem worthwhile, however, to mention some of the findings of recent research conducted under the auspices of an economic think-tank of which I have the honor to be Chairman, the Centre for Economic Policy Research (CEPR). One of the main focuses of CEPR's research is the economics of restructuring the economies of Eastern Europe and the former Soviet Union, and within our applied macroeconomics programme, Professor Colin Mayer has made some international comparisons of how industry is financed. These have produced interesting conclusions which throw light on the questions of how much capital matters for growth and development and whether countries with capital markets have grown faster than those without. Although these conclusions run somewhat counter to conventional wisdom, I believe they have relevance as background to this conference's deliberations, notwithstanding that they derive from consideration of the developing countries of Eastern Europe and, in the case of industrial finance, from the experience of industrialized rather than developing countries.

<u>How much does capital matter?</u>

CEPR held a conference on "Finance and Development in Europe" at the end of last year, which examined the role of finance in development with particular reference to issues such as the ability of financial intermediaries to enhance an economy's production opportunities, the contribution of capital markets to the real economy and the effects of gaining access to international capital markets on developing countries. The papers presented to the conference are in process of being published as a conference volume and I would simply quote from the overview chapter by one of the conference's organizers, Professor Giovannini of Columbia University:

> "Overall, the papers in this volume offer a rather skeptical assessment of the role of financial markets in economic development. In particular the papers have indicated that, first, simple growth models and models of the role of financial intermediation in the economy do not work very well, and even if they did, capital cannot play a central role in the process of growth. Second, informational problems are pervasive, and their presence is what prevents financial markets to fully perform the risk-sharing and income-smoothing functions which makes them desirable in developing countries or regions. Third, government policies aimed at financial market liberalization have had limited success even in those countries whose economic performance has been much superior to the average."

On this last point, the conference heard an interesting case study examining the situations of two of the most successful developing economies, South Korea and Taiwan, by a Korean economist, Y. C. Park. He pointed out that until the last decade or so, Korea had a very repressed financial system, bank-oriented, highly regulated, with control led interest rates and with resources directed toward successful export industries. Despite this, Korea has had an impressive growth record. Even when deregulation of the financial sector began to be encouraged in the 1980's, Park concluded that there was no evidence that this had increased the savings rate, or improved allocative efficiency or led to an above average productivity of investment. He attached importance to the predictability of the availability of finance and suggested that the financial sector grows as a result of output growth rather than vice versa.

The experiences of Korea and Taiwan are hardly typical. Both are poorly endowed with natural resources and were therefore naturally pushed toward developing their manufacturing bases. Both share a common Confucian culture with an emphasis on education, frugality, hard work and discipline. And both share a common Japanese colonial heritage, which affected their basic financial structure. The lessons to learn from the Korean and Taiwanese experience are, I suggest, that financial structures are to a considerable extent derived from cultural and historical experience, and that while financial markets are obviously important, there are many other factors in the development process which are equally as important or more so — in particular human capital resources.

DO CAPITAL MARKETS LEAD TO FASTER GROWTH?

The Korean and Taiwanese cases are relevant to the second question, whether countries with capital markets have grown or developed faster than those without. Here it is interesting to look at the findings of Professor Mayer's research into the sources of finance of non-financial enterprises in eight industrialized countries (U.S., U.K., Japan, Germany, France, Canada, Finland and Italy) over the period 1970-1985, which may be summarized as follows:

- Retention rather than external finance are the dominant source in all cases;
- Within the group of 8 countries there are wide variations in self-financing ratios: in the United States and the United Kingdom these ratios are around 70 percent; while Italy, Japan, France and Finland raised more than 50 percent externally;
- In none of the countries was a substantial amount of finance raised from securities markets, whether fixed interest or equities;
- Banks were the dominant source of external finance in all countries, particularly so in Japan, France and Italy. The German percentage was about the same as that of the U.K and the U.S. — slightly more than 20 percent;
- In the U.K. and the U.S. the significance of securities markets has declined overtime;
- In the U.K. at least, small and medium-sized firms were more reliant on external finance than large ones, and (unsurprisingly) used securities markets less.

In drawing conclusions from his empirical observations, Mayer concedes that equity markets perform an important function in promoting allocative efficiency through the provision of prices, and can also promote productive efficiency in facilitating the takeover process. He rejects as an explanation for the preponderance of bank finance the suggestion that banks are the financial intermediaries best able to overcome the deficiencies of financial markets arising from asymmetries of information, pointing out that other intermediaries can and do this quite efficiently. And indeed, recent experience of loan losses and provisioning in the banking sectors of the world make information theory explanations implausible.

Mayer concludes that it is the extent to which and the form in which institutions influence the activities of firms that is likely to determine the nature and extent of external financing. He emphasizes the managerial functions of creditors, and the fact that it is banks, rather than diffused bondholders or shareholders, which have the ability to intervene in a company's affairs and if necessary take control. In developing countries where managerial resources may be scarce they are likely to be deployed at the higher levels of a country's economic activities, i.e., the banking sector has a role in spreading managerial skills downward to the firms it finances. Mayer suggests, therefore, that in the early stages of the growth of firms and economies an efficient banking system is an essential requirement for expansion and that securities markets are unlikely to be effective substitutes. Our own experience in the Overseas Advisory Division of Warburgs suggests that the largest source of equity finance in developing countries comes from major joint venture projects, and thus does not pass through a capital market.

I would draw from all this research four main lessons:

- securities markets are not in general a significant source of industrial finance;
- securities markets are of much less significance than the banking sector in the early stages of the development process;
- the nature and role of securities markets in developing countries depends to a considerable extent on the cultural and historical development of the country concerned;
- human capital resources are of much greater importance than financial capital resources in the development process, because only they can ensure that available financial resources are efficiently and productively utilized.

Let no one think that is a negative list. Look at it rather as a list which might help place the development of a securities market in the order of priorities for the government of a developing country.

THE ROLE OF SECURITIES MARKETS IN THE EVOLUTION OF THE FINANCIAL SECTOR

I turn now to the positive role that securities markets have to play in the evolution of the financial sector. Since the financial sector intermediates between those who save and those who use those savings in investment, it is useful to analyze the role of the markets from the point of view of those supplying funds and those using them.

The level of savings in an economy is a function of the wealth the country is able to create and the propensity of its people to save or consume. Once an economy has evolved beyond the subsistence state, the main determinant of that propensity may well be cultural or psychological. But the savings habit can be encouraged by the availability of a variety of savings media, offering differing levels of risk and reward, different maturities and different characteristics such as capital growth or income.

Although equity investment has been shown, at least in industrialized countries, to be an effective hedge against inflation — and inflation is a disease to which developing countries are even more prone than developed ones — in developing countries where the large majority of savers are individuals, the greater risk of equity investment over bank deposits or bonds does produce problems of volatility in prices. The aim of securities markets must be to create stability through maturity and depth. Maturity requires investors to take a long-term view of equity growth and not to invest purely for short-term speculative gain.

One of the best ways to develop the maturity that comes from long-term investment is to encourage the growth of institutional savings through institutions such as life insurance companies, provident funds, pension funds, mutual funds and so on. Such institutions have an interest in spreading risk and therefore have a valid interest in the development of a variety of investment instruments. They are also by definition takers of a long-term view, and therefore able to tolerate short-term fluctuations in the value of the market as a whole or of particular stocks more easily than individual investors. It is encouraging, therefore, for the development of securities markets that an increasing number of developing countries are considering mandatory contributory pension schemes in both the public and private sectors.

To a certain extent foreign investors (which are likely to be predominantly institutional) perform the same function, although one must bear in mind that when the going gets tough domestically, it is very often foreign investment that is cut back first. Global investors are extremely return-conscious, so that they will not hesitate to withdraw from a market whose prospects change or which demonstrates immaturity through high volatility or the repetition of speculative bubbles. Nevertheless, foreign investors will have the research capability to determine what promise to be "blue-chip" companies and in their necessarily selective entry into a newly emerging market will tend to validate that judgement, encouraging both the maturity and the depth of the market in the process.

So institutional investors, both domestic and foreign, have the capacity to establish virtuous circles for markets. They look for liquidity and depth and they look for long-term investment. By their entry into equity markets they begin to provide the depth and liquidity which encourages others to utilize the market and thus enhance the liquidity, and by taking a long-term view of investment, they enhance stability.

But the supply of savings from institutions requires a balancing supply of investment instruments from the would-be users of those savings. Otherwise, price increases will reflect the weight of speculative money rather than improvement in the fundamental health and growth prospects of companies. The availability of companies suitable to be listed on a public stock exchange and the timing at which it seems advantageous to the original proprietors of companies to sell equity to a wider public obviously depend on a number of factors which will be unique to each country. In the early stages of development, size is important, since it is the prerequisite for the essential liquidity that characterizes an efficient stock market.

But perhaps the more fundamental question is why should the original proprietors of companies in developing economies, whether they be governments or in the private sector, be willing to cede equity to other investors at all? There are perhaps two main reasons: the first is to widen the range of financing possibilities open to a company and thus reduce the overall cost of finance; the second is to establish a value for corporate assets and to open the possibility for original proprietors to realize some of that value.

Although, as I indicated earlier, countries may vary in the degree of their equity-orientation, and thus in their perceptions of an appropriate debt-equity ratio, equity is the ultimate long-term capital. It is permanent, it provides a cushion against bad times since it has no contractual return. It also represents the commitment of the owners to the enterprise, without which it is hard to attract other sources of finance. Within whatever convention for debt/equity ratio pertains in a country, the larger a company's equity the greater the control of the company the owners will retain and the easier and cheaper it will be to raise finance. The gearing effect of loan finance is both the key to the maximization of return on equity and the most frequent cause of corporate failure.

The desire for enhanced and possibly cheaper financing possibilities may well be an incentive to a proprietor whose ambitions for his company's growth cannot be satisfied from his own pocket or who simply wishes to maximize shareholder value. Submitting oneself to the discipline of a public listing on a reputable stock exchange and the subsequent need to take into account the interests of outside shareholders in the management and performance of a company is, nevertheless, a price which many may find irksome. But where the original proprietor wishes to realize his investment, being listed on a stock market can facilitate change of control of companies, particularly through the takeover route.

One of the major problems of corporate development is the transfer of managerial control from a dominant original proprietor to a more advanced management structure which may at the extreme be wholly divorced from ownership. Even when this has been accomplished, a new set of problems arises. How can management be made accountable to the proprietors — i.e., the shareholders — when there are no dominant or significant shareholdings, or when the stock are in the hands of institutional investors? For such investors tend to be reluctant to exercise the notional proprietorial control over management because of their perceived fiduciary duty to their beneficiaries, which may dictate sale of a shareholding when corporate performance is going wrong rather than taking action such as replacing management to improve matters. Problems of corporate governance are a complex subject. Suffice it to say here merely that one method whereby management's interests and those of owners may be made more convergent is to encourage management to become owners themselves through share incentive schemes, options or even management buy-outs. Clearly this incentivisation of management is much easier in a public than a private company. This apart, the continual judgement of corporate prospects and performance exercised by markets, through the research function in particular, can in itself be a useful spur to improved managerial performance.

Where the original proprietor is a Government, as is likely to be the case in many developing countries, an analogous set of pressures is at work. Obviously, the Government enjoys and exercises power and patronage through a large public sector controlling important areas of industrial or financial activity. But the costs are increasingly seen to be budgetary problems and inefficiency.

That is why privatisation has appeared almost worldwide as an idea whose time has come. It helps to remove from the national budget and transfer to the private sector the burden of financing the companies and industries in question. A nation's savings may be easier to tap through attractive investment opportunities than through taxation that can often easily be avoided. The repatriation of flight capital to a number of Latin American countries in the past two years or so points a lesson here.

Privatisation can also be particularly beneficial to the development of securities markets. Many of the largest enterprises in developing countries, understandably if not inevitably, originate in the public sector — public utilities, major industrial concerns, banks and so on. The problem of the availability of sufficient equity to feed a growing stock market and to satisfy the investment needs of institutional investors is greatly reduced for countries with comprehensive privatisation programmes. Size, of course is helpful from the point of view of liquidity, but it can also be a problem. When a newly privatized firm dominates the market capitalization of a whole market, or indeed when investment performance — on which the spread of the shareholding habit is importantly dependent — may be held back by a market's fears of the overhang of further tranches of the state's retained shareholding, headaches can be produced for securities market authorities and regulators. But this is a far healthier problem with which to deal than lack of liquidity through an inadequate supply of securities.

You may feel that the tone of these remarks is more positive toward the development of securities markets than the conclusions I drew from a consideration of theoretical and empirical studies earlier. The explanation lies, I think in the distinction between primary and secondary markets. Secondary markets redistribute the ownership of assets, they do not provide the finance for listed companies. That only happens when a company increases its equity by making a new issue. "Going public" or "privatizing" normally involves the sale of existing shares. The price at which such shares are sold may well lead to new and increased investment in so far as it realizes value which was unrecognized previously and the selling proprietors put the proceeds of sale to productive use enhancing consumer demand or making new investment. Or new investors remove money from under the proverbial mattress and invest it in the market. But the majority of those who buy shares in privatized companies will be shifting their portfolios — to buy the shares they reduce bank deposits, sell government bonds, sell other shares, borrow or whatever. So unless the selling proprietors link the sale transaction to a new issue of shares, the finance available directly to the company remains the same.

Similarly, a government may use the proceeds of privatisation to reduce the budget deficit, or to reduce taxation, or to repay borrowing, any of which is likely to have beneficial results. And the process of privatisation should lead to the application of purely commercial considerations to the management of the company — increasing efficiency, reducing waste of human or financial resources and releasing hitherto suppressed entrepreneurial talent. But those are indirect additions to the public good rather than new injections of finance to the privatized company. So the limitations of the stock market as a direct provider of new funds must be set against the numerous ways in which it enhances and improves the process of saving, the development of the financial sector and thus economic growth more generally. Having said this, it is obviously also true that a healthy secondary market is a precondition for the optimum utilization of the primary market.

THE CONFERENCE THEMES

Finally, let me redeem my promise to say something about the four conference themes, which are relevant whatever the state of development of an economy or its financial sector.

(a) Partners in Capital Market Development

The extent to which capital market development should be stimulated by the regulator or the authorities more generally, or can safely be left to the securities industry itself is an interesting question to which no single answer can be given. It depends on the cultural background of the country in question and the state of development of its financial sector. I personally believe that left to themselves markets are spontaneous organisms which develop their own direction in response to commercial demands and opportunities. The authorities have a duty to consider the wider public interest and possible threats to financial stability, but otherwise their response to innovations or developments formed by the market should be "why not?" rather than "why?"

Much depends, of course, on how spontaneously innovative or creative the market itself is. Even in a mature economy where the authorities espouse the philosophy I have just described, such as the UK, it may be necessary from time to time for the authorities to give markets a nudge or even a shove. Bank of England encouragement to the development of ECU-denominated money and capital markets in London would be an example of the former, the role of the authorities more generally in encouraging the market changes known as "Big Bang" in 1986 of the latter.

Other countries have more authoritarian traditions — or perhaps just less mature markets. I have in mind countries like Japan, Korea, Taiwan or Singapore, where virtually all capital market developments originate with the regulatory authorities rather than the markets themselves. France would be a non-Asian example.

In developing countries, the relative lack of sophistication of the markets makes it likely that the authorities will need to take a firmer hand in capital market development. Mistakes which lead to loss of the fragile confidence of new investors in immature markets are too costly to make. There is of course a risk of the blind leading the blind if capital market development is all done from the top down, so the idea of a partnership between the regulatory authorities and the securities industry in the development process is very appealing. Obvious areas where the regulatory authorities will have a major role is in encouraging the emergence of institutional investors, as well as ensuring that the market is genuinely competitive and does not become a cozy cartel. In this connection, it is the regulatory authorities who must take a public interest view on the appropriate part to be played by foreign firms and investors, which may well be beneficial for capital market development in so far as it helps with convergence with international practice, but carries also the risk of overwhelming the burgeoning, but in some cases relatively weak, domestic industry.

At the same time, however, the interests of regulator and market may well diverge, and it is desirable that regulators should be willing at an appropriate stage to draw back and permit organic market development to flourish, subject to the requirements of regulatory oversight to which I now turn.

(b) Government Regulation and Self Regulation

It is a paradox to the market deregulation that captured the imagination so widely in the 1980s that it required at the same time re-regulation: as market structures and market participation became de-regulated it became necessary to construct new systems for supervision and investor protection. In a number of countries, including the United Kingdom, that process involved an intense, and often still unresolved, debate on the relative merits of statutory regulation as against self-regulation, or as I would prefer to phrase it, "practitioner-based" regulation.

The argument in favor of self-regulation was that statutory regulation involved rigid rules administered by civil servants lacking knowledge of the market place, making the operations of the market inflexible, expensive and hard to adapt. The SEC in the United States was, somewhat unfairly, held up as the exemplar of what was to be avoided. But, these alleged deficiencies of the U.S., or any other statute-based system, can to a large extent be overcome if the regulatory agency is well-staffed with practitioners, some no doubt on secondment, and if the legislation delegates to the market authorities those aspects of market operation and practice that properly fall within their competence. There is pretty general agreement, I would judge, that those would include the regulation of market transactions, the conduct of market participants and possibly their licensing, subject to transparent criteria of the requirements to qualify for a license, as well as conflict resolution and disciplinary procedures. I am less certain that responsibility for compensation funds to protect customers against losses arising from the failure of a regulated institution should fall on the industry itself, rather than on the taxpayer, but the issues are complicated.

In the design of new securities markets in developing countries, there is a tendency perhaps to concentrate on trading and settlement procedures, and the requirements for listing and new issues, but to tack regulation on at the end, often mirroring the regulatory institutions and practices of some other country, which may be wholly inappropriate. The regulatory system should never be an after thought in the construction of a capital market, because effective supervision and sensible cost-conscious regulation are essential ingredients for the establishment and maintenance of investor confidence in a market. It is also important to ensure that the degree of regulation is appropriate to the type of investor: the type of investor protection appropriate for retail investors may well be very different from that suited to professionals. The search for the right balance of responsibility between regulator and the market authorities themselves is an important and continuing one. The bias should be toward delegating as much toward the market authorities as is reasonably possible. How much is 'reasonable' will of course change as the markets themselves mature.

(c) The Role of Foreign Investors

Efficient regulation is also a requirement for participation by foreign investors. I have already indicated my belief that foreign investment can be very helpful to market development in the same way that imports provide valuable competitive stimulation to a developing country's manufacturing industry. Foreign demand brings depth and liquidity to a market and will facilitate the convergence of emerging market practices to international norms, as will the participation within the securities market itself of foreign firms. Furthermore, the growth of knowledge of an emerging market — its economic development, its political stability and the investment merits and prospects of its companies — will contribute toward the ability of those companies to gain access to international capital markets and thus provide a further diversification of funding sources.

In the first instance foreign investment is likely to be in the form of a professionally managed regional or country fund, only later developing into investment in individual stocks, as a securities market matures. The criteria for foreign interest are fairly obvious: good economic growth prospects, political stability, availability of enough stock and adequate liquidity, satisfactory settlement procedures, reliability of accounting procedures and availability of reliable financial information, good local research and a well-regulated market which can detect and prevent undesirable practices such as share-ramping. A government committed to a radical privatisation programme is of particular interest, because of the promise this holds for deepening the market, as well as being a symbol of political support for the private sector.

(d) Automated Systems

My final word is about Automated Securities Market Systems, on which subject I am very glad we will hear from an expert tomorrow. The appropriate design of trading and settlement systems is one of the foremost concerns of all involved in securities markets. Indeed, emerging markets are in a good position to learn from the mistakes of more mature markets, where it is proving difficult and expensive to graft new systems onto old ones. Emerging systems can adopt systems which are *ab initio* compatible with the requirements of internationalised investment. One emerging market which is doing just that is the Jakarta Securities Exchange, after the adverse developments of 1989-1990 when the impact of deregulation and foreign demand overwhelmed the capacity of both systems and participants, leading to illiquidity, back-office settlement problems and broker defaults. One of the problems seems to be that the organisation and control of the market was in the hands of a Government agency rather than the broker-dealer practitioners themselves. Now, under new legislation, it is planned to establish a new system of private securities exchanges in Indonesia, with Jakarta no doubt dominant, with new systems of trading and settlement which are compatible with international requirements and will permit the evolution of a single national marketplace.

The characteristics of the system which will be introduced include:

- no arbitrary restrictions on the numbers of participants as broker-dealers, other than tests of competence — the market should determine the appropriate numbers;
- capital requirements and operational costs should be such as to offer a reasonable return on investors' investment;
- a fast and efficient automated trading system;
- a system for guaranteeing same day settlement through a central depository, but with special settlement arrangements for foreigners to take account of time differences — those aspects are of particular importance if foreign investment is to be encouraged;
- book entry settlement of dematerialised securities.

The trading system itself provides for an automated quotation system, computerized order matching and the encouragement of an adequate number of market brokers and traders. Finally, the component pieces of software needed for the proposed exchange are all tried and tested and available at relatively short notice.

Now the requirements of each exchange will certainly be unique. The characteristics of the Jakarta proposal derive in part from the fact that about 50 percent of volume on the Jakarta exchange is international. Nevertheless, many of these characteristics will have relevance for most exchanges, taking into account the state of evolution already achieved, the size of the economy and the extent of or prospects for international interest.

CONCLUSION

My odyssey is complete, and your patience may well be exhausted. I hope I have said enough to stimulate discussion rather than to cause mental indigestion. I hope also that in delivering a message that you should not pitch your expectations too high as to what developing a securities market can achieve, and emphasizing that each of you must find your own uniquely appropriate evolutionary path toward the development of your financial sector, I have not obscured my own conviction of the important part that securities markets can play in that process, and of the desirability that governments should aim to create liberalized rather than repressed markets.

ROLE OF THE REGULATOR IN DEVELOPING THE SECURITIES MARKET

by

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Chairman, Securities and Exchange Commission
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INTRODUCTION

Securities markets evolve over time, growing and declining in response to various stimuli and other adverse influences. The principal factors that affect a securities market are economic, fiscal, political and, generally to a lesser extent, social and educational. Some factors that influence the market are internal and others are external. Some factors can be created or controlled, others come unexpectedly, sometimes suddenly, or are beyond control.

The stable markets are those that grow steadily in volume and value with a minimum of market ups and downs. It is growth and not merely size that attracts investors. A large market that is declining drives away investors. A small market that is growing and shows a potential for growth, with economic and political stability, attracts investors. But too rapid a growth that promotes uninformed bull trading invariably results in a market correction that can often be painful to new investors and harm further growth.

Probably as a result of my professional marketing background and my own experience as Chairman of the SEC in Sri Lanka since the inception of the Commission in October 1987, I believe that, especially in emerging securities markets, the regulator can and should play a vigorous, positive, and pivotal role in promoting the development and growth of the securities market. The regulator is really the "man in the saddle," and can best see how the market is performing and can best advise the government on policies and measures to develop the capital/securities markets. My own experience is that the members of the securities industry are primarily interested in self-promotion and are uninterested in generic efforts to promote market development. In the developed securities markets the individual self-promoting activities by the large number of institutions in the industry have an indirect but cumulative effect in developing the market. On the other hand, emerging securities markets in our countries are still grossly under-developed with only a minute fraction of the investing population engaged in the securities market. In Sri Lanka, my colleagues and I on the SEC decided at the very outset to devise and adopt a number of strategies, plans and promotions to make our market grow, and in my talk I will attempt to share with you our thinking and describe the strategies and promotions that we adopted and the results that we have achieved. As a professional manager with extensive marketing training and experience, I see the securities market as being closely akin to the other markets that trade in goods and services. The securities market has most of the features and uses most of the tools and elements of the "marketing mix" as the other standard markets. Thus, in the securities market we have sellers (investors seeking investment capital), buyers (investors seeking investment instruments), products (securities), a market place (the stock exchange and the trading floor), traders (brokers and other market intermediaries), exchange (the buying and selling of securities for money), price (the price of securities), and the use of communication through advertising, and promotions. The differences are that, like services, securities are essentially intangible because they have no stable form or substance, are changeable and even volatile, often have no determined life span, and are heavily dependent on the quality and reliability of the service offered by those who administer and regulate the market. But, like all other markets, I believe strategies, plans, and promotions can be used to make the market grow.

BRIEF HISTORY OF THE SHARE MARKET IN SRI LANKA

The history of the share market in Sri Lanka dates back to 1896 However, the market which served the needs of the sterling plantation companies and the number of shareholders was small. From 1904 to

November 1985 the market was administered by the Colombo Brokers' Association. The share market continued to remain small because, prior to Independence, the government was content to develop an economy based on plantations producing primary agricultural commodities, and an import and export trade. Industry received no encouragement and was left to develop on its own. Following Independence in 1948, successive governments followed policies based on achieving economic self-reliance using import substitution, backed by strict controls, and combined with the creation of a welfare state. Governments believed that investment in industry is best led by government and the private sector received little or no encouragement.

It is, therefore, not surprising that in this sterile economic and business climate the share market did not grow. In fact it declined soon after a new government took office in 1956, when as a result of the introduction of a policy of nationalization, sterling company interest weakened and looked for investment opportunities in other countries. The worst blow to the share market came with land reform in 1974 and other highly restrictive economic policies which virtually killed the share market.

The new economic policies of the government that took office in 1977, built on an outward looking "open market" policy based on market forces, competition, the dismantling or rapid liberalization of controls, emphasis on export development, and recognition of the private sector as the engine of economic growth, together with a number of tax and investment incentives, gave new life to the share market. A number of new companies, especially in the newly developing tourist and hotel industries, were formed which sought and successfully raised new investment capital through the share market.

However, it was not until July 1984 that share trading based on the open outcry system was established. In December 1985 the trading floors of the Colombo Brokers' Association and the Stock Brokers' Association were amalgamated to form the Colombo Securities Exchange, which later changed its name to the Colombo Stock Exchange.

When the Stock Exchange was formed, it established its own rules and administered and regulated itself in the absence of a regulatory authority. The only legislation that was directly relevant was the Companies Act. The first piece of legislation to regulate the securities market was the Securities Council Act No. 36 of 1987, which was certified at the end of August of that year. The Securities Council, renamed the Securities and Exchange Commission in mid-1991, was set up under the act to regulate the securities market. The three ex-officio members and the seven appointed members are appointed part-time, and the chief executive officer of the Commission who heads the secretariat is a paid Director-General, working full-time. Although the act provided for the regulation of the securities market and laid down the objects, powers and functions of the Council, it was described as an enabling act, and the Council was provided with a minimal budget. Although the members of the Council were all eminent and experienced persons in their own fields of work, none of them had any experience in regulating the securities market, and only a few had familiarity with the share market. As Chairman, I had neither. At that time I owned a small portfolio of shares acquired directly from share issues, and I had never traded any shares in the market. I had visited the New York Stock Exchange after I learned that I had been appointed Chairman of the Council whilst I was on holiday in the U.S.A., but I had not visited our own stock exchange, nor did I know any active share brokers.

INITIAL STRATEGIES

A quick visit to the Stock Exchange, a discussion with the Chairman and officials, and a study of the share market revealed the following picture. The share market had grown encouragingly from a total turnover of Rs. 79 million in 1985 to Rs. 288.5 million in 1987 and average daily turnover had grown from Rs.332 thousand in 1985 to Rs. 1.46 million in 1987. The number of shares traded had increased from 4.78 million in 1985 to 17.3 million by the end of 1987, and the number of share transactions from 4148 to 14,964 respectively. The All Share Price Index grew from 96.07 at the beginning of 1985 to 217.97, and the Sensitive Price index from 81.69 at the beginning of 1985 to 384.12 during this same period. Yet the market was still very small. Only 168 companies were listed, and of these the shares of less than 50 were being traded regularly and the total turnover represented less than 2 percent of the total number of shares issued. The Stock Exchange had only seven members. Shares of listed companies were being tightly held and new companies were reluctant to seek listing both through fear of losing control as well as unwillingness to become subject to the required corporate disclosure. At the same time, banks were only too willing to give substantial roll over loans to finance even investment capital needs.

With this scenario, the Commission decided upon the following preliminary strategies:

(1) Conduct market research to determine investor habits, attitudes and perceptions.

(2) Arrange for a study of the capital market to determine its size, composition and characteristics.

(3) Obtain the services of technical experts to review the Securities Council Act to make it more effective.

(4) Obtain the services of technical experts to study and review the rules. by-laws, procedures, and systems and administration of the Stock Exchange so as to enhance its capability to provide more efficient and effective investor services and provide quicker and more accurate market information with the necessary electronic hardware and software.

(5) Arrange to visit neighboring securities markets to study and learn from their experience, regulatory methods and systems.

(6) Quickly find foreign donor agencies that would be willing to support and fund the above activities.

We were very fortunate to find a very responsive and willing donor and supporter in the USAID in Sri Lanka. Soon thereafter, the Asian Development Bank too pledged its support to the Council. By the Middle of 1988 the market research survey was completed. Its results confirmed our own hypothesis that although the savings habit was widespread, almost all investors preferred to invest their savings in fixed deposits with banks, savings institutions, and finance companies that paid a fixed return in the form of interest.

Almost all investors were ignorant about the share market, and most were either suspicious of it or had negative feelings toward investing in it. Very few appeared to appreciate the adverse effects of inflation upon the purchasing value of money held in fixed deposits, and even the few who were active investors in the share market hardly understood this subject. Investors felt that company directors only look after their own interests and not those of the shareholders. The need for investor education was obvious.

The study of the capital market was completed by August 1988, and it too confirmed some of the findings of the market research survey. In addition, it showed the need to encourage the setting up of new financial institutions such as merchant banks, venture capital companies and unit trusts, as well as new securities such as bonds and debt securities.

Study visits to emerging and emerged securities markets, especially in the South Eastern and Far Eastern Asian Region, gave us valuable insights into effective regulation, market development, and the dissemination of accurate and speedy market information. In particular we were very impressed with the electronic Central Depository System in Bangkok.

Based on the above, the following initial strategies were adopted with the promise of funding and technical assistance from USAID and the ADB:

(1) Study, review, and proposed amendments to the Securities Council Act. This was completed in 1990 with the assistance of a technical expert.

(2) Another technical expert made a thorough study of the Stock Exchange, its rules, by-laws, systems, and administration and a very comprehensive report also completed during 1990.

(3) Another technical expert studied the existing state of market monitoring, surveillance, compliance, and enforcement capability and made several urgent recommendations.

(4) Set up of a Central Depository System to provide post trade automation of share transactions, enable scripless share trading, and the accounting for share transactions, plus the speedy dissemination of market information.

(5) Conduct a public awareness campaign to educate the public and attract them to the share market.

(6) Arrange with the Ministry of Education to include "The Securities Market" as a subject for commerce students at the A Level Examination. This is being implemented. A mini-textbook to supplement the standard textbook on Economics & Commerce has been printed, a teachers' guide prepared, and a core-group of teachers trained to serve as trainers.

(7) Conduct workshops on the securities market and capital market, with expert technical assistance, for brokers and others employed in the securities industry. These were completed during 1990-91. They were preceded by a conference on the Role and Function of Capital Markets in Economic Growth for policy makers and senior decision makers in this area.

(8) Propose tax incentives to attract investors to the share market and thereby stimulate rapid market growth.

(9) Encourage the establishment of specialized financial institutions such as merchant banks, venture capital companies and unit trusts. Today we have four venture capital companies with another being set up, three merchant banks, and four unit trusts.

Unfortunately our efforts were hampered during 1988 and 1989 when the country was severely affected by civil disturbances which disrupted the economy and industrial and commercial activity and sent the securities market into the doldrums. But we persevered with our activities which were to produce dramatic results during 1990 and 1991, after the civil disturbances had been brought under control, and several new measures were put into place by the Government.

CATALYSTS FOR RAPID MARKET GROWTH

Beginning in 1990, the share market grew rapidly and enjoyed boom conditions right through 1991 as well, reaching dizzy heights beyond our expectations. Several factors and events contributed to this rapid growth:

(1) The successful suppression of civil disturbances in the South before the end of 1989, enabling industry, trade and commerce to recover and grow and infusing new confidence in the economy, and the fact that the presidential and general elections were held despite strong subservient efforts to disrupt them, created confidence in the basic political stability of the country.

(2) An increase in the inflow of tourists giving a much needed shot in the arm to the sagging tourist industry.

(3) The New Industrial Strategy announced by the Minister of Industries in early 1990 clearly assigned to the private sector the lead role in promoting economic growth, with a new package of tax incentives to encourage new investment, job creation and exports.

(4) Government's commitment to the Peoplisation Programme promised the infusion of a large number of new shares into the market, increasing share liquidity and the bringing in of a large number of new shareholders through its scheme to gift 10 percent of the shares of "peoplised" state owned enterprises to the employees.

(5) The decision to open the listed share market to foreign investors up to 40 percent of the issued capital in these companies by the withdraw of the 100 percent Property Transfer Tax on shares traded by foreigners, in June 1990. This decision was greatly influenced by the advice given to the Government that the capital market was probably too small to absorb the Peoplisation Programme and that, in any event, the transfer of such a large amount of funds from the capital market to the government was not desirable.

(6) The relaxation of Exchange Control Regulations to allow the free flow in and out of the country of foreign exchange brought in for [illegible]ing in the share market.

(7) The excellent results declared by most public quoted companies for the year 1989/90, which underscored the basic stability and resilience of the economy to bounce back quickly after difficult times. The foreign financial press carried highly favorable comments based on studies done on the share market by a well known international fund and investment management institutions which described Sri Lanka as newly emerging securities market that offered attractive investment opportunities for foreign investment.

(8) As mentioned earlier, a generous range of tax benefits relating to investment in the share market was announced in the Finance Minister's Annual Budget speech in November 1990. The principal measures were the withdraw of the Capital Gains Tax on all shares purchased and held for a minimum period of one year, with a reduced rate of only 20 percent on sales made earlier, the

removal of the Wealth Tax on shareholdings in listed companies, the removal of the Withholding Tax on dividends declared by listed companies, plus several other tax exemptions to facilitate and encourage the setting up of unit trusts.

(9) Double Taxation Relief Agreements and Investment Treaties and Agreements were signed with many countries.

RAPID GROWTH OF THE SHARE MARKET

Even before foreign investors came into the market in June 1990, share prices boomed in anticipation of their coming. Except for a mild dip in the market soon after the Gulf War was declared, the share market continued to grow through 1990 and 1991 in a truly spectacular manner as will be seen in the tables, charts and graphs in the annexure. For example, total trading turnover which was just Rs. 225.8 million in 1989 soared to Rs. 1.56 billion in 1990 and escalated to Rs. 4.3 billion (excluding a further Rs. 1.24 billion extraordinary transaction). The daily average turnover rose from Rs. 1.1 million in 1989 to Rs. 6.6 million in 1990 and to Rs. 17.6 million in 1991. The number of shares traded jumped from 12.2 million in 1989 to 41.7 million in 1990 and to 79.2 million in 1991. Similarly the number of share transactions soared from 16,792 in 1989 to 48,332 in 1990 and as many as 91,571 in 1991. Market capitalization, which was a low Rs. 17.1 billion at the end of 1989, jumped to Rs. 36.9 billion in 1990 and then leapt up to Rs. 81.1 billion in 1991. During this period the All Share Price Index rose from 179.49 at the end of 1989 to 384.39 in 1990 and to 837.89 in 1991. Similarly, the Sensitive Share Price Index jumped from 341.74 in 1989 to 680.30 in 1990 and to 1198.65 in 1991.

As mentioned earlier, the entry of foreign investors was the principal factor that led to the share market boom. Purchases and sales by foreign investors during the two years were Rs. 7.2 million and Rs.435.6 million respectively. Today nearly 70 investment funds are registered in the country. Initially foreign investors were interested largely in the shares of blue chip companies, especially the large local groups in which they saw undervalued assets with good growth potential, and so paid what then appeared to be very high prices for their shares.

Only five new companies were listed during 1991, which was disappointing. However, nearly all these public share issues were heavily oversubscribed. Whereas earlier share issues attracted only a few thousand share applicants, with the exception of one that had been marketed cleverly, these new share issues drew in some 40,000 over-enthusiastic applicants. It was obvious that many new investors were rushing into the market, tempted by the news of quick and big profits.

THE INEVITABLE MARKET CORRECTION

As was to be expected, the market, which had become overheated due to the sustained bull market conditions through two whole years, entered into an inevitable market correction early during 1992. I believe that the market correction was welcomed, even though, sadly, several investors must have been financially hurt. But, what I find most encouraging is the fact that the market correction did not cause market panic, in fact, investors have been behaving in a very mature and balanced fashion. Both sellers and buyers have been acting with commendable caution and patience, with the result that the decline in the market has been relatively small and gradual. I feel that the Public Awareness Campaign is at least partly responsible for this mature market behaviour, but it is obvious that more market education is necessary. It is estimated that the number of shareholders has increased sharply from about 15,000 to some 60,000.

A critical study of the share market movements show that from January 1992 the All Share Price Index and the Sensitive Price Index had fallen slowly but steadily by 14.2 percent and 14.92 percent respectively as at the end of August, with signs that the market correction had started to bottom out by then. Yet, compared with the same period in 1991, total market turnover was up by 101.4 percent, average daily turnover by 97.9 percent the number of shares traded by 81.9 percent, the number of share transactions by 113.2 percent, and market capitalization by 37.6 percent. The lesson to be learned is that a too sharp and too long bull run in the market usually results in an uncomfortable and discouraging market correction which tends to shake investor confidence and interest, especially in an emerging market. A more modest but steady growth is much more beneficial.

Incidentally, foreign investor interest in the market from January to August 1992 slowed but was still significant. Total purchases amounted to Rs. 1.421 billion, and total sales amounted to Rs. 0.883 billion, with a net gain of Rs. 0.538 billion. This compares with total purchases of Rs. 1.270 billion and total sales of Rs. 291.545 million during the same period during 1991.

STRATEGIES FOR THE NEXT THREE YEAR PERIOD

It could be said that during the last few years our strategies concentrated upon building our market regulatory and systems procedures, enhancing the capacity of the Stock Exchange to disseminate accurate market information speedily, and educating the investing public as well as the market operatives. During the next few years, our strategies will concentrate upon the following areas:

(1) Improve and enhance market surveillance to achieve greater compliance and enforcement where necessary. This will be done both by the Commission and the Stock Exchange. Good self-regulation backed by effective surveillance and enforcement are essential for promoting investor confidence. Special technical assistance has been arranged to establish the systems, procedures, and guidelines, and to train the staff of both the Commission and the Stock Exchange.

(2) In order to bring greater discipline into the market, the Commission will obtain the legal power to regulate all public offerings of shares, in both the listed and unlisted markets, and also all market intermediaries engaged in the securities industry. Regulation will also cover Employee Share Ownership Plans.

(3) A company mergers & take-overs code will be put into operation.

(4) Better standards of financial reporting and disclosure by listed companies will be promoted in collaboration with The Institute of Chartered Accountants of Sri Lanka.

(5) The Central Depository System will be provided with additional capacity and better back-up and security facilities.

(6) The Public Awareness Campaign will be continued to promote greater investor education. In addition to another educational advertising campaign, arrangements have been finalized with the

Asian Development Bank to conduct a seminar for policy makers and senior decision makers on the role and function of capital markets in promoting economic growth, plus a series of training workshops for investors, stock brokers and investment managers, and other professionals engaged in the securities industry. Education through well written articles to the newspapers, and public seminars will also be carried out. The programme to educate A-Level Commerce students on the securities market will be put into full gear, supported by the specially prepared and printed mini-textbook on the securities industry.

(7) The special drive, already started, to promote the professional skills and performance by stock brokers and investment advisors will be continued. By early next year, all stock brokers and investment advisors in stock brokering firms and investment managers in the management companies of unit trusts will have completed a special training course, examination, and certification organized by the Commission and the Stock Exchange, using the services of an expert trained in the U.S.A. The foreign brokering firms that have been allowed to join in partnership with local brokering firms will be encouraged to transfer technology and skills, conduct market research, and establish contacts for their local partners with foreign markets. All brokering firms will be required to acquire the necessary equipment, facilities, and staffing to provide a more professional service to their clients.

(8) The Stock Exchange and its members will be encouraged to promote new companies to seek listing and find ways to increase the supply of securities into the market. At the same time, steps will be taken to encourage the introduction of new types of securities into the market, as well as the setting up of market professionals and services such as investment managers, investment advisors, and credit rating agencies. We will also examine the desirability of establishing a lower level of listing requirements to enable a new category of medium and smaller companies to enter the listed market. We will also conduct a study to establish the feasibility and the timing for setting up an Over-the-Counter-Market.

All these strategies and consequent activities will require the hard work and commitment of both the Commission and the Stock Exchange, working together in partnership with shared objectives, goals and targets. We will need the full and active support of the government for our joint efforts, and the success of our joint efforts will be reflected by the extent of investor confidence both local and foreign, and participation in the securities market.

COLOMBO STOCK EXCHANGE

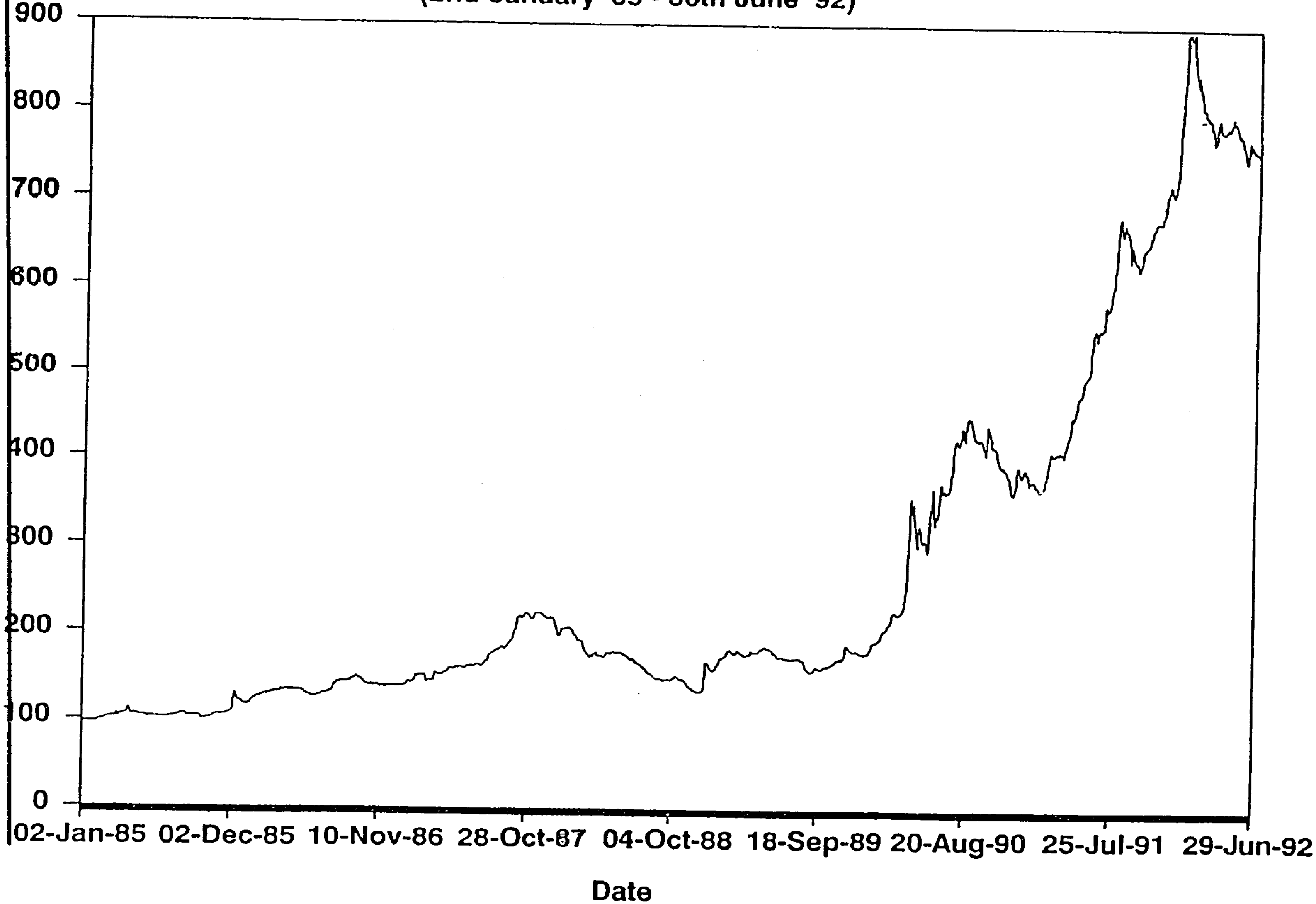
Stock Market Information Service

SUMMARISED TRADING STATISTICS 1992

	January	February	March	April	May	June	upto 28th July
Total Turnover (Rs.)	870,511,758	387,735,356	519,200,829	437,769,754	517,860,223	413,476,300	325,460,256
Domestic	569,122,882	257,161,165	375,613,452	242,900,000	412,752,266	282,962,098	207,752,559
Foreign	301,388,876	130,574,191	143,587,377	194,869,754	105,107,957	130,514,202	117,707,697
Market Days (No.)	21	18	21	17	18	22	19
Daily Turnover Average(Rs	41,452,940	21,540,853	24,723,849	25,739,397	28,770,012	18,794,377	17,129,487
Shares Traded (No.)	12,884,111	6,503,013	8,060,522	5,400,908	8,614,798	6,575,333	5,403,658
Transactions (No.)	12,913	7,290	9,044	7,778	9,355	9970	8,267
Companies Traded (No.)	131	119	114	110	120	130	125
New Listings (No.)	-	-	2	-	4	1	-
De-Listings (No.)	-	-	-	-	-	-	-
Companies Listed (No.)	178	178	180	180	184	185	185
Market Capitalisation (Rs)	83,462,949,576	78,296,072,304	78,564,547,361	79,955,029,002	76,527,733,459	74,240,850,151	71,449,144,036
All Share Price Index	843.08	797.90	781.52	793.73	753.78	762.03	728.12
Sensitive Price Index	1,164.37	1,103.88	1,107.39	1,121.38	1,084.02	1,082.55	1,038.31

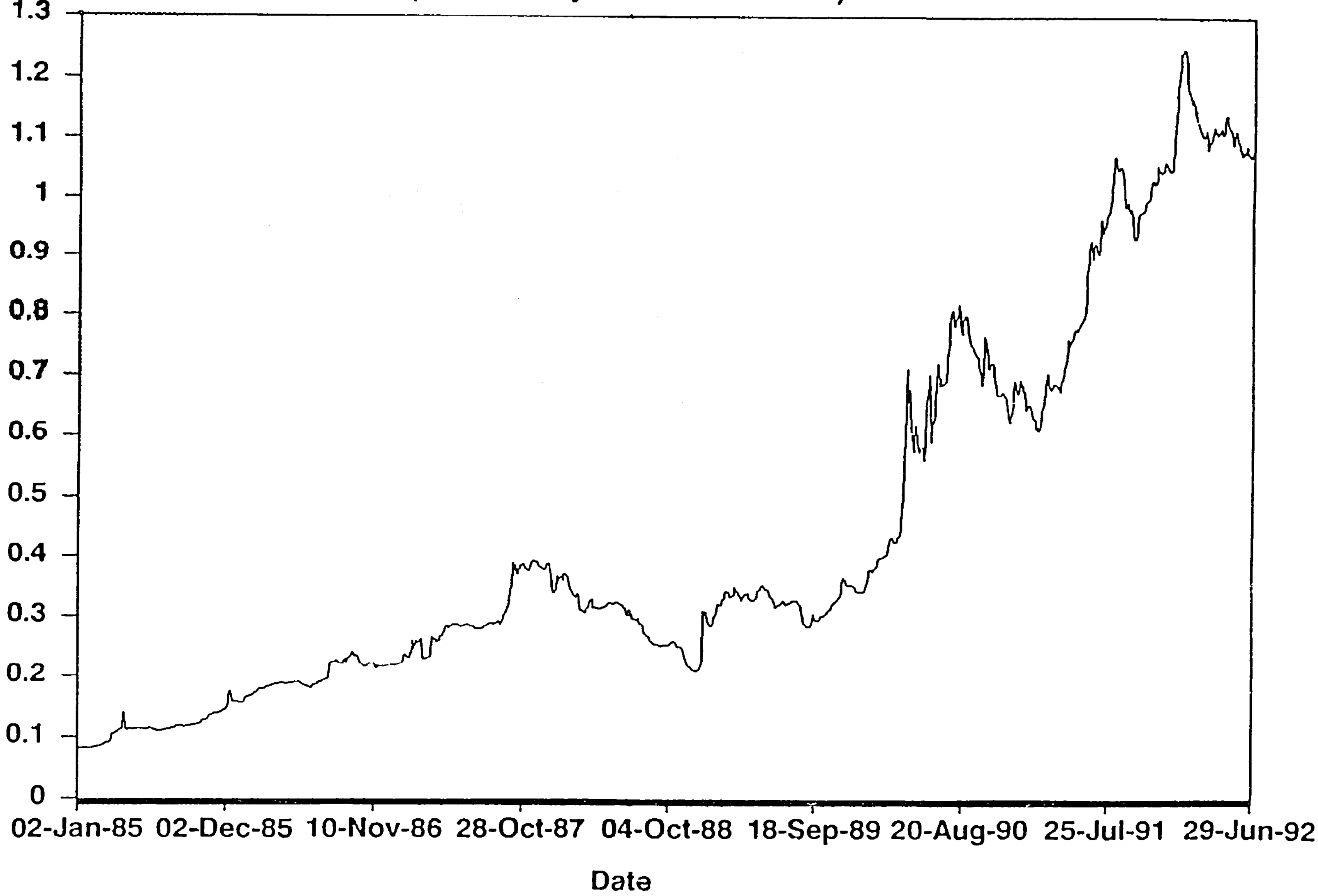
CSE ALL SHARE PRICE INDEX

(2nd January '85 - 30th June '92)



CSE SENSITIVE SHARE PRICE INDEX

(2nd January '85 - 30th June '92)



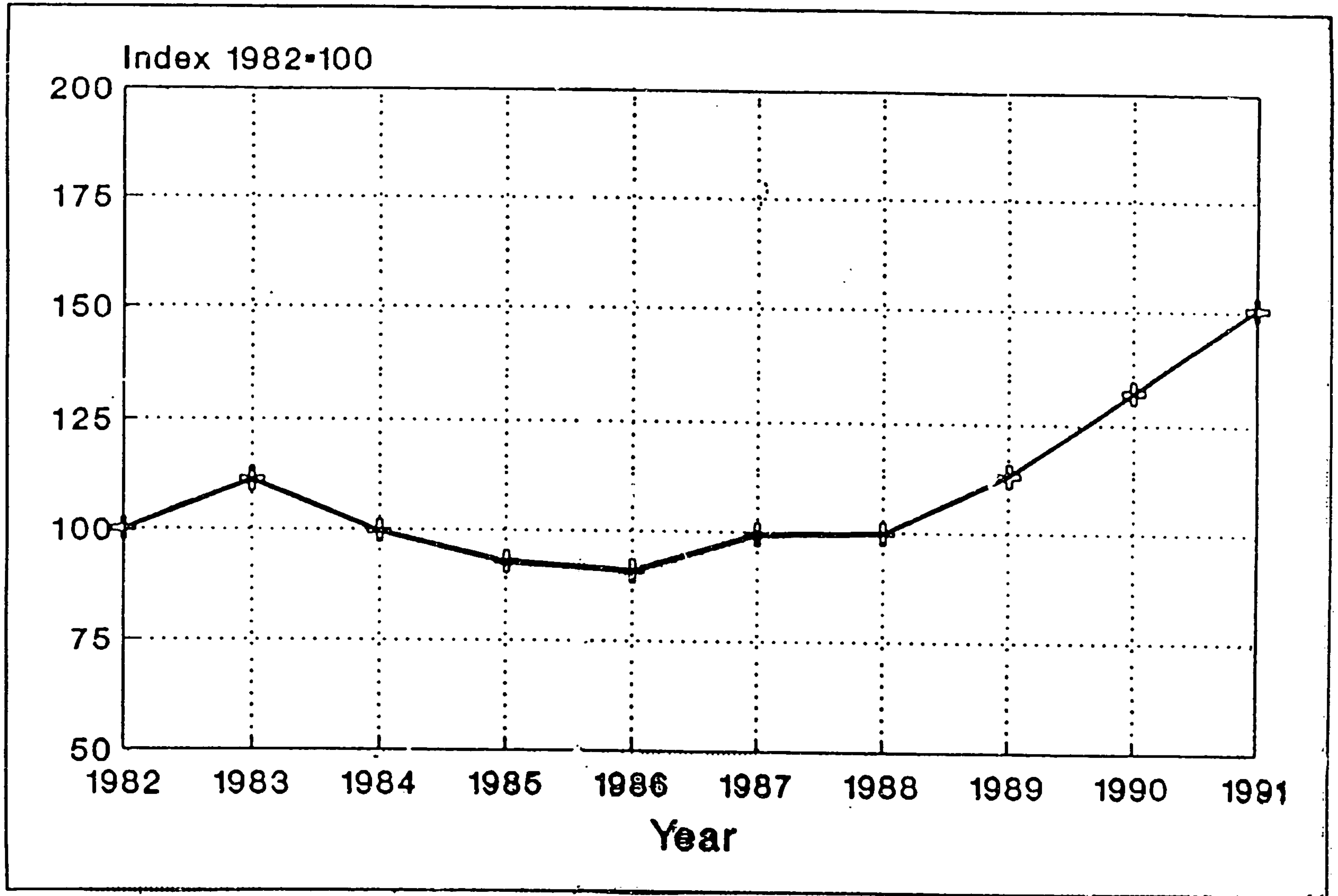
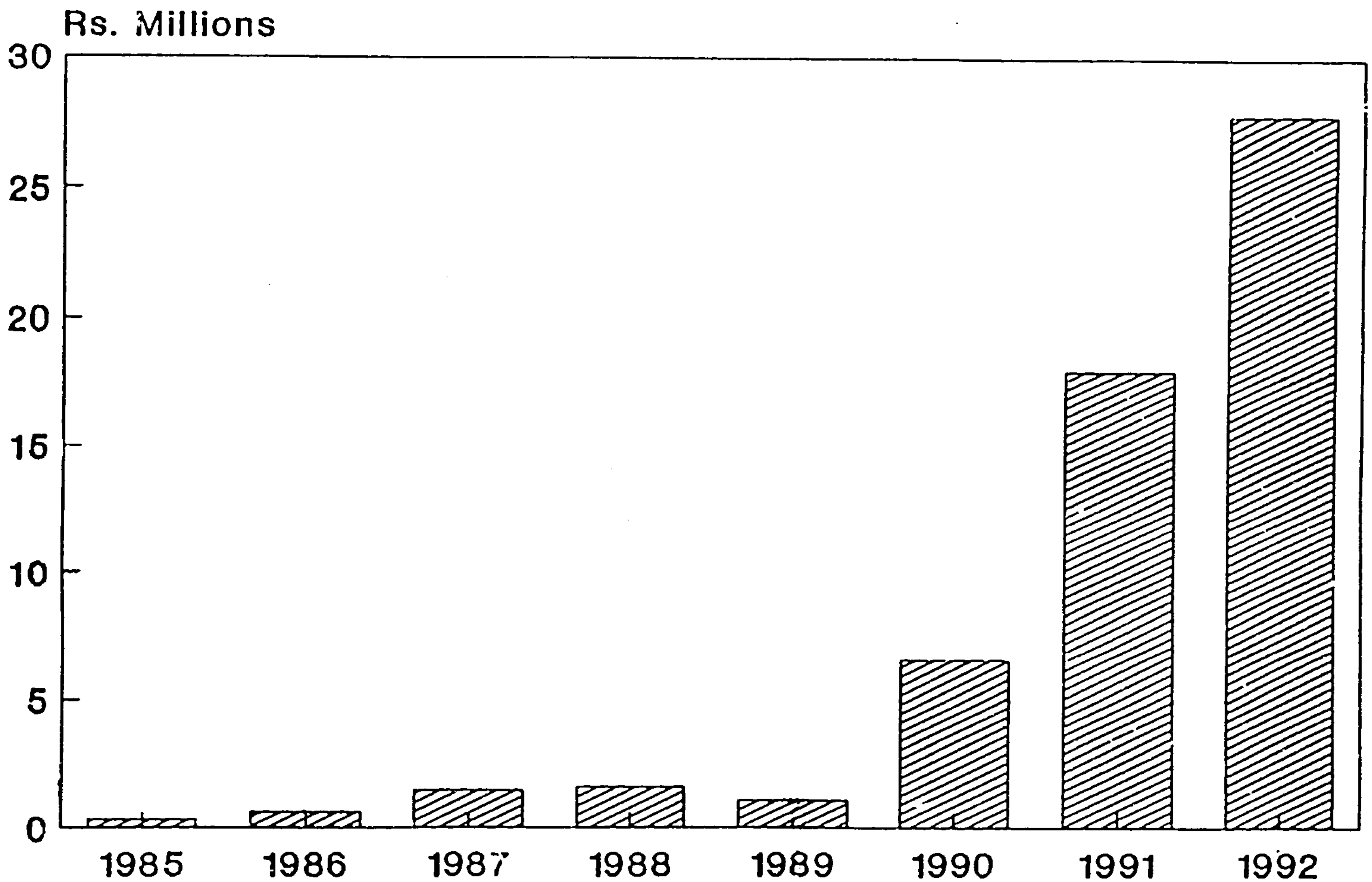


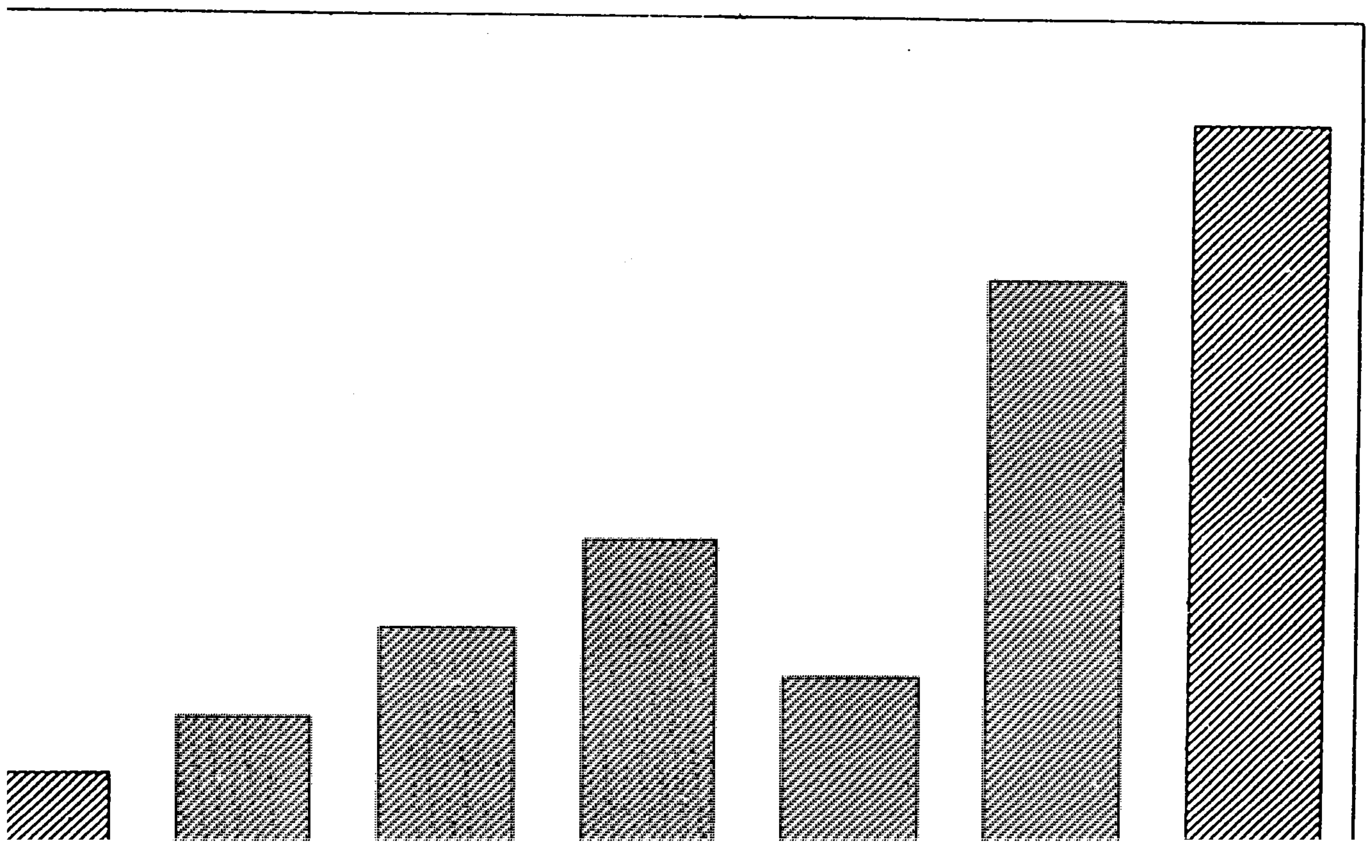
Figure 4: Private Sector Real Investment Index (1982=100)

Average Daily Turnover 1985 - 1992 June

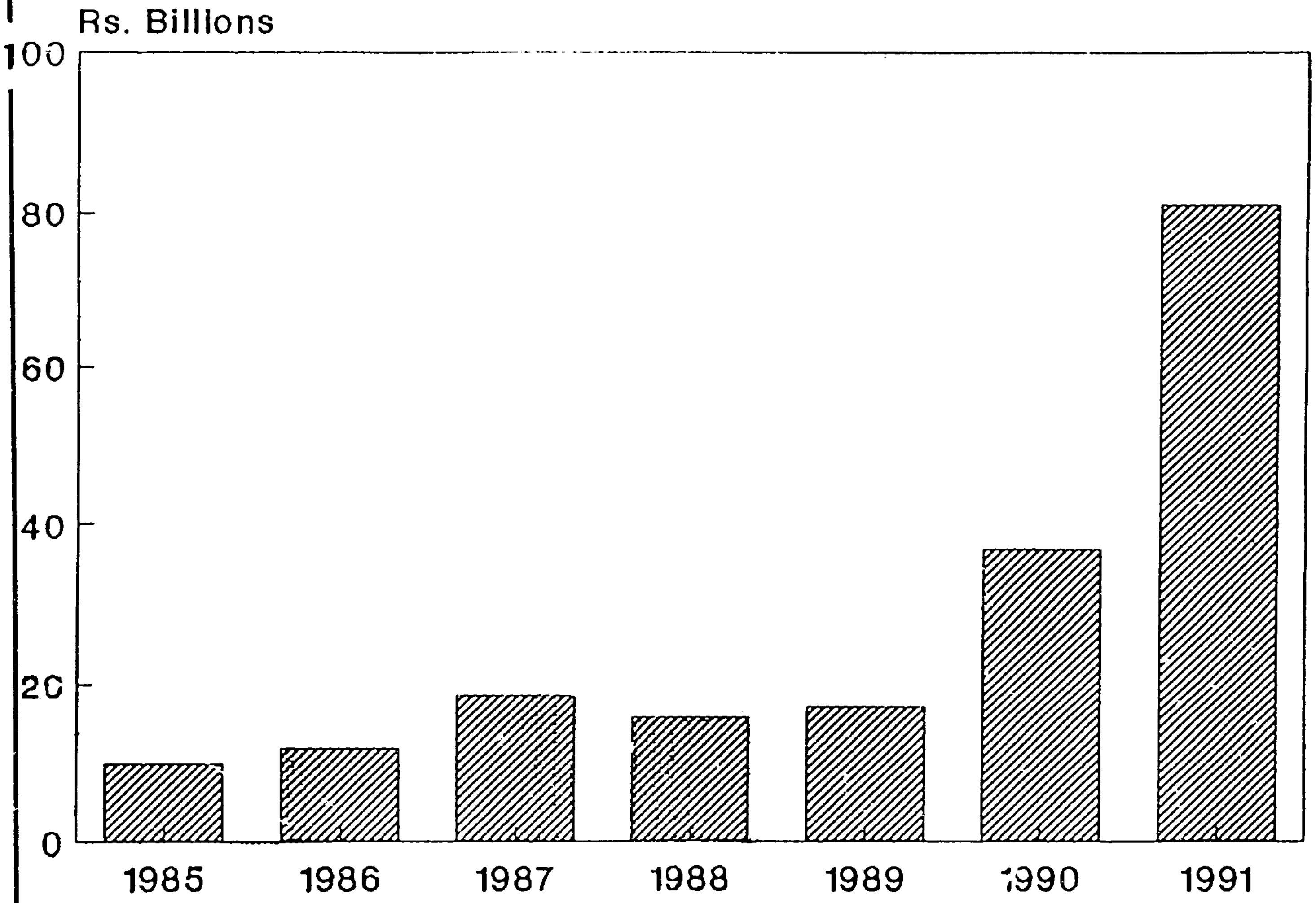


COLOMBO STOCK EXCHANGE

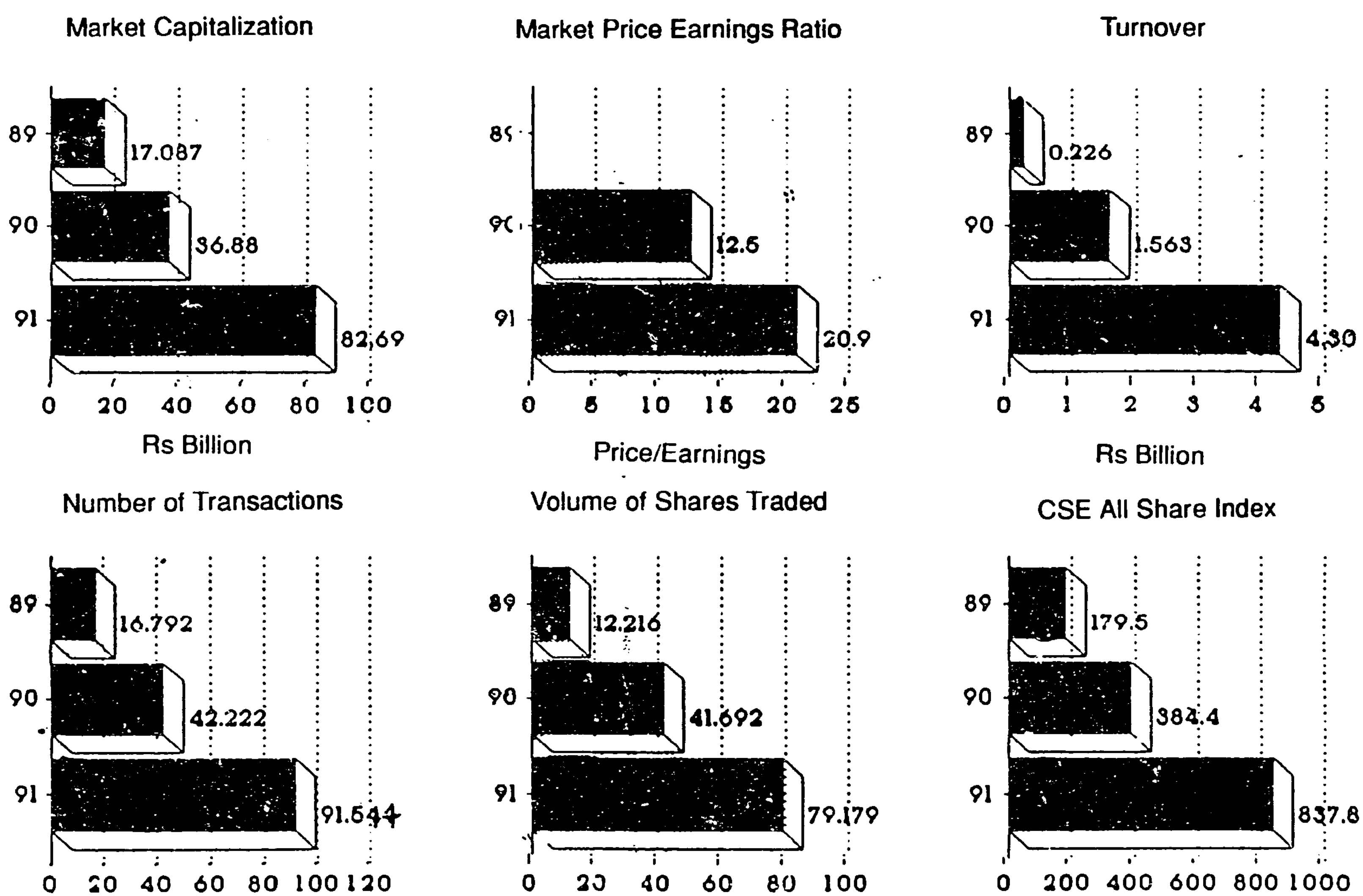
Trading Turnover as a % of Mkt Capital



Market Capitalization 1985 - 1991

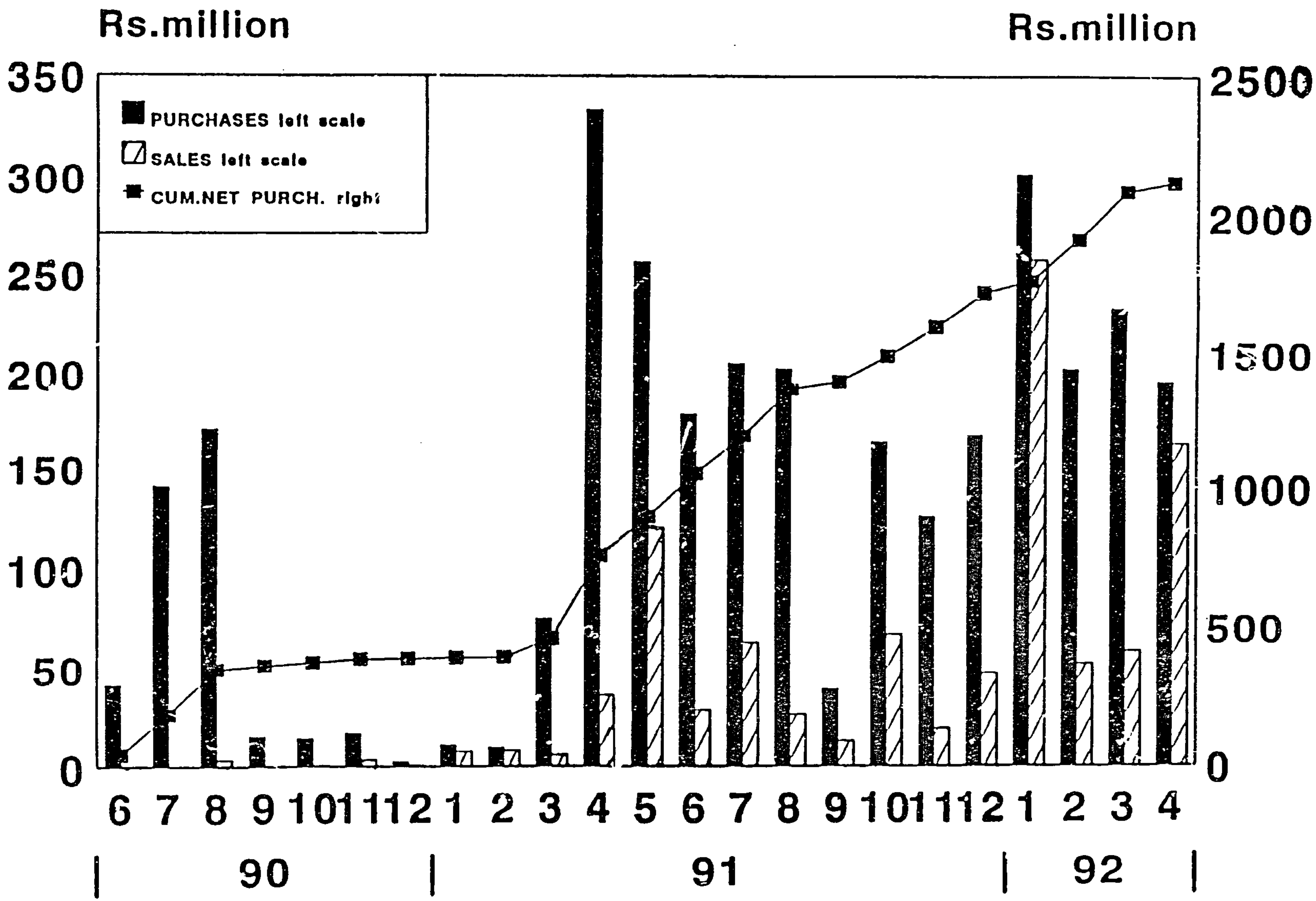


COLOMBO STOCK EXCHANGE



Market Capitalization
89
90
91
17.087
36.88
82.69
0 20 40 60 80 100
Rs Billion
Market Price Earnings Ratio
89
90
91
12.6
20.9
0 5 10 15 20 25
Price/Earnings
Turnover
89
90
91
0.226
1.563
4.30
0 1 2 3 4 5
Rs Billion
Number of Transactions
89
90
91
16.792
42.222
91.544
0 20 40 60 80 100 120
Volume of Shares Traded
89
90
91
12.216
41.692
79.179
0 20 40 60 80 100
CSE All Share Index
89
90
91
179.5
384.4
837.8
0 200 400 600 800 1000

Foreign Investment In the Columbo Market



THE BALANCE BETWEEN OVERSIGHT REGULATION BY THE REGULATOR AND SELF-REGULATION BY THE STOCK EXCHANGE

by

Tom Healy
General Manager, Irish Stock Exchange

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INTRODUCTION

This subject is one in which we are investing a lot of thought and discussion in Ireland at present. We are in the process of changing from a system largely of self-regulation by the stock exchange subject to broad oversight by the Department of Finance. Our new system, which is at an advanced stage of planning, will involve more direct oversight, and in some areas direct intervention, by the Central Bank of Ireland, combined with a high degree of self-regulation by the Irish Stock Exchange. We have studied the question of balance in detail and also reviewed the structures in other countries in the European Community. The model that we are moving toward represents, in my view, a balance that is designed to meet, as far as possible, the various needs and conflicts that are part of every securities market whether it is developed or developing.

One clear lesson we have learned from the process we have recently gone through is that there is no single answer or blueprint for the balance between oversight or regulation by an external regulator and self regulation by a Stock Exchange. (For the purpose of this speech, when I refer to the regulator I mean an external regulator, like the SEC in the U.S. or indeed in Sri Lanka). Wherever you have such external regulators you will find that the division of functions between them and stock exchanges and the degree of oversight the regulators perform vary considerably from country to country. While deciding on the best workable balance may seem simple on a theoretical level, it is far from this in practice.

PHILOSOPHY OF REGULATION

There is a philosophy of regulation which, in Europe at least, has evolved in its present form over the past decade. It is simple — the regulatory structure must ensure investor protection and confidence while facilitating the health and development of the market itself. You might say there is nothing new in this, it is simply stating the obvious. What is important, however, is that it recognizes that the regulatory structure will have to deal with conflicts and achieve a balance that, while it will not make everyone happy, will safeguard and encourage investors while allowing the market sufficient freedom and encouragement to develop.

Our structures of regulation must, therefore, achieve a reasonable balance between a range of conflicting needs. I will now refer to some of the more important conflicts:

(A) **Small investors vs. big investors.** Small investors need a high degree of protection in relation to the types of investment and prices offered to them. They are in a weak position in relation to the broker and can easily be led into investments which are totally unsuitable for them. Big investors, such as fund managers, are in a strong position in relation to the broker. They expect brokers to look after their buying and selling needs on a priority basis because of their importance as clients. The conflict here is that the regulator has to protect the small investor but keep the big investor in the market.

(B) **Domestic vs. foreign investors.** All developing markets want to encourage participation by foreign investors. Foreign investors are wary of small, less-developed markets. They expect to be welcomed but fear that when they want to sell they may not be treated fairly, or the market may not be liquid enough. There is a strong temptation on the part of brokers to give them preference. While the regulator and the stock exchange must ensure that there is no unfair treatment of foreign investors, they must also ensure they are not given unfair advantage over local investors. Foreign investors will come and go but you will always have to rely on domestic investors to create the basic level of liquidity that attracts foreigners. We must remember that foreign investors will tend, for macro-economic or world market reasons, to all be buyers or sellers in your market at any one point in time. They will never provide the basic level of liquidity — at best they will top it up.

(C) **Brokers v. small investors.** Some systems of regulation go so far in placing restrictions on brokers and trading that they kill off the freedom and profitability of brokers. Brokers who are unprofitable will go out of business or provide services at the lowest possible levels of cost, and therefore quality. We must recognize that it is brokers who develop a market and they must be profitable if they are to invest in development. They must also have the freedom to innovate.

(D) **Regulator vs. stock exchange.** One seldom finds a regulator or a stock exchange which believes that part of its functions would be better performed by the other. It is natural for each to seek the maximum degree of power and control and it will do so in the belief that this is in the best interest of the market. Within this conflict is the perception that there would be conflict between heavy-handed regulation by the regulator and light-handed regulation by the stock exchange.

The above conflicts exist in almost every stock market. The challenge is to resolve them in a way that the needs of any one group do not unduly dominate those of another.

The reason I have outlined these conflicts is to illustrate that the solution to one of them might call for a different balance between regulator and exchange than would another. I would argue therefore that the balance must not be chosen by the bureaucratic layer model whereby the same degree of balance is applied in all areas of regulation or in resolution of all conflicts. The balance between regulator and stock exchange should be decided separately for each area of regulation or market function. Furthermore, the decision on what balance is appropriate in each area must be based on objective tests which I will discuss shortly.

BALANCE — TEST BY FUNCTION

I will suggest six tests that should be applied to help make a decision on where the balance should lie between oversight regulation by the regulator and self-regulation by the stock exchange. I will then suggest that regulation should be divided into five areas and that the balance should be decided separately for each of these.

(A) **Investor Confidence.** This should not be confused with investor protection which I will deal with next.

Investor confidence in your system of regulation is obviously of enormous importance and tends to be a very subjective judgement. Foreign investors in particular will approach a developing market with suspicion. They expect, as I said earlier, to be welcome when buying into the market but fear they will not be treated fairly when selling out. If the stock exchange is run exclusively by or dominated by brokers, as is usually the case in developing markets, foreign investors will rely more on the regulator to safeguard their interests. This leads markets to give the majority of power across the board to the regulator for this reason alone. It is a very important consideration but is not the only test that must be applied.

(B) **Investor Protection.** This should be a more objective test based on an examination of whether the regulator or the stock exchange is in the better position to ensure that the interests of investors — large and small, domestic and foreign — are protected. It should take into account the relative strengths of brokers and investors in each of these cases but should avoid making a distinction on the basis of domestic versus foreign alone. It should consider if the stock exchange personnel are in a better position to protect investors if they are closer to the market on a day-to-day basis or if it is more effective to have decisions in this area taken outside the stock exchange by personnel not affected by day-to-day relationships with brokers. However if the system of investor protection is seen not to work, perhaps because it has been allocated to the wrong organization, confidence will disappear.

(C) **Expertise.** Allocation of regulatory functions should take account of the expertise that will be required to discharge this function. If the expertise already exists, for example in the stock exchange, this should be an influence for leaving the function there, subject to the other tests. However, if the area is one which is likely to continually develop and change, requiring different or new expertise, the question becomes where is the expertise itself likely to develop? Another question under this test is whether the expertise benefits from proximity and easy access to another expertise which may be available in only one of the organizations.

(D) **Speed and Efficiency.** Certain areas of regulation require instant decisions by people who fully understand the case in question and its context. This tends to suggest that the stock exchange should have primary responsibility for these functions in relation to the market and the brokers. However, this situation can be balanced by having an appeal or subsequent approval procedure allocated to the regulator.

(E) **Evenness/Fairness of Treatment.** There is always a concern that the stock exchange, especially if it is dominated by brokers, will find it more difficult to be fair and even-handed in deciding on disputes between brokers and investors, and between different types of investors. The need for evenness of treatment may also arise between the securities market and other parts of the financial markets. Care must be taken that different standards of regulation do not result in the flow of savings being diverted to or from a market for the wrong reasons. Basically the standard of regulation should be equally high across the financial markets but it should not of itself interfere in economic or commercial decisions.

(F) **Partnership vs. Conflict in Regulation.** A factor to be considered when deciding on the balance must be whether it is likely to facilitate partnership and cooperation as opposed to conflict between the regulator and the stock exchange. One recognizes that this is not always practical but both parties should be as comfortable as possible with the balance in each area.

FUNCTIONS

(A) **Listing and Regulation of Companies.** This is a highly specialized function in most developed markets and lies equally often with the stock exchange and an external regulator. In many developing markets, however, it is not a developed function and the behaviour of companies is governed mostly by how they wish to be seen by the market. If a company does not need to raise new capital in the near future it will often treat the market and its investors with disdain in terms of information and dividends. A market in this situation will have to develop an effective regulatory regime, probably supported by statutory powers, if it hopes to attract foreign investors in particular. The tests outlined earlier are likely to be fairly neutral on whether this function should be with the regulator or the stock exchange. However, brokers and the stock exchange may be more likely to be in touch with the requirements of various types of investors, particularly small investors who are more likely to be poorly treated by companies. The overriding consideration must be which organization is likely to have the expertise and develop both market requirements and expertise in line with developments in other markets.

(B) **Market Regulation.** By market regulation I mean the regulation of trading, reporting of deals, publication of prices, and resolving of disputes between brokers. It requires understanding of and sensitivity to the trading process, speedy decisions, and the ability to achieve compromise where neither side is clearly right or wrong. The allocation of this function to the regulator or the stock exchange is usually neutral in relation to investor confidence or protection which are more dependent on broker regulation. In practice this is always a core function of the stock exchange and the regulator is not directly involved.

(C) **Broker Authorization and Regulation.** Investor confidence and investor protection would, on the surface, tend to suggest that this should be handled by the regulator. However it is a constantly developing function with the advent of new products and practices. So, the most important consideration should perhaps be the existence and future development of expertise. In most developed markets this traditionally rested in the stock exchange but has subsequently changed in some cases. In some markets also, the authorization functions are handled by the regulator and the continuing regulation of brokers by the stock exchange. Where the stock exchange is responsible for broker regulation the external regulator usually has control over the standards applied by the stock exchange. This is a major factor in investor confidence, particularly among foreigners. It should also help to ensure evenness of standards between the securities market and the other financial markets.

This is probably the area which will require the most careful and prudent allocation of functions between the regulator and the stock exchange as it has the greatest potential for conflict between them.

(D) **Capital Adequacy and Financial Regulation.** Unlike broker regulation, this can be a simpler area to regulate than it might seem. If a quality set of requirements and rigid reporting systems are established, the monitoring will be fairly mechanical with in-built alerts and warning systems. While the tests outlined earlier are otherwise neutral on who is responsible for this function, investor confidence would suggest it should be handled by the regulator.

(E) **Settlement.** This may or may not be operated by the stock exchange. Essentially settlement is a utility which must operate safely and efficiently and it should be supervised by the regulator or the stock exchange to ensure that it does so. Otherwise it is neutral on the tests I described earlier.

FINALLY

I have argued that the approach to striking the right balance between oversight by the regulator and self-regulation by the stock exchange should be to assess each major area of regulation separately and allow for a different balance for each of them, judged on its particular merits. However, I would also like to offer a few final suggestions:

(A) Regulatory structures should not be rigidly fixed in stone. They should be capable of change as the market develops. However, it would be wise to avoid ad hoc or piece-meal change. It would be better to have a regular major review of structures and balances, perhaps every two years or so.

(B) Regulators and stock exchanges at a similar stage of development should talk to each other to benefit from each other's experience.

(C) In South and South East Asia you have a number of stock exchanges which are at various stages of development. I find that developing markets, in particular, see themselves as competing with each other, for example in the same way as their textiles industries. Capital markets don't work like that. You are not in competition with each other so much as in competition with the developed markets. You have more common interest than competition between you. There is room for all of you in the world capital market provided that you develop the structures and standards that promote confidence. I believe that the best interests of each of you is served by working together to establish a standing for developing markets in general.

THE GLOBAL SHARE MARKET FOREIGN INVESTORS AND THEIR EMERGING MARKETS' EXPECTATIONS

by

J. Mark Mobius, Ph.D.
President, Templeton Emerging Markets Fund

To make generalizations about what all fund managers want from emerging markets is certainly presumptuous and probably quite impossible. But today I would like to tell you what we at the emerging markets team of Templeton consider when entering new emerging markets.

The critical areas include the following:

1. Foreign Exchange Controls
2. Taxation
3. Foreign Ownership Restrictions
4. Custodial Arrangements
5. Settlement Requirements and Systems
6. Pricing Information
7. Trading Fairness
9. Trading Efficiency
9. Trading Liquidity
10. Trading Transparency
11. Company Information Disclosure

Foreign Exchange Controls: The existence of any type of foreign exchange control presents a considerable barrier to market entry by international fund managers. It adds another element of risk to what is already a risky profession. If there is a possibility that foreign exchange controls may result in our not being able to exit a country, or just as importantly, delay our exit, then we have a considerable degree of risk. A delay, for example, could result in foreign exchange losses. In the past this happened to us in the Philippines. With foreign exchange controls in place the Central Bank of the Philippines required considerable documentation before money could leave the country. This resulted in delays, often as much as six mouths. During that time, the Bank decreed that the money could not earn interest, thus compounding the risk. So, we were sitting on deposits not earning interest with a steadily devaluing currency. Happily, the Philippines no longer has these restrictions. As a result, incidentally, more foreign exchange is entering the country.

Taxation: Foreign portfolio investors agree that taxation is necessary, but that taxation should be efficient and fair. If for example, taxation of investments results in double taxation — in the invested country and the borne country, which may often happen in cases where double taxation treaties do not exist — then it is not fair. If the taxation exists it should be easy to collect. This is why we do not object to taxation of dividends. Such taxation is easy for the government to collect since it can be withheld at the source and does not involve a great deal of paperwork on the part of the investor. However, the capital gains tax is another matter. With capital gains taxes the foreign investor is discriminated against since, for all practical purposes, he cannot reflect capital losses as domestic investors may. In addition, the entire record keeping and monitoring process of capital gains taxes, particularly for long-term investors, is extremely laborious. In 15 out of the 16 emerging markets in which we are now invested, there is no taxation of capital gains.

Foreign Ownership Restrictions: A few years ago my brother, who lives in the United States, complained about Japanese investment in America. He asked, "Don't you think Japan is buying up too much property and assets in America?" I replied, "Let them buy what they want. They can't take it back to Japan with them! We should be flattered that foreigners have so much confidence in the country. They will probably do a better job of taking care of those assets and improving them. They will also probably pay high prices." There is certainly a xenophobic attitude when it comes to foreign investment and thus a number of countries have restrictions on such investments. But these fears are misplaced and result in many problems. For example, in Thailand the limitations of what percent of a company foreigners may purchase leads to a disparity between the price of locally registered and foreign registered shares with foreigners often having to pay hefty premiums when demand is high. When the market declines the foreigners then suffer a double loss, the stock price declines and the premium disappears. More importantly, the entire market liquidity is affected and pricing confusion reigns. In China the foreign reserved "B" shares are now selling at a discount to the local "A" shares. The local investor is thus deprived of liquidity. Countries who fear foreign control and ownership may solve this problem very easily by simply creating a single "golden share" in each listed company which will have the power to prevent control of the companies from being taken over by foreigners. In this way the foreigners are free to purchase all the shares of a company and thus contribute to the overall market liquidity. Or the Mexican system may be used where shares are sequestered in the central depository when purchased by foreigners so that those shares may not be used for voting. As soon as the shares are sold to local investors their voting rights revert.

Custodial Arrangements: Prior to investing in any country, a foreign portfolio investor, like Templeton, must find a reliable and efficient local custodian who will take care for the safekeeping of the shares purchased, keep track of corporate actions such as dividends, act on those corporate actions, make payment for shares and receive or disburse shares certificates. In the global fund management business there is a careful separation of power between the fund manager and the custodian of the assets. Thus our global custodian chooses the local custodian bank and ensures that all concerns about trading and settlement safety and efficiency are satisfied. If there are no local banks with the experience or ability to undertake such work, it prevents us from investing.

Settlement Requirements and Systems: Foreign investors are quite concerned about settlement requirements and systems since any problems in this area could result in defaults, delayed payments, and additional costs. It is for this reason when a local stock exchange announces that they will institute a T+I settlement system that the foreign investors raise a hue and cry. This is because in this global investment arena, fund managers are managing assets from places on all continents. Instructions for transfer of funds or receipt of securities must thus travel around the world and originate in time zones quite different from the zone in which the trade was conducted. Each country has a different set of holidays and delays are thus inevitable. Foreign investors thus need a fair degree of time for settlement. We have found that a time frame of T+3 is best, since it allows for sufficient time for payments and transfers to be affected while not being too long and encouraging speculation. A fortnight, for example, I believe is much too long. But in order for a reasonably tight time frame to be achieved, all elements in the trading system must be coordinated and efficient. Last year when I was in Poland, one of the banks who is a member of the stock exchange described the settlement system as requiring a T+1 payment for the delivery of shares. I expressed satisfaction and told him that although difficult, we could meet that time frame as long as the bank was a member of SWIFT — the international telegraphic funds transfer system linking all major banks around the world. He said, "Oh yes, our bank is a member of that system. However there is one problem: although the bank can obtain instantaneous notification of payment, the department in charge of SWIFT operations is in the next building and it takes them three days to notify us of payment!"

Pricing Information: When purchasing millions of dollars worth of shares around the world on a daily basis, information regarding pricing is essential. This information must be timely and available while trading on the stock exchange floor is transacted or at least immediately after the close of trading. We subscribe to a number of very expensive stock price information systems such as Reuters. However, some markets are not sufficiently covered by these services or even not covered at all. In some cases, this is because the host country stock exchange restricts the release of such information to independent information services. This is quite ludicrous and is a severe impediment. Emerging stock markets should freely make available such information and even subsidize its dissemination worldwide since this will popularize their market and increase trading turnover.

Trading Fairness: The concept of trading fairness implies that each market participant will have equal access to shares at a given price. It means that when a seller offers stock at a given price, all buyers will have access to that offer and when a buyer offers to purchase, all sellers will have access to that offer. This is almost impossible when there are broker conflicts of interest. If a broker is also acting as an underwriter, corporate financier, fund manager, and also operating a trading account for his own benefit, it is extremely difficult if not impossible for him to resist the temptation to take advantage of buy or sell orders placed by his clients. When the client places a buy order at a given price and the market price is lower, the broker may first purchase at the lower price for his own account and then turn around and sell it to his client at the higher price. It is not surprising, for example, that recently one of the large U.S. brokerage houses announced record profits, the bulk of which came from trading for its own account.

Trading Efficiency: As fund managers we try to achieve the best possible returns for our clients. We thus must keep costs at an absolute minimum. Trading commissions and costs must be low, and this can be only achieved through efficient stock market settlement and custodial operations. Fortunately, stock market computerization is making great advances in efficiency. This could result in much lower trading costs and greater accuracy. Greater trading efficiency and lower costs lead to increased trading and liquidity. For example, after Taiwan installed a modem trading and settlement system, trading turnover exploded while important paperwork savings were achieved.

Trading Liquidity: The lack of liquidity in many of the emerging stock markets is a source of major problems for foreign portfolio investors. We at Templeton, for example, have about U.S. $2.0 billion in emerging markets money under management. Let us assume that we have 200 companies in our portfolio, or an average of U.S. $10 million per company. If we try to dispose of one of those companies, how long would it take to do so without disturbing the price when daily trading of that company amounts to only U.S. $100,000?

Trading Transparency: In order for the investor to determine the correct price at which to offer shares for sale or to bid for the purchase of shares, information regarding the nature of the bids and offers is essential. For this reason, the size and pricing of bids and offers on the exchange should be accurately reflected to market participants in a fair and equitable way. Computerized trading facilitates better record keeping so investors may study longer term trends.

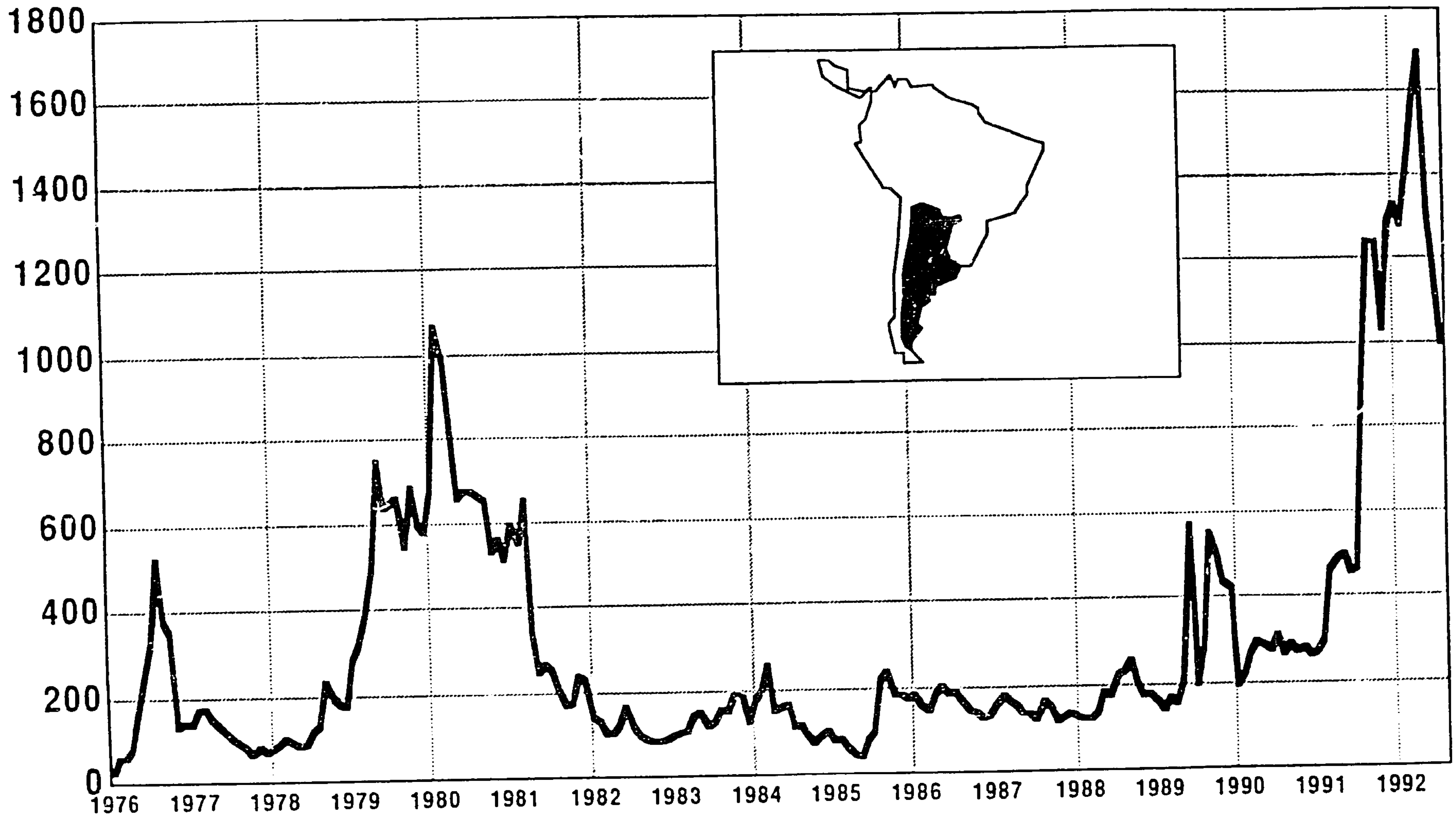
Company Information Disclosure: Perhaps the most essential and highly critical area for foreign investors, or any investor for that matter, is the area of company information disclosure. Many government officials in emerging markets around the world decry the gambling nature of stock market trading but it is no wonder that investors' behavior resembles gambling when they have no information on which to base their investment decisions. If government regulation had only one task, it would have to be to ensure that listed companies made full and fair disclosure of company information. Full disclosure means that all information relevant to business operations is made to investors so that they may make an intelligent and informed assessment of the firm's performance and prospects. Fair disclosure means that the information must be revealed to the entire market at the same time in the same degree, not only to a few insiders. It also means that auditors should be made responsible for preparing company accounts which are complete and detailed enough so that they fully reflect the operations, problems, risks and performance, as they have been experienced by the company.

Throughout the discussion, you may have noticed that I have not talked about government regulation of the stock market. This is not meant to diminish the importance of such regulation. It does have a role, but that role should be restricted to acting as a referee and not as a participant. For example, efforts by government regulators to fix fair prices to stocks is simply misdirected since it is the market which is better able to determine the fair prices. The market boosting measures now being applied by the governments in Korea and Japan are detrimental to fair and equitable capital markets. Such measures distort pricing and discourage rational investor decisions. Such efforts may benefit investors in the short term but in the long term they hamper a truly healthy capital market.

In conclusion, foreign investors' interests and desires are really not significantly different from the interests and desires of domestic investors. A fair, efficient, liquid and transparent market is in the interest of everyone and leads to a healthier economic environment in the emerging markets and throughout the world.

Argentina Index

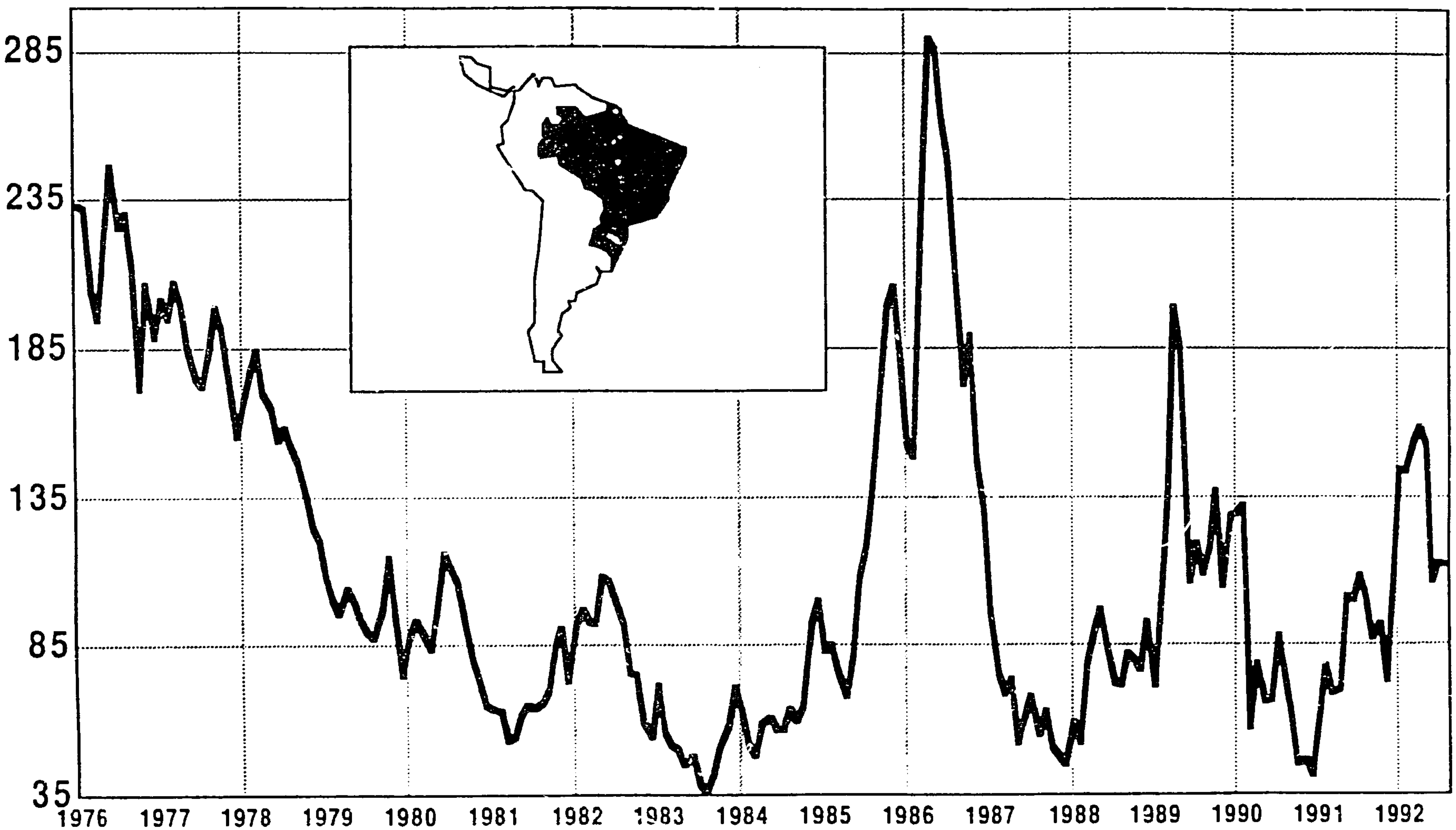
31 January 1976 to 31 August 1992 (US$)



Source: IFC

Brazil Index

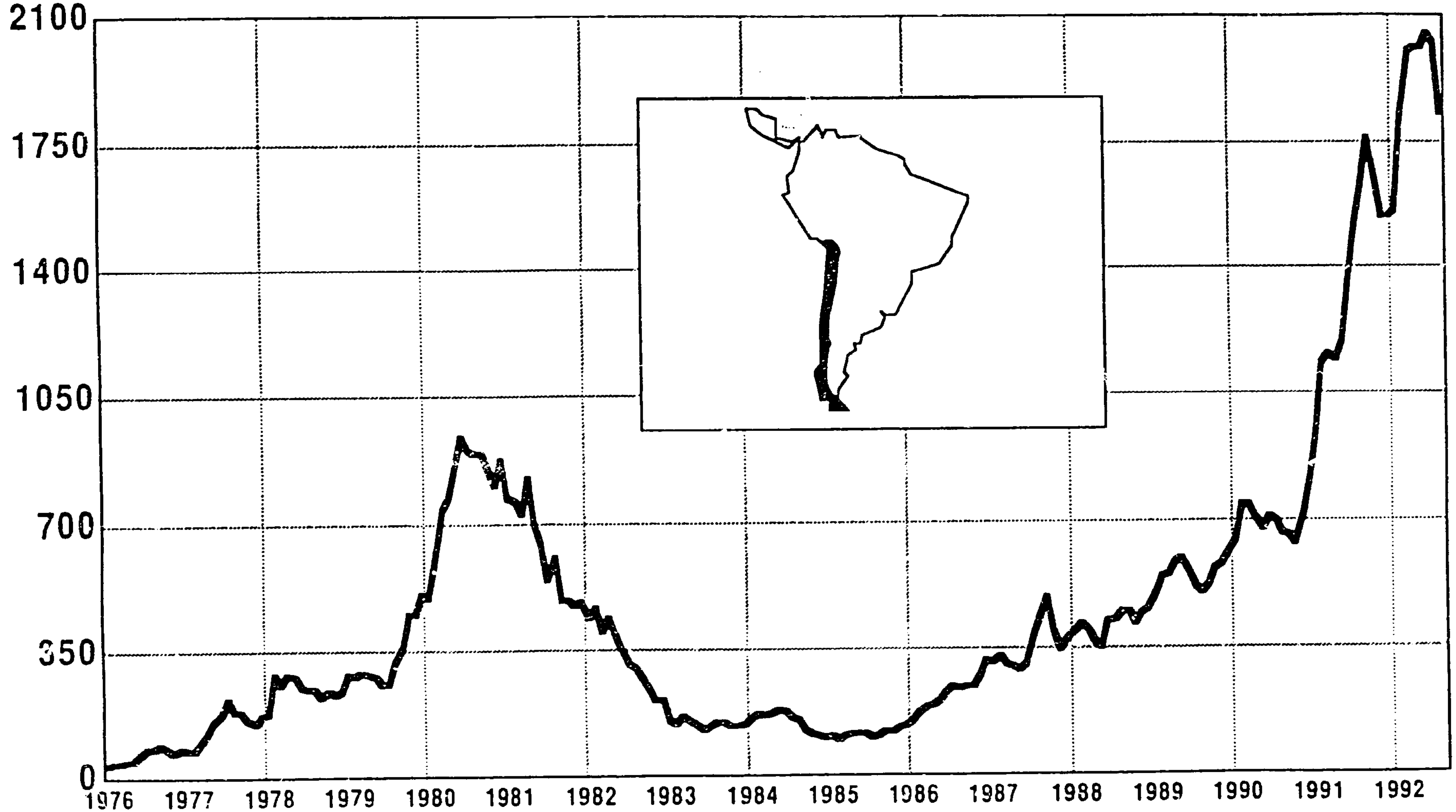
31 January 1976 to 31 August 1992 (US$)



Source: IFC

Chile Index

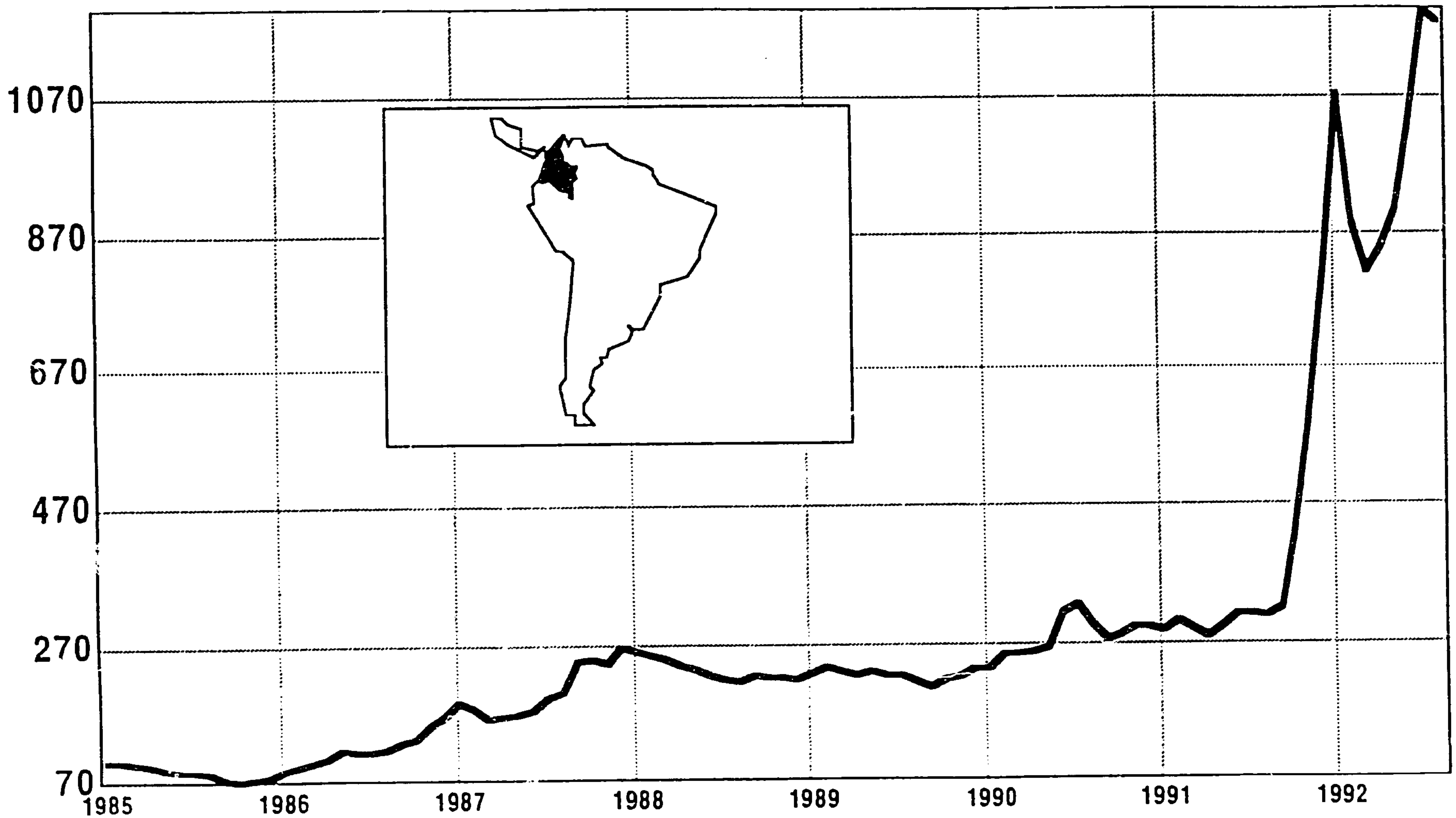
31 January 1976 to 31 August 1992 (US$)



Source: IFC

Colombia Index

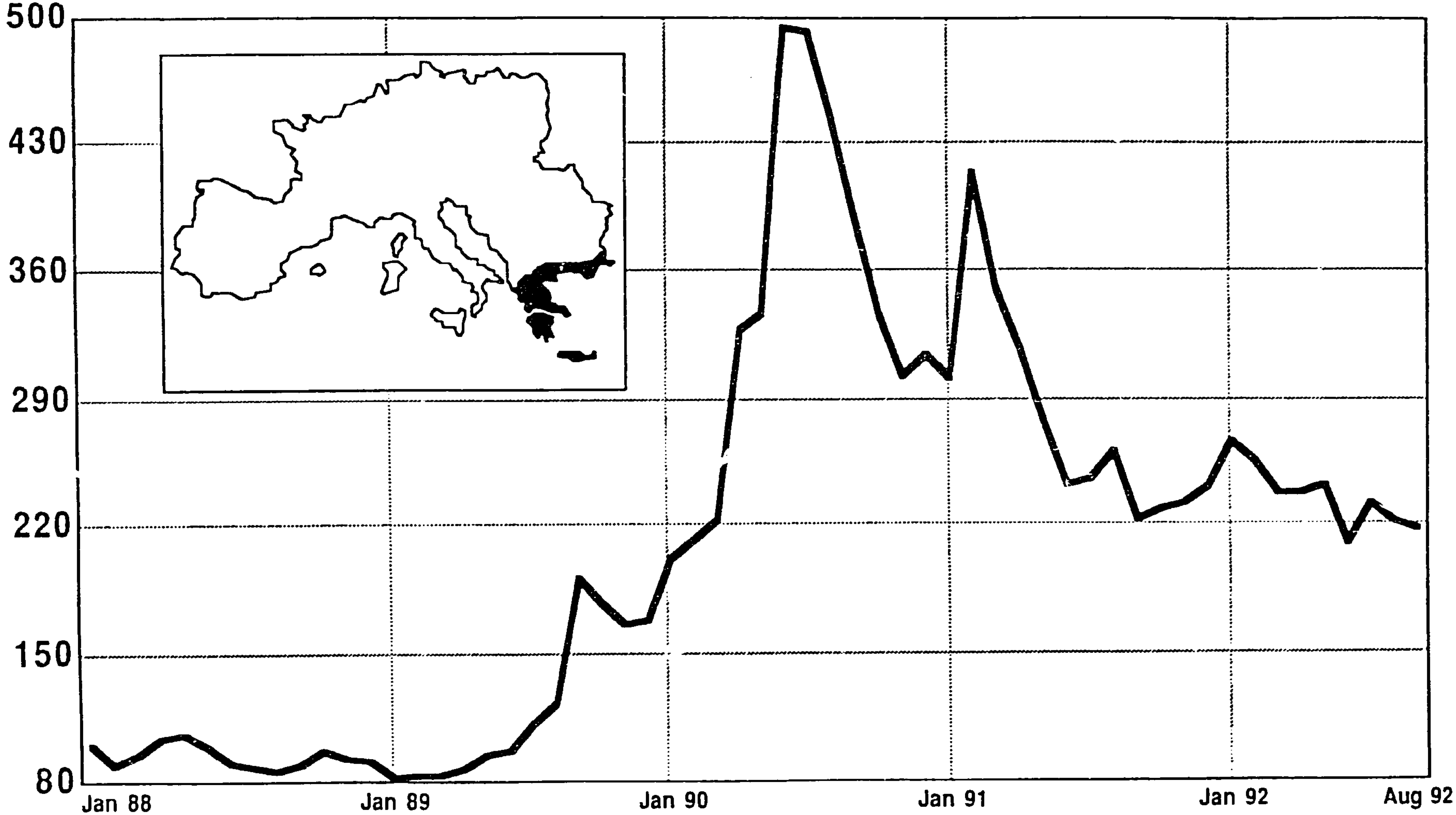
31 January 1985 to 31 August 1991 (US$)



Source: IFC

Greece Index

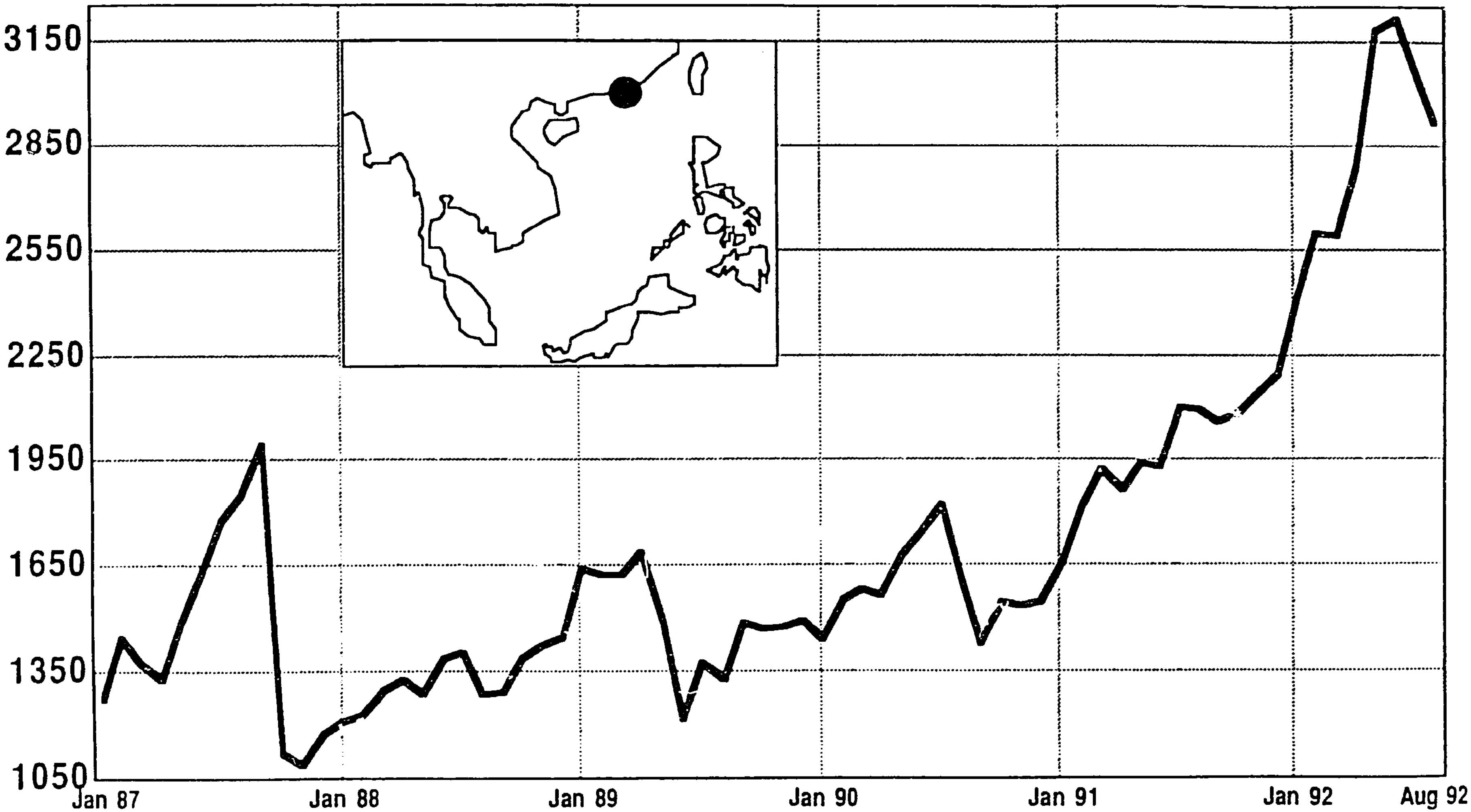
1 January 1988 to 31 August 1992 (US$)



Source: MSCI

Hong Kong Index

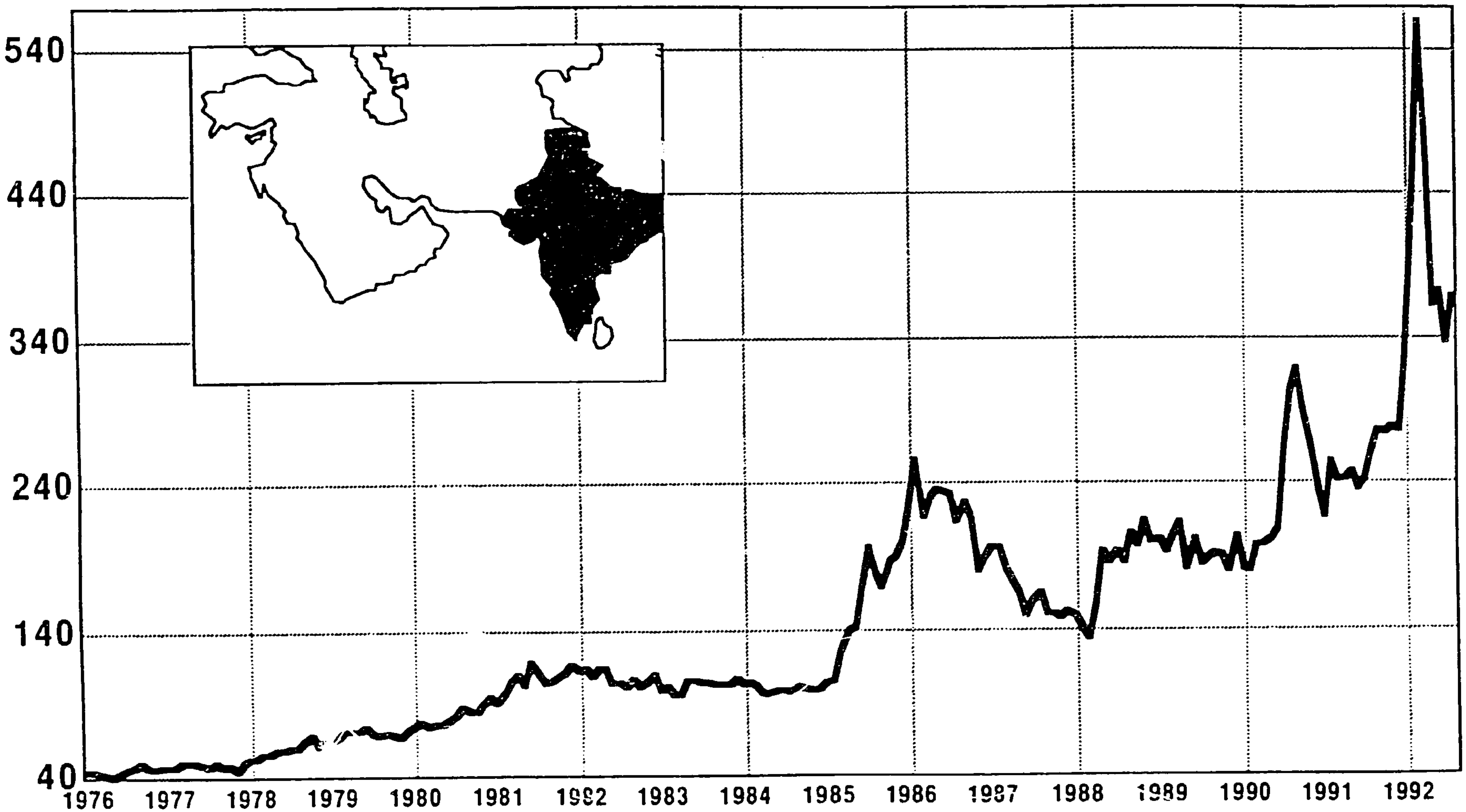
1 January 1987 to 31 August 1992 (US$)



Source: MSCI

India Index

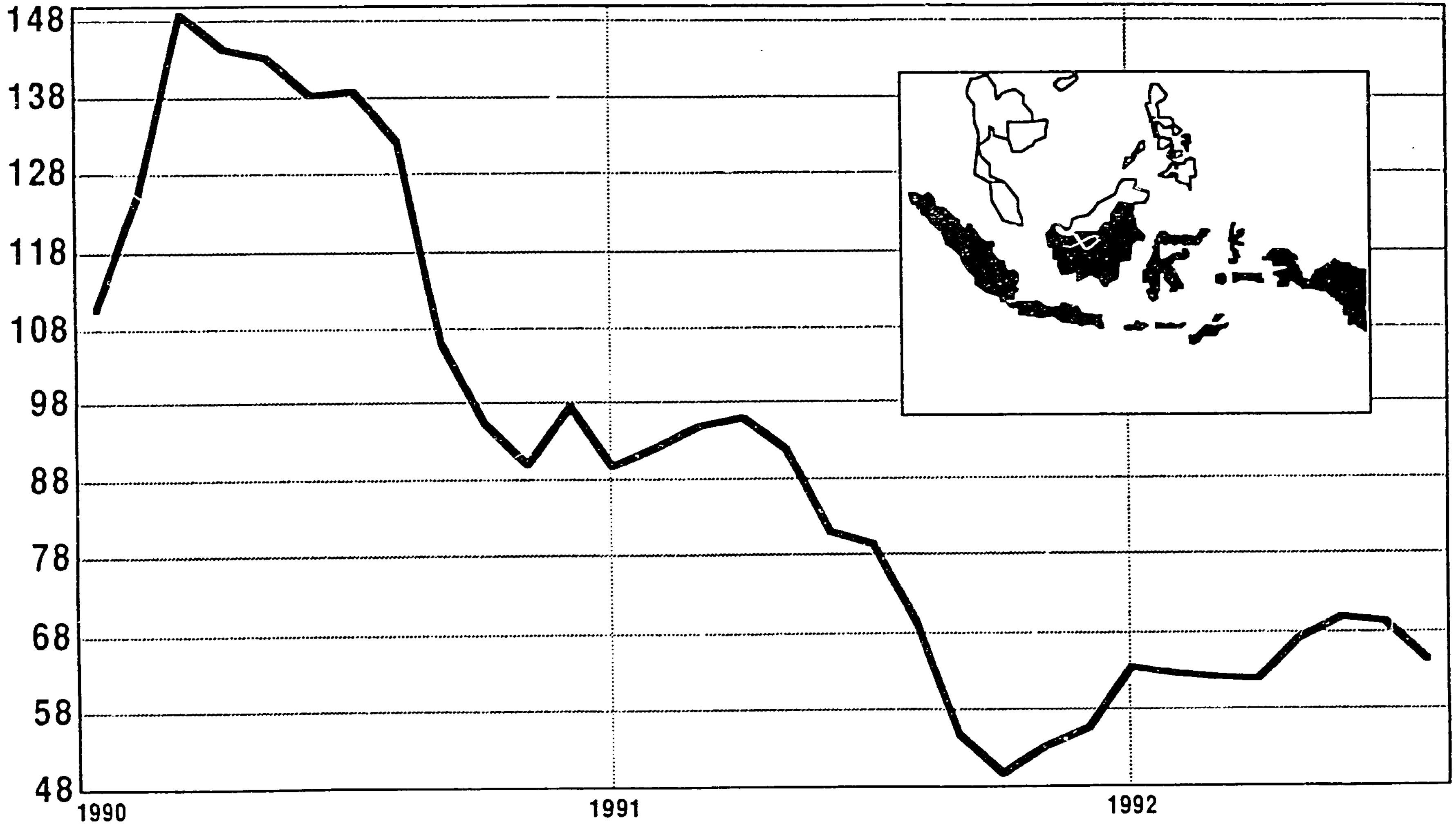
31 January 1976 to 31 August 1991 (US$)



Source: IFC

Indonesia Index

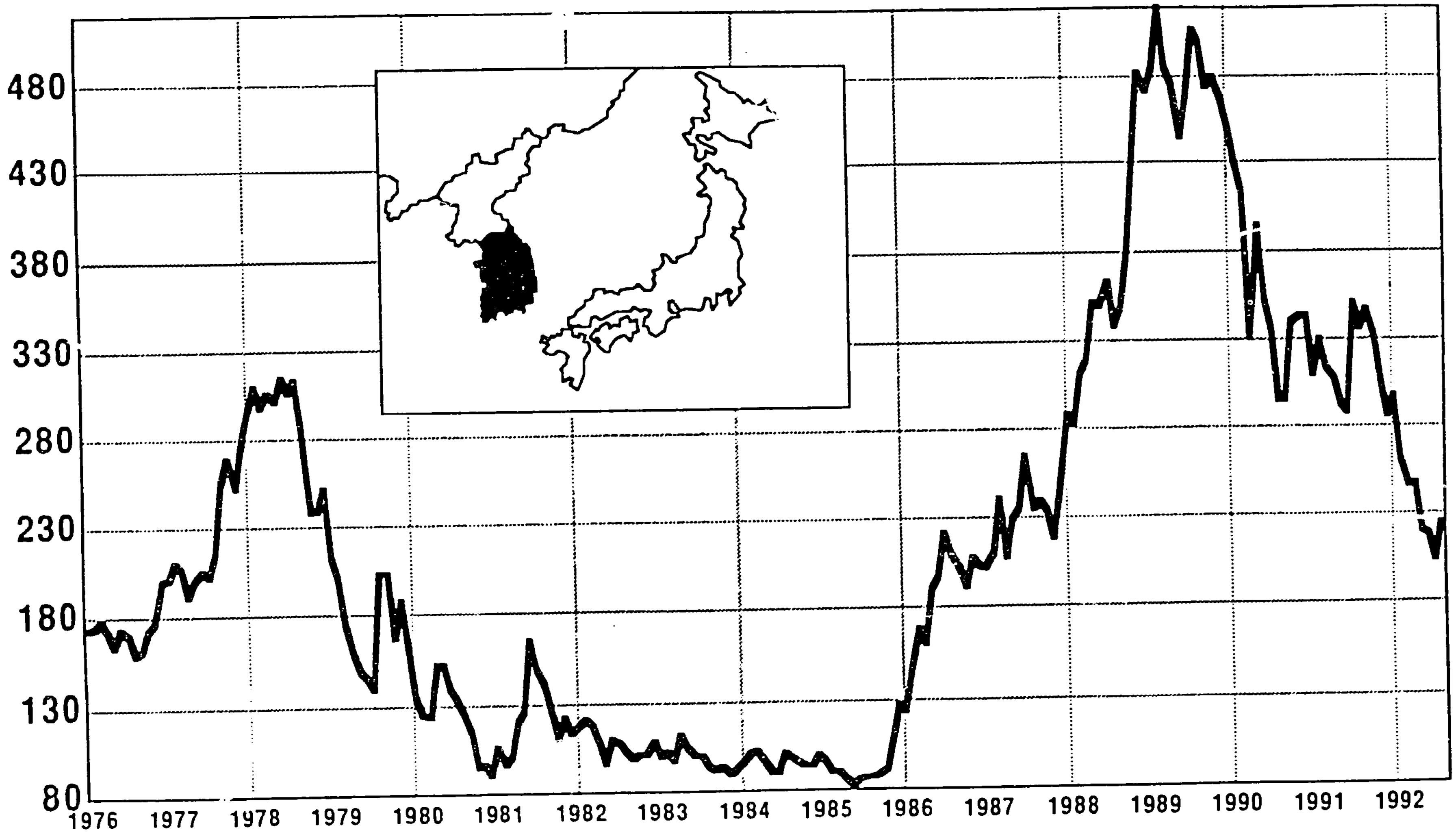
31 January 1990 to 31 August 1992 (US$)



Source: IFC

Korea Index

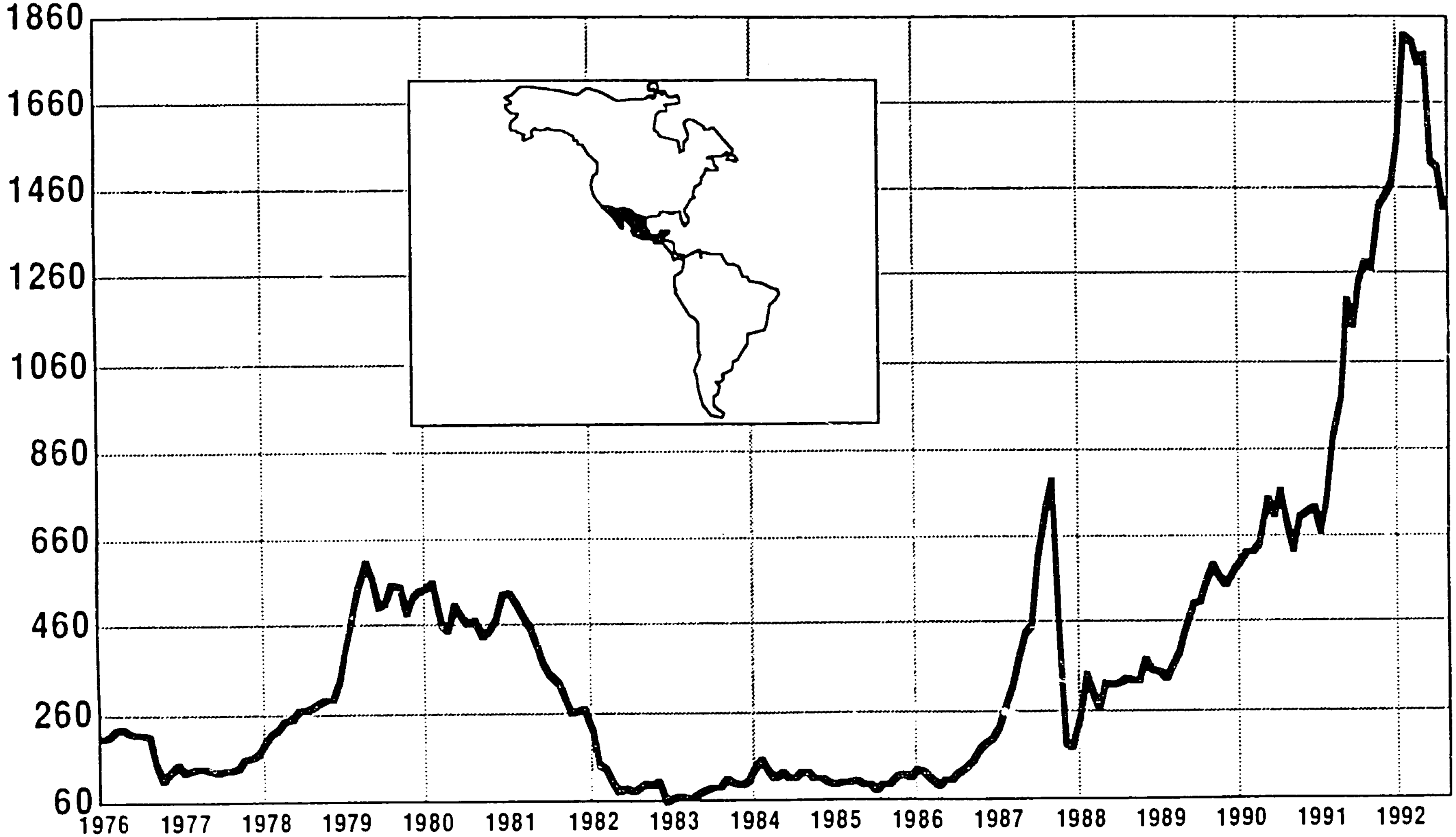
31 January 1976 to 31 August 1992 (US$)



Source: IFC

Mexico Index

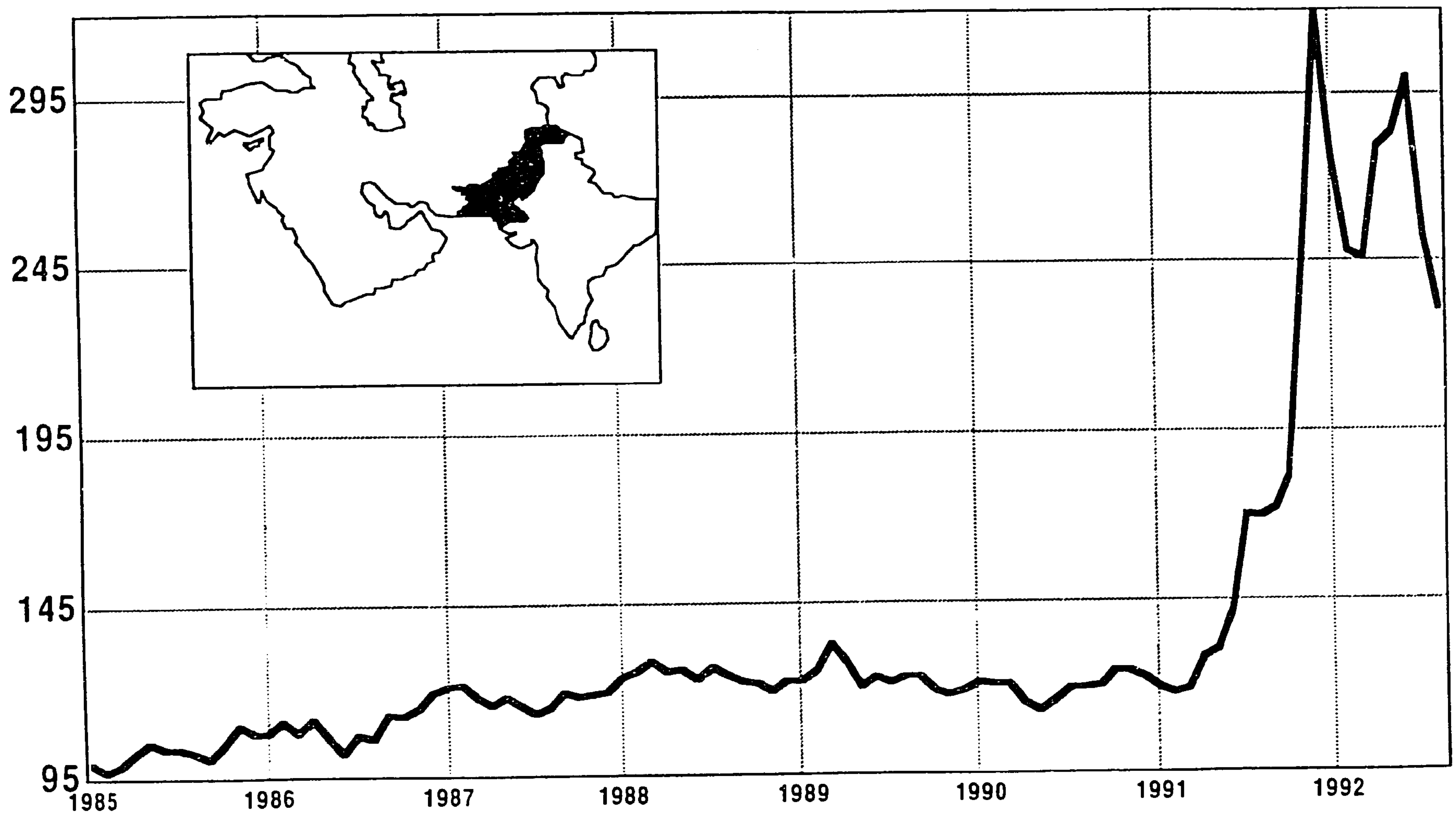
31 January 1976 to 31 August 1992 (US$)



Source: IFC

Pakistan Index

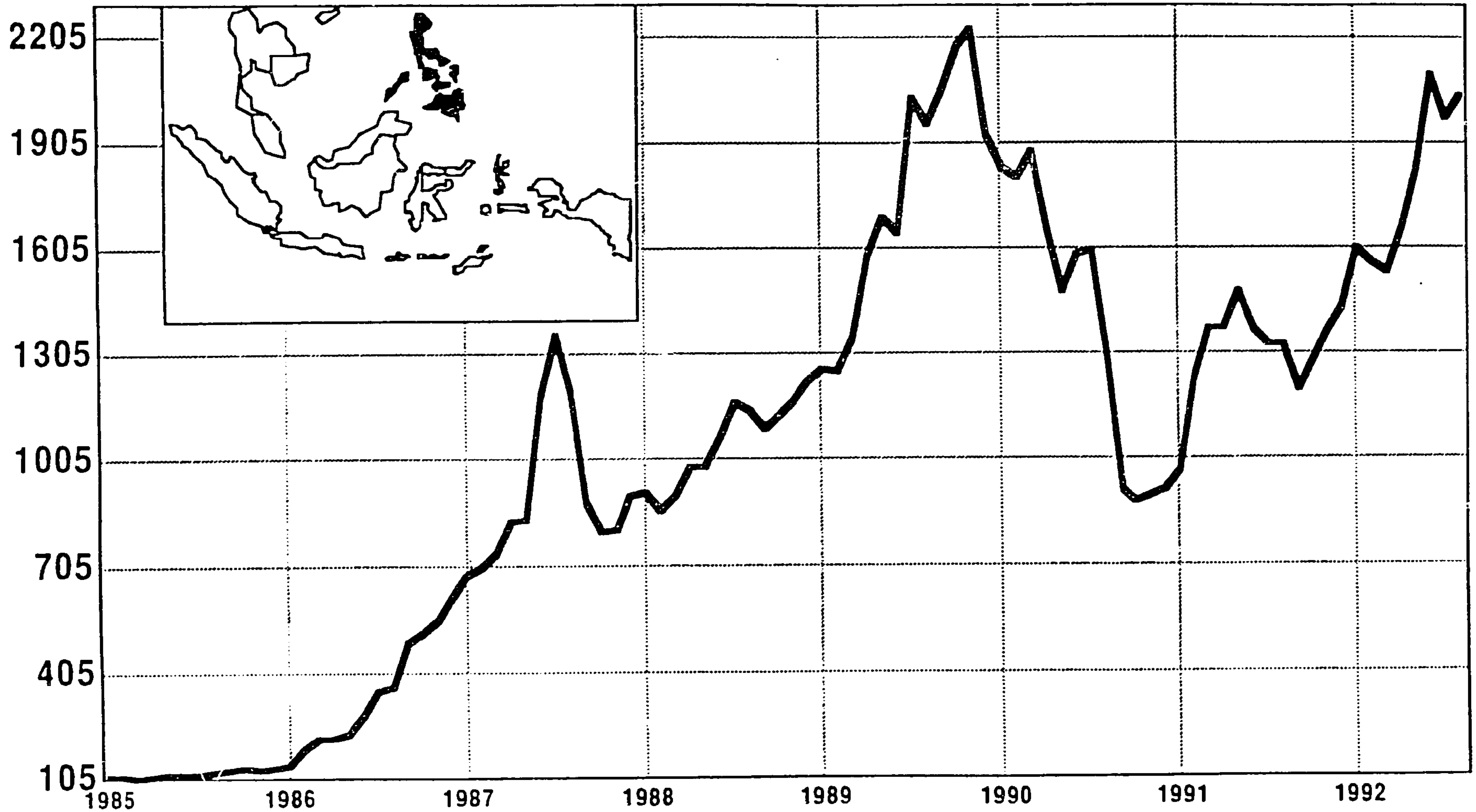
31 January 1985 to 31 August 1992 (US$)



Source: IFC

Philippines Index

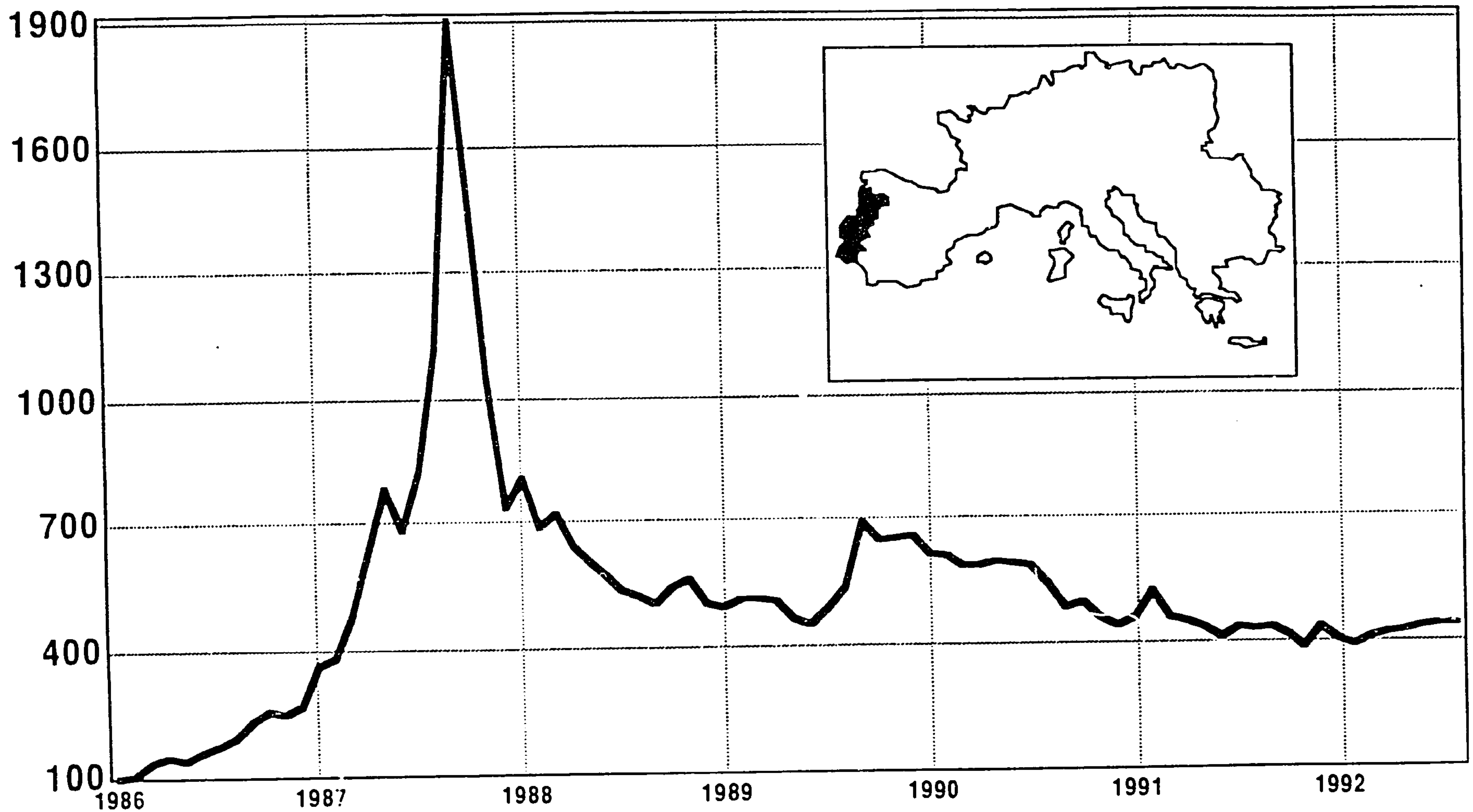
31 January 1985 to 31 August 1992 (US$)



Source: IFC

Portugal Index

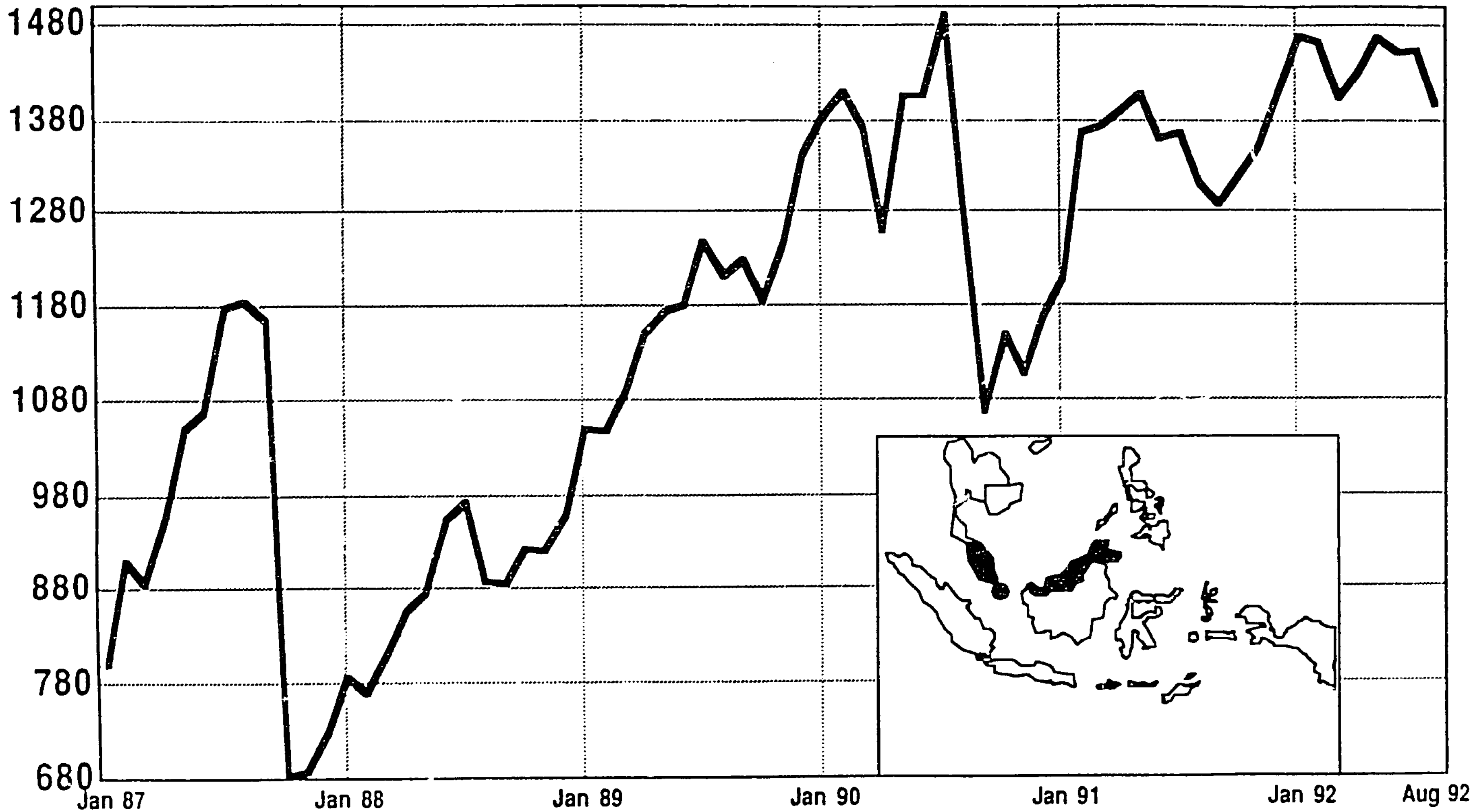
31 January 1986 to 31 August 1992 (US$)



Source: IFC

Singapore/Malaysia Index

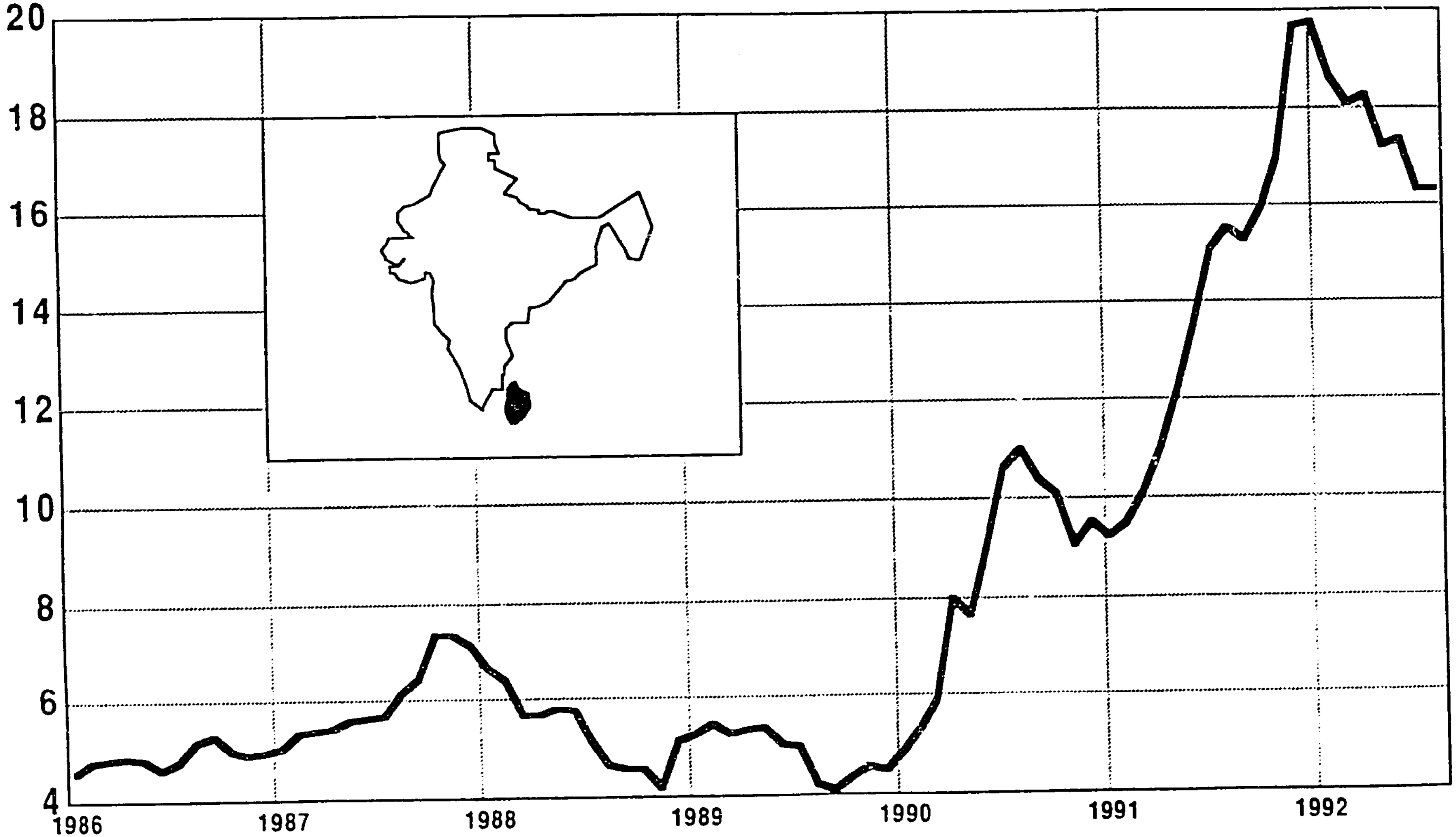
1 January 1987 to 31 August 92 (US$)



Source: MSCI

Sri Lanka Index

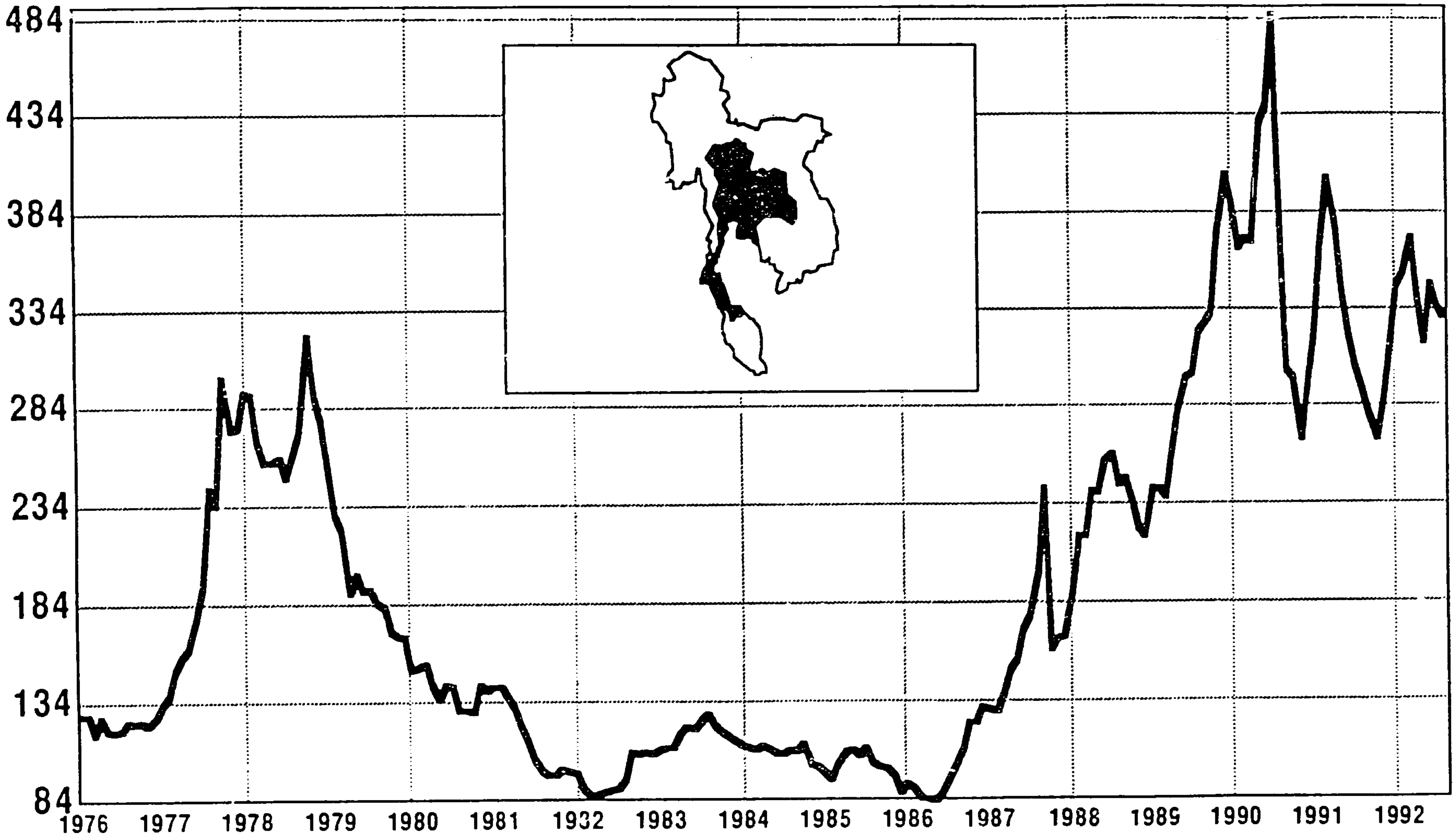
31 January 1986 to 31 August 1992 (US$)



Source: CSE

Thailand Index

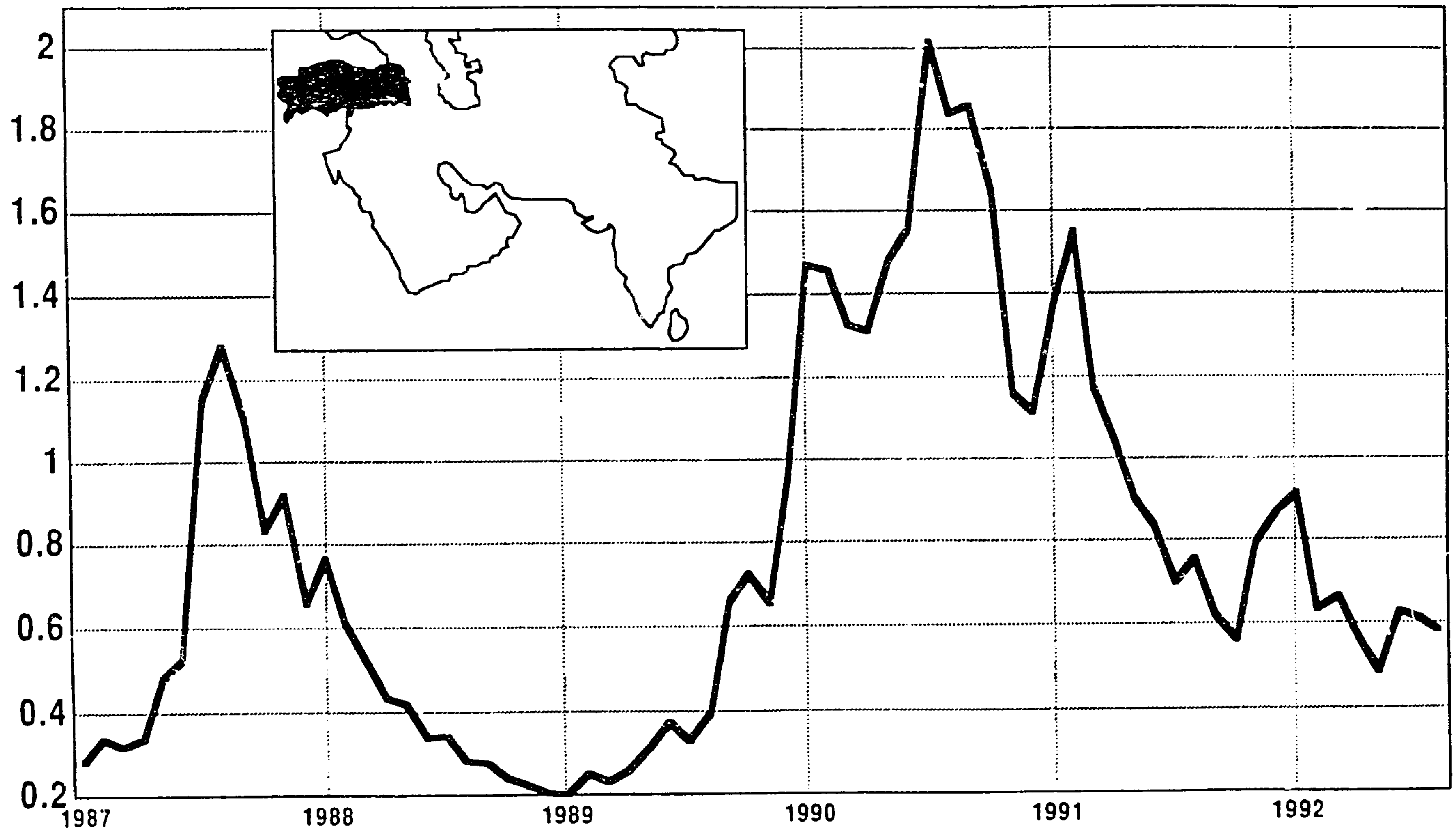
31 January 1976 to 31 August 1992 (US$)



Source: IFC

Turkey Index

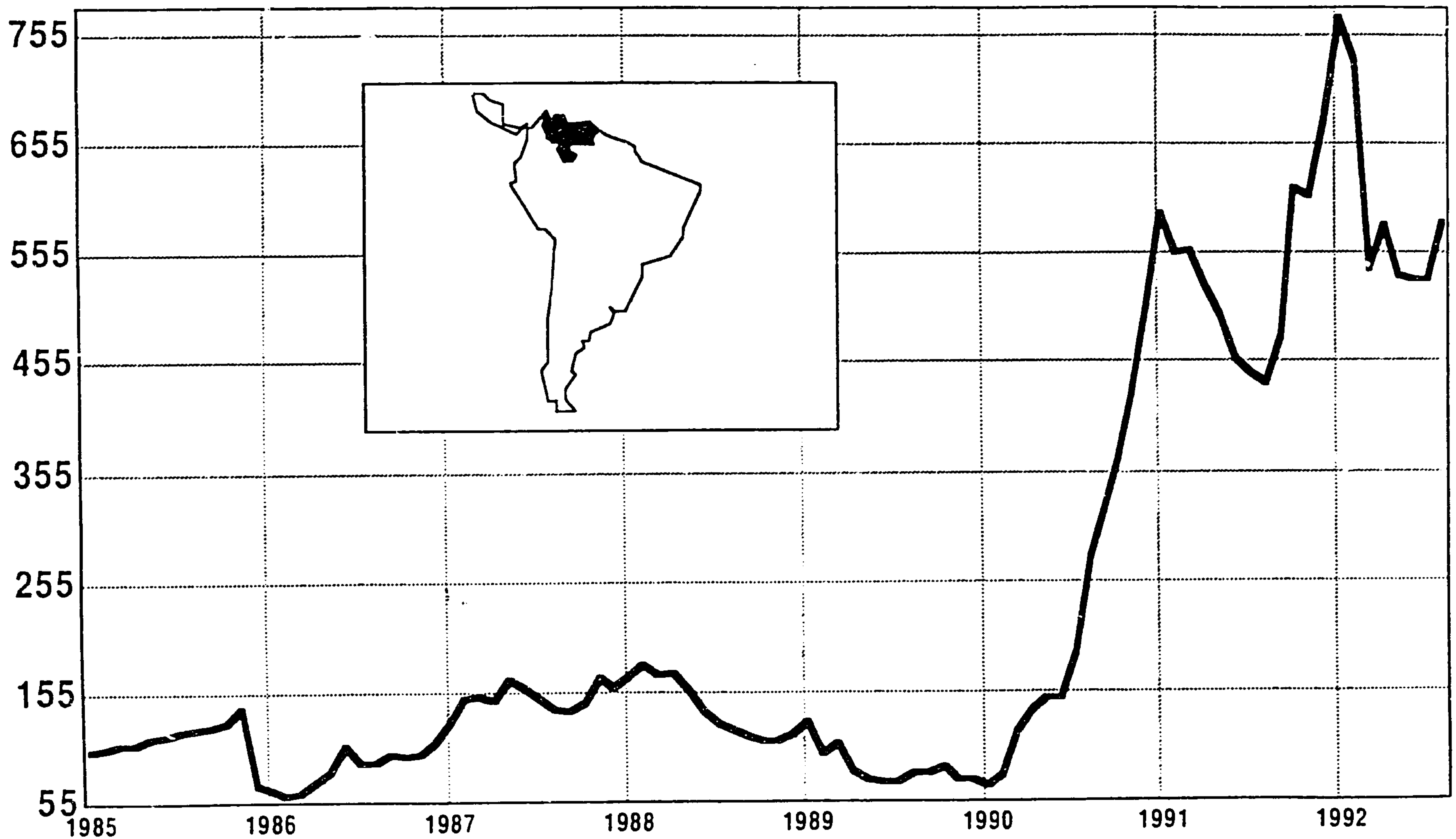
31 January 1987 to 31 August 1992 (US$)



Source: ISE

Venezuela Index

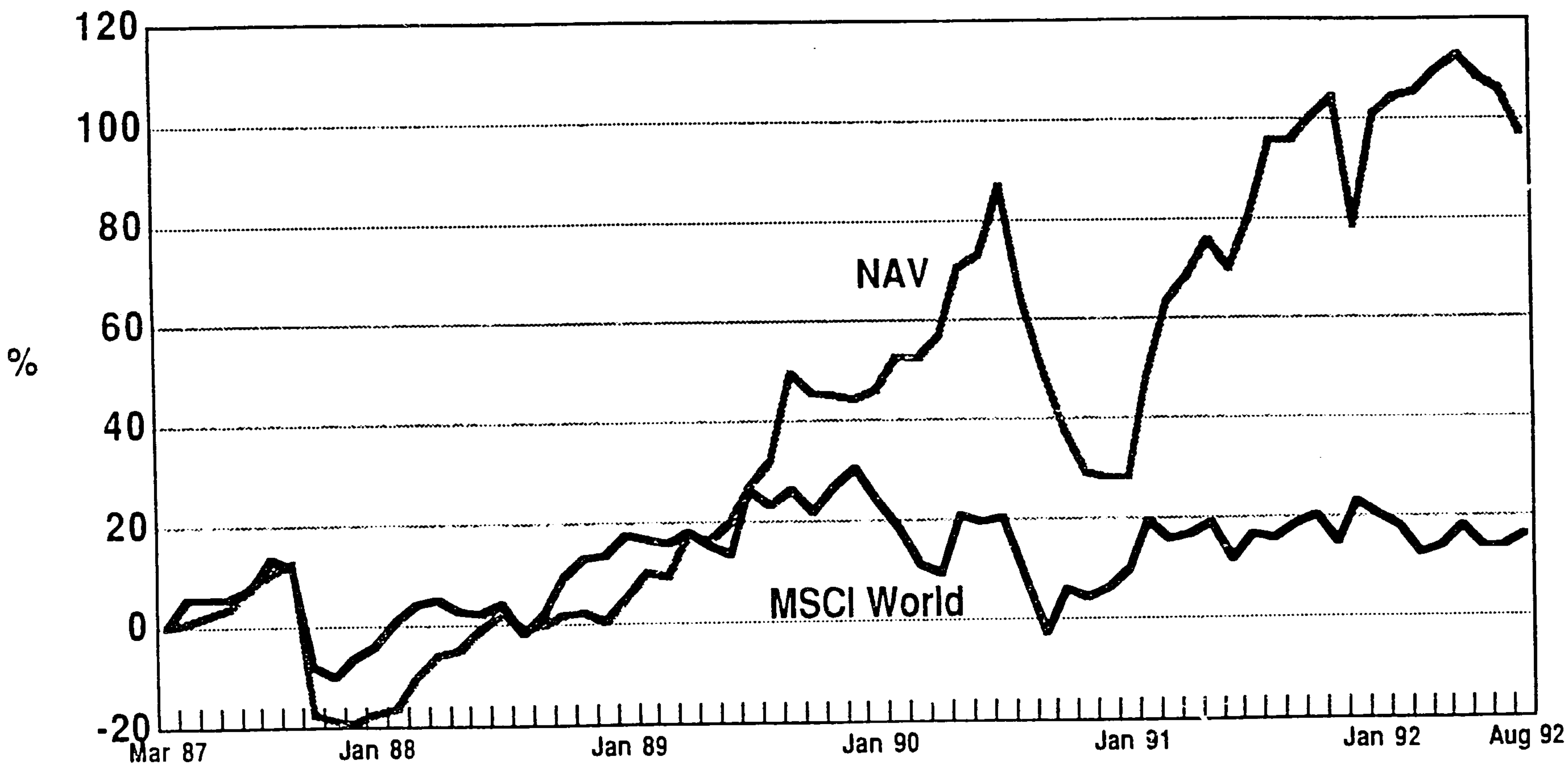
31 January 1985 to 31 August 1992 (US$)



Source: IFC

Templeton Emerging Markets Fund

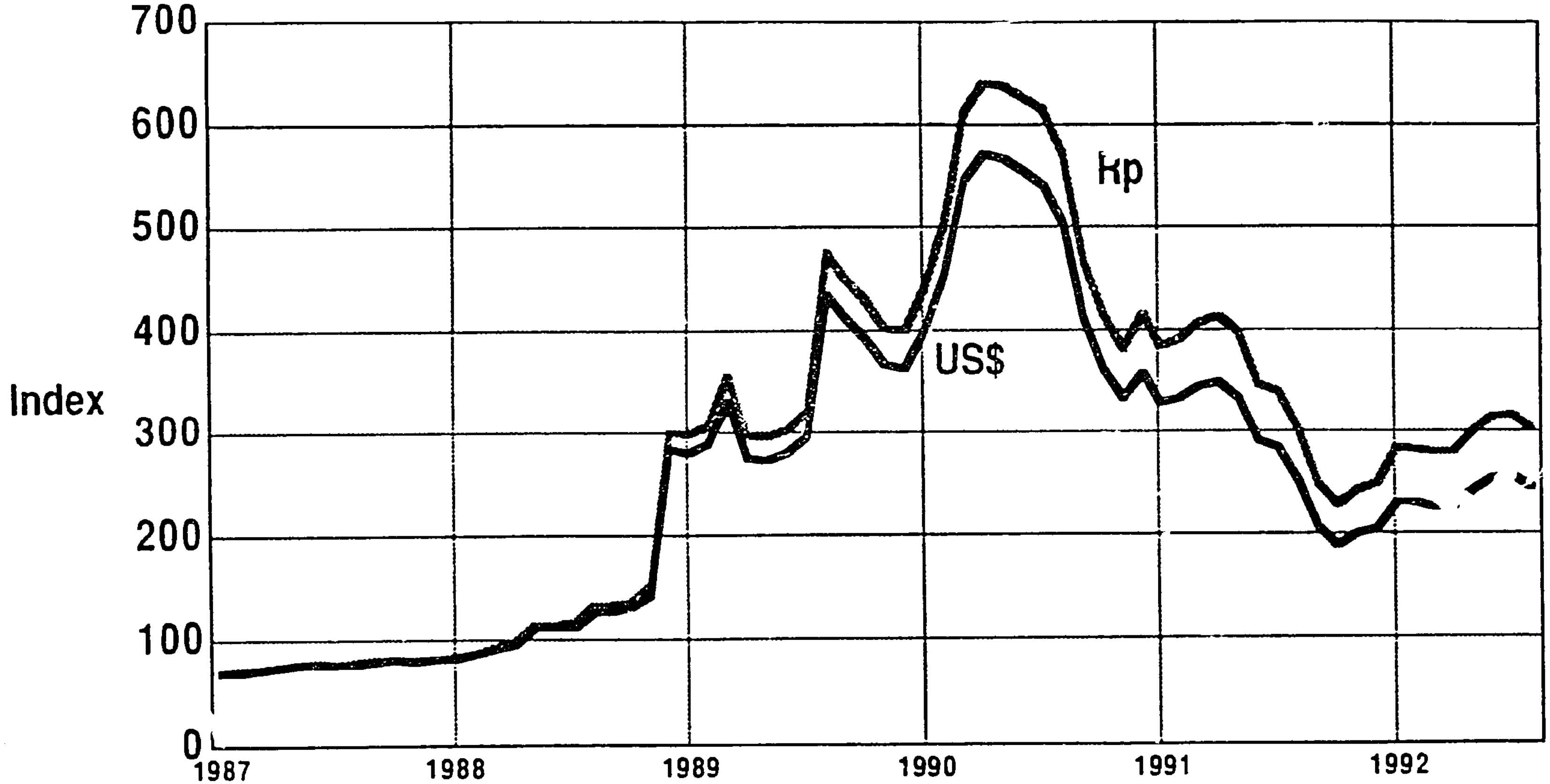
NAV vs MSCI World (% Change from 31 March 1987 to 28 August 1992)



TEMPLETON
INTERNATIONAL

Indonesia: Jakarta Stock Index (Rp & US$)

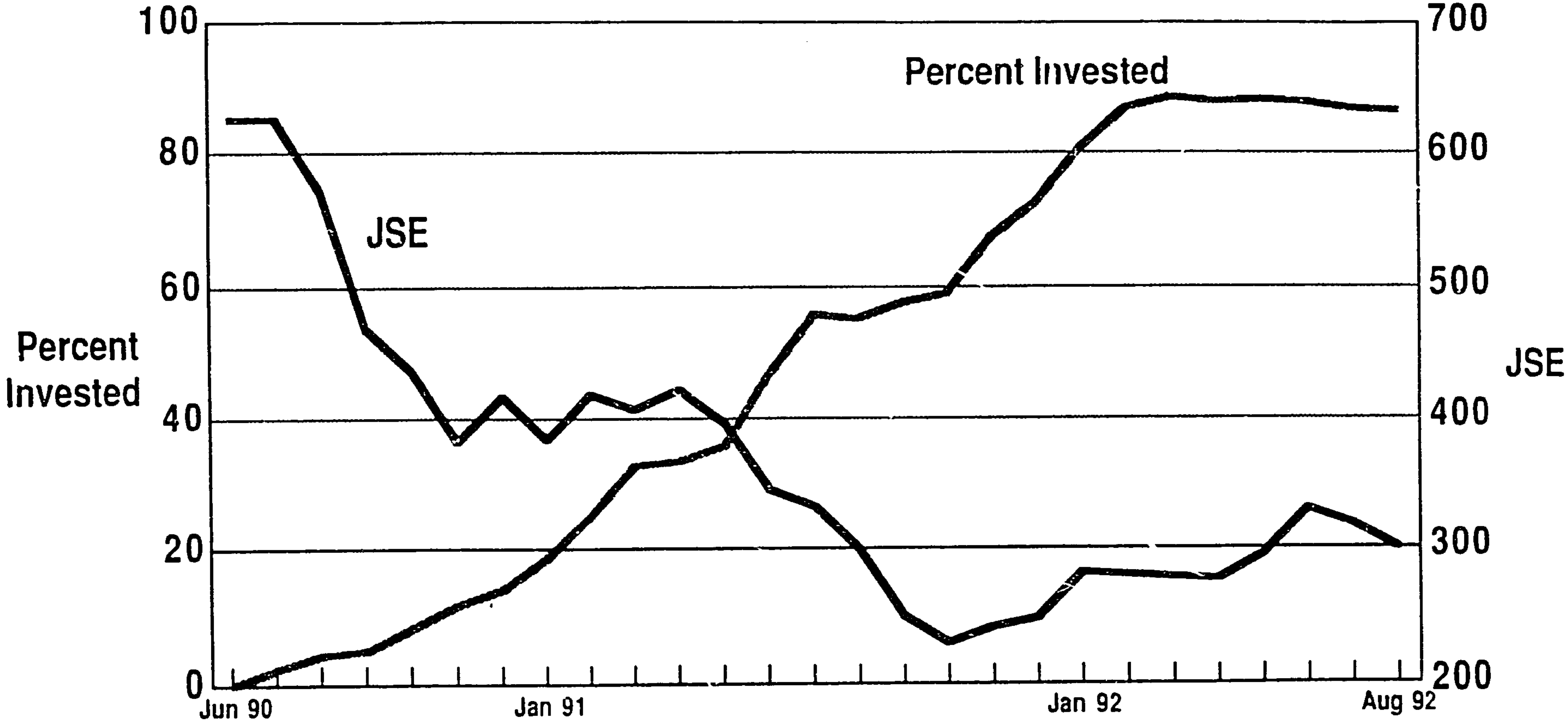
1 January 1987 – 31 August 1992



TEMPLETON
INTERNATIONAL

Indonesia: % of IDF Invested vs JSE

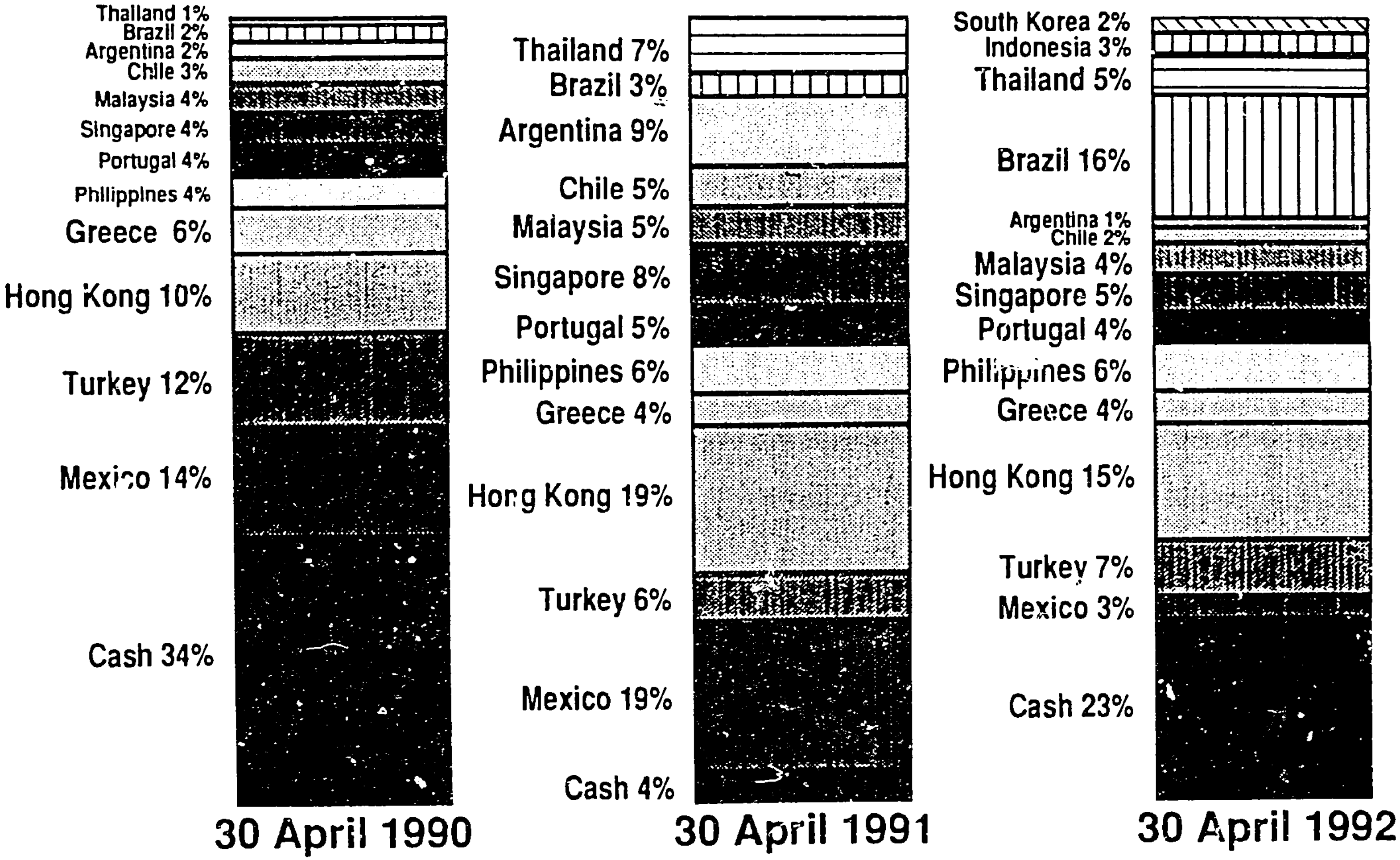
30 June 1990 – 31 August 1992



Source: Lipper Emerging Market Funds Service

TEMPLETON INTERNATIONAL

Templeton Emerging Markets Inv. Trust



TEMPLETON
INTERNATIONAL

AUTOMATED SECURITIES MARKET SYSTEMS – THE PATH TO THE FUTURE?

by

Bill Gorman
Consultant, Securities Trading, Settlement and Custody Systems

Regional Conference of Emerging Securities Markets of South and South East Asia

Automated Securities Market Systems- The path to the future?

October 2, 1992

Bill Gorman, Consultant
Securities Trading, Settlement and Custody Systems
Los Angeles CA; USA 1-213-661-8050

Gorman's Law
on Emerging Securities Markets

- Automation is essential to their Success.
  - Emerging markets seek to attract Global Investors.
  - Global Investors demand convenient, cheap, reliable, liquid and efficient markets.
  - Global Investors discount markets that do not meet their requirements.

- Automation is the only practical way of addressing these requirements.

Information Technology

- Will be a dominant force for change in the Capital Markets of the 1990's.
- Provides an effective, affordable means of addressing the needs of market participants.
- Exchanges should automate all functions not inconsistent with their Core.
- Surveillance should be built-in not added-on.

Why an Exchange?

- Attract investment capital
- Increase economic efficiency of investment
  - Liquidity & immediacy
  - Price discovery
- Protect investors
  - Information & regulation
- Distribute ownership

Ask yourself:

Why should issuers, investors and intermediaries come to your exchange?

Your answer should guide your automation efforts.

Financial Flows

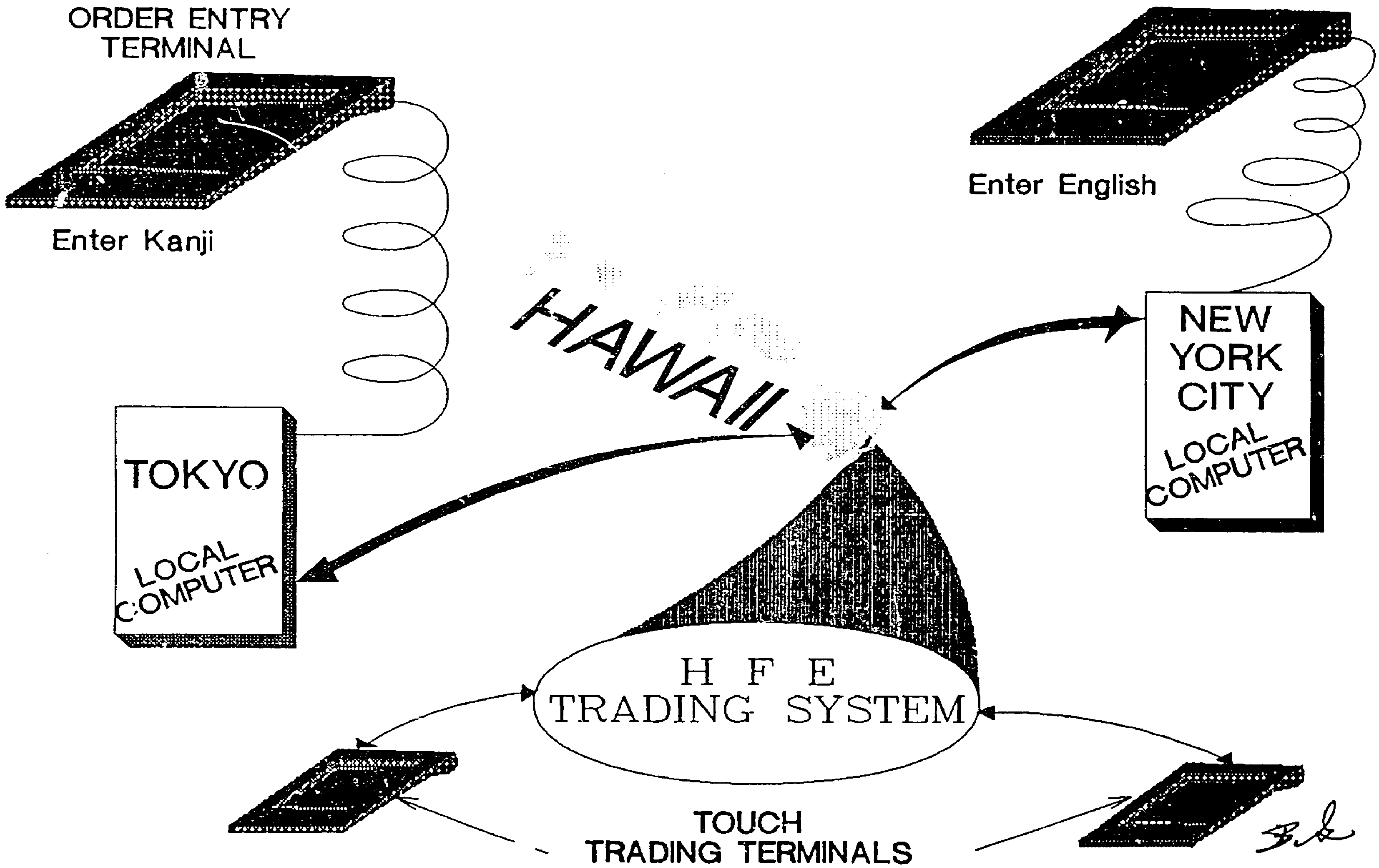
Cross-border equity flows to and from global stock markets have grown twenty-fold since 1979.

Financial flows will be a key catalyst for market developments.

New investors will invest globally and in large size. They will demand cheap, liquid and efficient trading systems that are better suited to their needs.

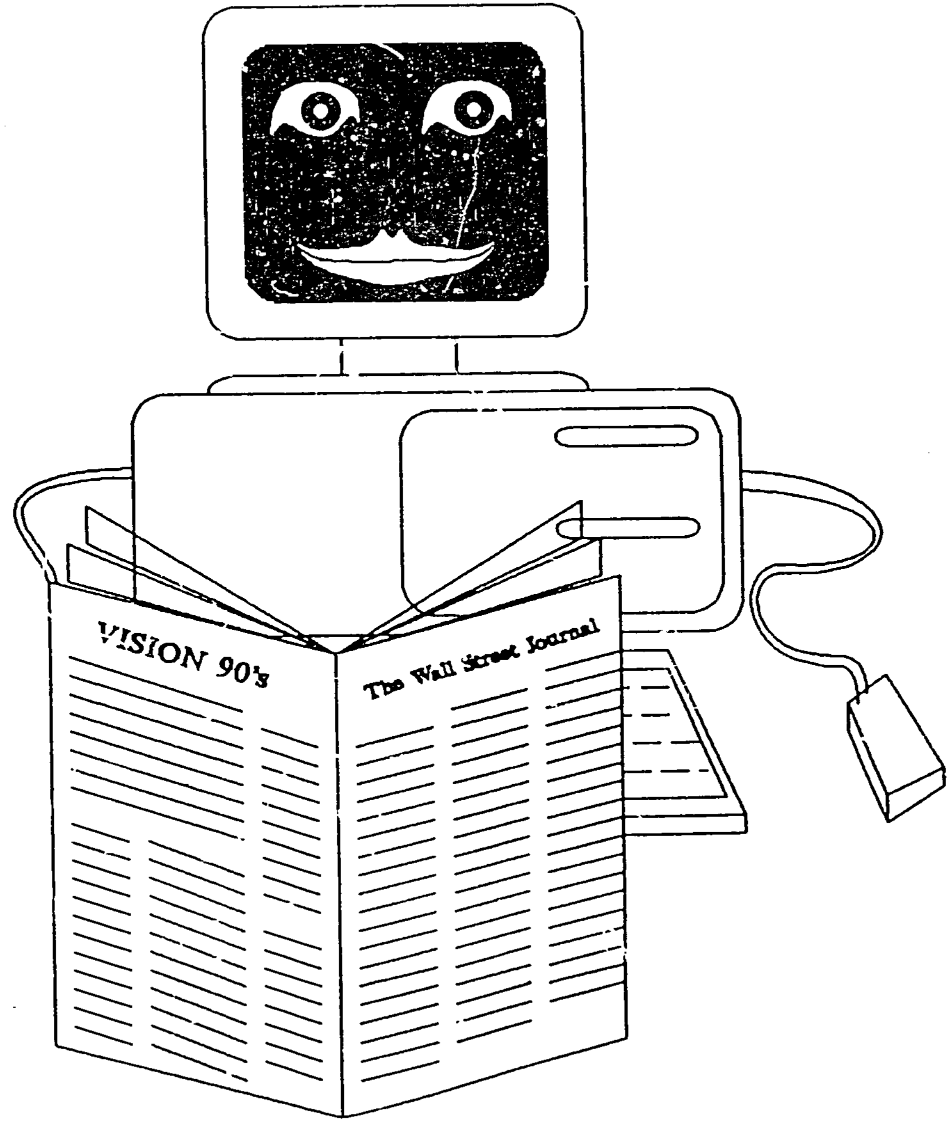
Salomon Brothers »International Equity Flows 1991'

OUR TRADING COMPUTERS WILL "INTERPRET" HANDWRITTEN CHARACTERS AND "TRANSLATE" TRADE INSTRUCTIONS



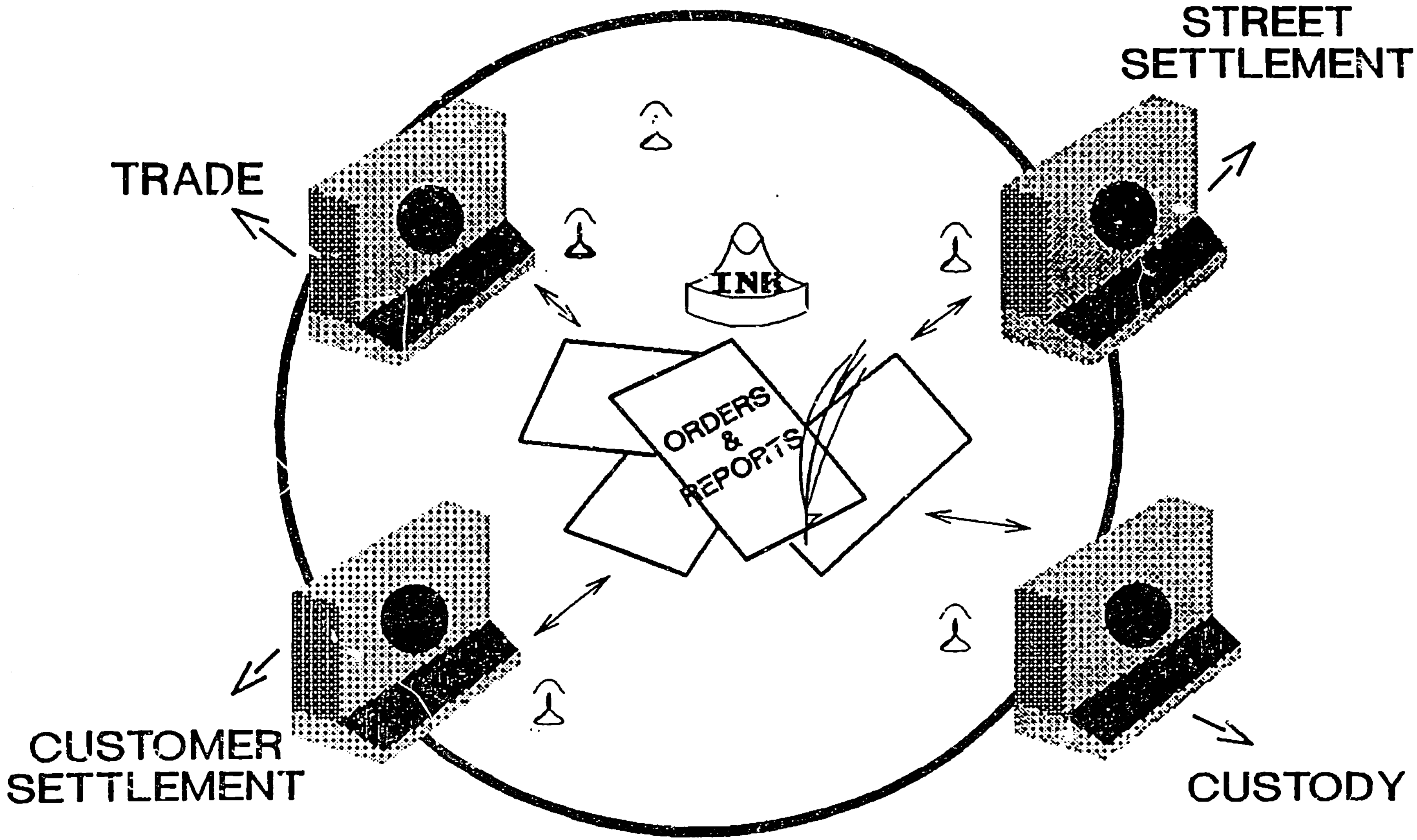
FUTURE NEWSPAPER DATA DELIVERY

NEWSPAPER
STOCKTABLES
WILL HAVE MACHINE
READABLE CONTENT
WITH PRE-INDEXING
CAPABILITIES



TODAYS MARKETS

EXPERIENCE EXCESSIVE MANUAL PROCESSING & RE-KEYING



TOMORROWS MARKETS MUST INTEGRATE THESE PROCESSES

Create a Regional Ticker

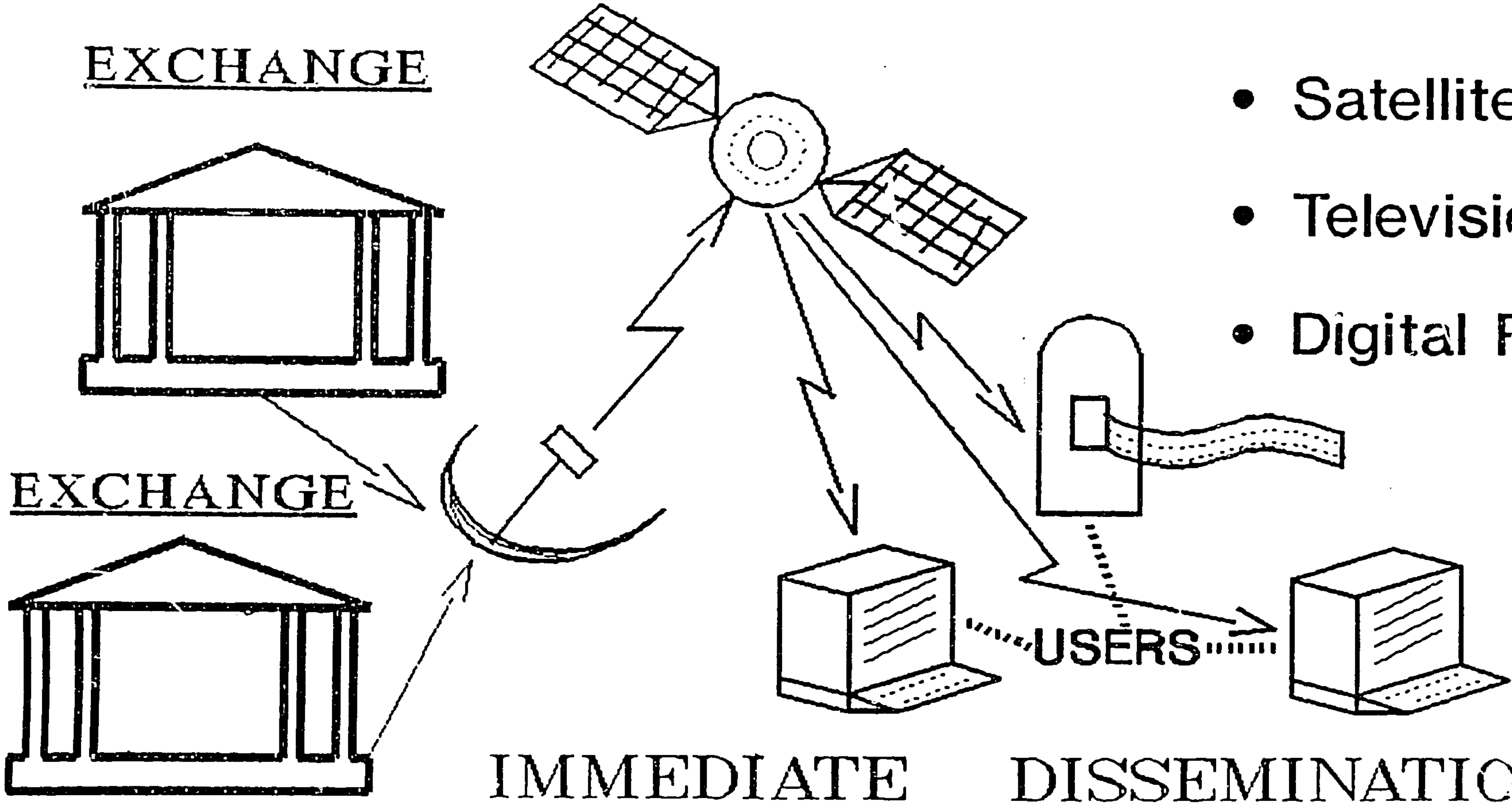
- Provides Economies of Scale.
  - Simplifies Data Vendor Access.
  - Lowers Communications Costs.
- Enhances Visibility of Participating Markets.
- Provides Greater Revenue Possibilities.

Make the Ticker World-Class

Increase its value by including:

- Real-time Trades, Quotes & Indices
- Equities, Bonds, Options, Futures & Commodities
- Scrolling News & Headlines
- Corporate Actions - Dividends, etc.
- Research Opinions
- History Retrieval

Affordable Ticker Technologies



- Satellite
- Television (VB
- Digital Radio

IMMEDIATE DISSEMINATION
OF
LAST SALE and QUOTE DATA

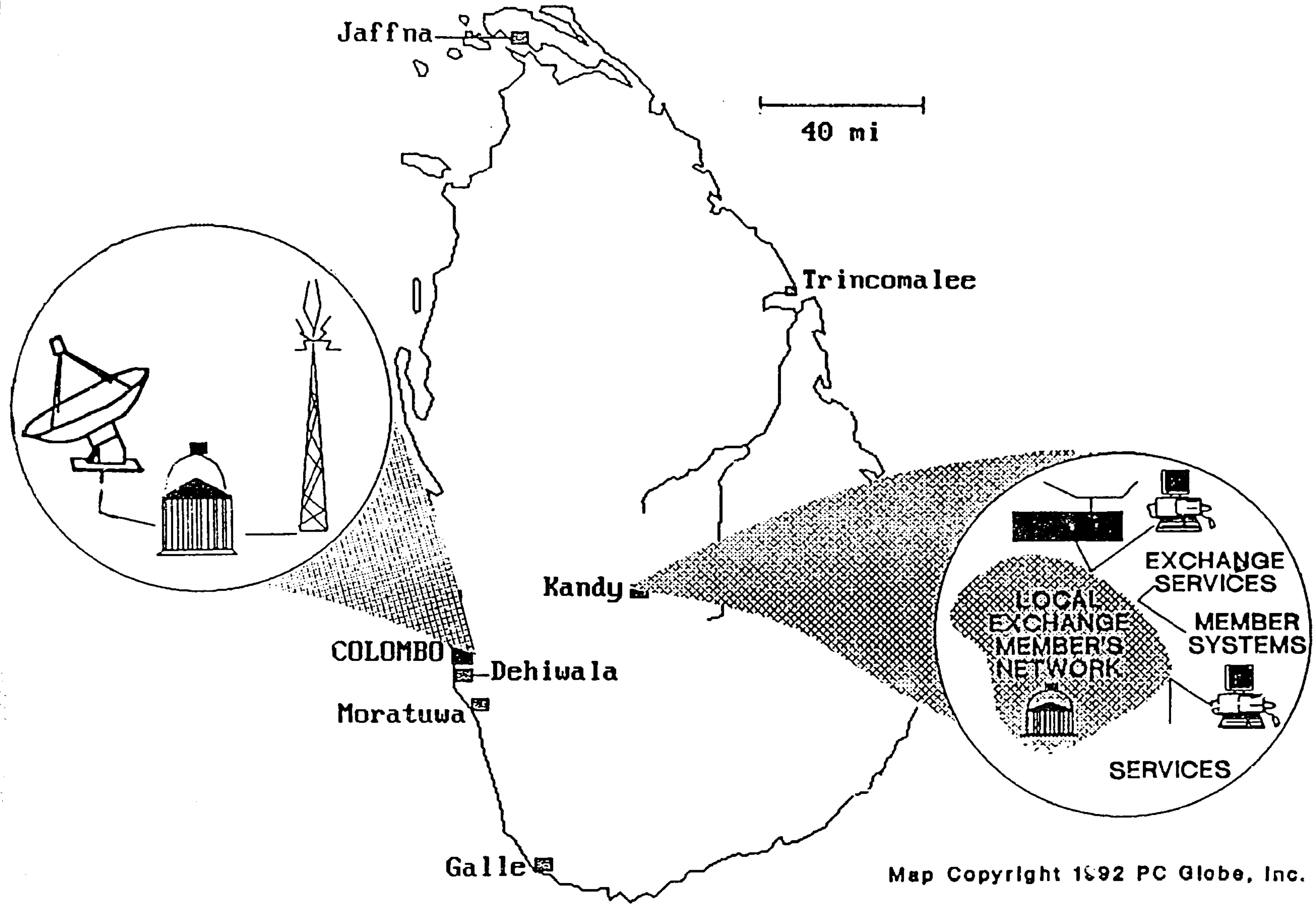
HIGH SPEED TICKER BROADCASTS

- 1200 to 9600 Baud Binary Synchronous Transmissions
- Fixed Format ASCII Text
- Quote & Tick Data
- Includes Security Symbol, Price, Size and Market I.D.
- Does Not Include Time or Buyer/Seller I.D.
- Messages are Sequenced Numbered

T NCR USG.SLD

$4_{S}\ 26\frac{3}{4}$ $60\frac{1}{2}$ $38\frac{1}{4}$

Create a Member Support System



Automate Settlement & Custody

- Harmonize on Rules and Procedure.
- Observe International Standards
  - ISO, ISSA, FIBV, G-30, etc.
- Build-in Security and Anti-Fraud Provisions.

FIBV

FÉDÉRATION INTERNATIONALE DES BOURSES DE VALEURS

Recommendations

- Adoption of International Settlement Conventions
- Cross-Border Settlement Links
- Securities Immobilized in the Country of the Issuer and transferred by Book Entry
- Listings Abroad in Original Form

Group of Thirty
Recommendations

- Trade comparison by T+1.
- Positive affirmation of institutional trades.
- Central securities depository.
- Research benefits of a trade netting system.
- Delivery versus payment (DVP).
- Same-day funds payments.
- T+3 rolling settlement.
- Securities lending and borrowing
- ISO standards.

Address Customer Settlement Needs

- Capture customer data at trade time.
- Provide an Electronic Confirmation capability.
- Enable Institutional Traders to Affirm trades.
- Develop automated custodian interfaces.
- Use the ISO standard for securities message formats (# 7775).
- Use the ISIN numbering system for securities issues (ISO #6166).

Strengthen your Custodian Links

- Provide your Custodians with direct tele-communications links.
  - example: SWIFT, International VANs, local direct links, etc.
- Provide status inquiry services.
- Develop a full range of services to Custodians, including the processing of corporate actions.

Create Specialized Networks

- To build a World-Class Exchange requires a First-Class Communications Infrastructure.
  - Most emerging markets lack access to such capabilities.
  - In many cases, market activity is confined to the big cities.
- Affordable technologies exist that enable Exchanges to overcome communications deficiencies.

Insist on Strong Registrar Links

- Promote rapid turnaround of deposits and withdrawals.
- Insist on immediate identification of lost, stolen and forged certificates.
- Develop a means of regularly synchronizing the Depository's and the Registrars' records.

Build-in Auditability

- Provide a continuous audit capability.
- Maintain a continuous transaction history.
- Enable the reconstruction of the system and its data base at any time.
- Maintain history on non-erasable media.

Save Through Sharing

- Share Development with Other Exchanges
- Harmonize on Rules & Procedures
- Adopt ISO Standards
- Share Basic Specifications & Designs
- Exchange Software with Other Exchanges
- Build Common Generic Systems

Seek Strategic Alliances

Having Mutual Benefits

- Seek Partners who gain from an Alliance
  - Brokers
  - Vendors
  - Custodians
  - Other Exchanges & Depositories
  - Trans-National Clearing Agencies
- Other Sources of Assistance
  - International Agencies
  - FIBV, ISSA, IOSCO
- Retain an appropriate Level of Control

When Sub-Contracting

Remember the KISS Principle.

- Build in small, clearly defined segments.
  - Use short-term contracts with reopeners.
  - Establish well-defined deliverables that perform useful functions and are easily recognized when completed.
  - Establish razor-sharp milestones.

- Actively monitor progress.
  - Cross-train staff in securities processing and data processing.
  - Use staff to guide and monitor contractors.

I Propose that the Securities Markets
of South and South East Asia
form a Federation
Whose Function is to
Develop Systems of Common Interest.

Bill Gorman - 2 Oct 1992

SECTION 2

COUNTRY PAPERS PRESENTED

RECENT DEVELOPMENTS IN THE INDIAN CAPITAL MARKETS

by

C.B. Bhave
Head of the Secondary Market Department
Securities and Exchange Board of India

\(?.)

It is at once a pleasure and a privilege to be addressing an important gathering like this and to have the opportunity of exchanging ideas with you on the recent developments in the Indian capital markets. To understand these recent developments, it is necessary to have an overview of the evolution of the capital market in India since independence. Although India has a long history of capital market institutions before the eighties, Indian capital market saw subdued activity.

Given the economic environment, namely the fact that interest rates on most of the financial instruments were administered by Government, it is not very surprising that the major instruments for channelling household savings were deposits with banks, the post office, units of the Unit Trust of India, contributions to provident funds, insurance premia and national savings certificates. The funds raised by the private sector through issue of equity, debentures or other similar instruments, were less important than the public sector government administered channels. One also needs to keep in mind here that a major portion of the banks and financial institutions are in the public sector in India. The industrial sector was also dominated by the public sector. It follows that the public sector was the major user of funds.

While the public sector used Rs. 220 billion[1] of the funds flowing from the household and the external sector the share of the private corporate sector was about Rs. 70 billion (1985-86). The channelling of funds to the public sector was achieved largely through the imposition of statutory liquidity/investment restrictions. If the captive funds raised by Government from banks and other financial institutions are excluded from calculations, the volume of funds channelled to the public and private corporate sector appears to be in the range of Rs. 120 to Rs. 160 billion. Of this, roughly Rs. 70 billion were utilised by the private sector and the rest by the public sector.

Even though the Indian economy turned out impressive savings rates, the financialisation of household savings (gross) was in the range of 6-8 percent of personal disposable income in the major part of the seventies. The eighties saw the same rates climb to a level of 11-14 percent. The steady change in the structure of household savings in favour of financial assets provided the market with an increasing stream of investible funds.

As the Government liberalised the economy, a gradual but definite shift toward greater reliance on the market and lesser dependence on government-directed flow of funds has been witnessed. It was during the eighties that the corporate sector started tapping investible funds directly from the investors in a substantial measure. The funds disbursed by the financial institutions rose from a level of Rs. 20 billion in 1980 to nearly Rs. 80 billion in 1989-90. During the same period funds raised from the capital market went up from about Rs. 1 billion to nearly Rs. 50 billion, indicating a clear shift toward disintermediation.

The developments on the stock exchanges during this period were no less remarkable. The turnover on stock exchanges, another indication of investor interest in the capital market, was Rs. 1 billion in 1980-81 and Rs. 29 billion in 1989-90. It increased to Rs. 710 billion at the height of its activity in 1991-92. The decade of the eighties thus saw a qualitative change. The corporate sector and the markets had developed the ability to raise resources directly from the market.

During this time the economy grew at an average rate of 5.6 percent. The savings rate continued to be in the range of 17 to 20 percent. Thus the growth in the primary market and the stock exchanges

[1] Note: 1 U.S. dollar ($) is equivalent to about 30 Indian Rupees (Rs.).

outpaced the growth of the economy. The capital markets in the country were beginning to come into their own.

Another important development in the latter part of the eighties was the growth of mutual funds. From 1964 to 1987 there was only one institution operating in the country in the area of collective investment schemes, the Unit Trust of India. Because of the legal framework and the history of its evolution, the UTI is not merely a collective investment scheme in the sense that such institutions are understood normally. The UTI also acts as a financial institution. Its role is thus mixed. It uses funds collected from the public not only for their deployment in the financial market but also for its activities as a financial institution financing projects. The Unit Trust of India accounted for 5.2 percent of the savings of the household sector in the financial assets in 1990-91. The investible funds with UTI increased tenfold from about Rs. 32 billion to about Rs. 300 billion between 1985-86 to 1991-92. The mutual funds industry, excluding UTI, made its beginnings only in 1987. From an amount of Rs. 1.3 billion collected in the initial year, it has reached a level of Rs. 30 billion collected in 1991-92. Today there are seven mutual funds operating 23 schemes, all floated by public sector banks and public sector insurance companies. Government's announcement of opening up this field to the private sector has generated an enthusiastic response from the private sector.

The Indian economy passed through a critical phase in the years 1990-91 and 1991-92. The years saw a decline in the growth rates of the economy from 5.6 percent to 2.5 percent. The Gulf war and the following balance of payments crises created the need for drastic measures to put the economy back on the path of progress. Government's initiatives in liberalisation of the economy, loosening of controls on foreign trade, dealings in foreign currency, and the expectation of financial sector reform was greeted by the market enthusiastically.

The secondary markets in the country saw hectic activity in the period July 1991 to April 1992. The National index rose from 660 to 1800, a jump of nearly three fold. The market capitalisation went up more than Rs. 2000 billion. The budget announcements on February 28, 1992, saw the market climb to dizzying heights. This was welcomed by and large in all quarters and considered a very positive development.

There were, however, some features about this phenomenal rise in the index that raised serious questions about the sustainability of such developments. The rise was based on thin trading. It was not backed up by growth in the economy — in fact the economy was going through a process of adjustment and experienced among the lowest rates of growth in a decade. The price earnings ratio had climbed to levels upwards of 50.

It was clear that the rise, even though explained by the optimistic expectations from an economy undergoing large doses of liberalisation, was taking place against fundamentals and was based on relatively thin trading. The crash came in the month of April 1992 and, following the discovery of some large scale irregularities in the banking sector with inter-related transactions in the capital markets, the stock markets nose dived. The index fell from 1880 in April to 1155 by August 1992. It appears now that the markets are coming to terms with the rapid developments that engulfed them in April to June 1992.

The growing size and depth of the capital market and the increased activity have raised questions relating to efficiency, transparency, and stability of the system and its ability to protect the investors. These issues are of crucial importance if the process of financialisation of household savings is to continue and the efficient channelling of these funds to the capital markets is to be achieved.

The Government was aware of this need and created in 1988 a non-statutory body called the Securities and Exchange Board of India for development and regulation of the capital markets, with its focus on investor protection. SEBI was given its legal status in April 1992, when the necessary legislation was passed by the Parliament. SEBI is expected to play the role of developing the capital markets in the country through effective regulation. In this connection the following initiatives have been taken by the Government and SEBI in the past year.

The Government of India abolished the Capital Control Issues Act in May 1992. Any issuer intending to issue equity or loan instruments needed a consent from the Government of India under the Act and under the power to give consent, matters relating to pricing, duration and yield were controlled by the Government. This has been replaced by guidelines lifting control on pricing and yield. The issuer now needs to get the issue documents cleared from SEBI and the focus of examination of such documents is on adequate disclosures for investor protection.

Government has delegated powers to the SEBI for regulation of stock exchanges. An ambitious programme of stock exchange reforms involving shorter trading cycles, efficient settlement systems, mechanisms for investor protection, stricter enforcement of market discipline and greater transparency for trade operations has been taken up. The success of these measures will go a long way in consolidating the achievements of the eighties.

India has had no statute or regulation to curb insider trading. The Securities and Exchange Board of India has recently asked all the major players in the market to evolve an internal code of conduct and institute a mechanism of checks and balances to prevent insider trading. The regulations governing the prohibition of insider trading activities are likely to be notified soon.

The increase in the volume of trading and the deepening of markets have exposed the inadequacies of the system in handling transfer of securities. The government of India is actively considering the question of immobilisation and dematerialisation of securities to enable faster settlements and to reduce systemic risks. Considering India's sheer size and the dispersed nature of holdings it is expected that a gradual approach would be preferred by the Government in tackling these issues.

Government has recently announced its intention to open the Indian capital markets for investment by foreign institutional investors. It is expected that apart from bringing in net flows of foreign exchange, this measure will provide healthy competition to domestic investors and would enhance the liquidity of the market.

To sum up, Indian capital markets have seen remarkable growth in the last decade. The challenge before us today is to reform our structure and systems to handle these large volumes, to ensure efficiency of transactions, and to enhance investor confidence in the system to sustain the growth witnessed in the past.

Note: *The views expressed in this paper represent neither the views of Government of India nor the views of the Securities and Exchange Board of India. These are personal views of the author.*

DEVELOPMENT OF THE INDIAN SECURITIES MARKET

by

G.B. Desai
President of the Bombay Stock Exchange

Presented by

W.M.R. Mayya
Executive Director of the Bombay Stock Exchange

96

India is one of the largest countries in Asia and has the second largest population in the world. We also have one of the oldest cultures and civilisations in the world starting from Mohenjodaro and Harappa, dating hundreds of centuries back. And we have a long tradition of trading in securities in India. Nearly 200 years ago securities trading was known, but the first stock exchange was established in 1875 in Bombay. It is, in fact, the oldest stock exchange in Asia. The establishment of stock exchanges gradually spread to other Indian cities like Ahmedabad, Calcutta, Madras, etc. In 1956, when the first all-India legislation regulating stock exchanges was introduced, there were eight recognised stock exchanges in the country. For nearly two decades thereafter, the number remained largely unchanged. The 1980s, however, saw the birth of a number of newly recognised stock exchanges in the country. There are at present 21 recognised stock exchanges spread as far as Ludhiana in the north, Cochin in the south, Gailhati in the east, and Rajkot in the west, as well as the OTC Exchange of India. Although the number of stock exchanges could increase in the near future, there would likely be a trend toward contraction of these markets into more compact and broader ones with better communication facilities.

The Indian stock markets have grown so sharply in the last 10 years that the decade has been christened the Decade of the Capital Market. The extent of growth can be easily measured by the fact that as against an annual average amount of just Rs. 900 million raised from the primary market in the 1970s, Rs. 57.49 billion was raised from the primary market in 1991-92. The number of listed companies rose over the decade from about 2,200 to over 6,500, catapulting this nation to second only to the United States of America, which had 6,742 listed domestic companies at the end of 1991. The daily turnover in the Indian stock markets has shot up from about Rs. 150 million in 1979-80 to about Rs. 3.32 billion during 1991-92. The number of shareholders has also risen sharply from about two million to over 14 million during the same period, again making India second only to the United States in size of shareholding population. And if investors in units, mutual funds, etc., are considered, then the figure may-well cross 25 million. We expect this figure to be over 50 million by the turn of the century. Market capitalisation has also increased from about Rs. 35 billion to over Rs. 2.25 trillion during the last decade, accounting for about 40 percent of the GNP, as against about five percent ten years ago.

India is now a major player in the emerging markets of the world, next only to Taiwan, Korea and Mexico, in respect of both market capitalisation and turnover. In terms of U.S. dollars, the market capitalisation at the end of 1991 was $53.03 billion, as compared to $124.9 billion for Taiwan, $96.4 billion for Korea, and $98.2 billion for Mexico. The volume of turnover in the Indian stock markets during the year ended 1991 was $36.5 billion as compared to $365.2 billion for Taiwan, $85.5 billion for Korea and $31.7 billion for Mexico.

In tune with developments the world over, the complexion of the governing boards of the Indian stock exchanges too are undergoing a change, as more non-broker directors are being inducted into the boards of the stock exchanges. Presently, non-broker directors who are generally representatives of the Ministry of Finance, Department of Company Affairs, Reserve Bank of India, financial institutions, Securities and Exchange Board of India — the regulatory body of the securities industry — and some leading personalities drawn from different professions including chartered accountancy, law, etc., constitute about one-third of the strength of these boards. It is our intention to raise the strength of non-broker directors so as to inject greater objectivity into the deliberations of governing boards.

With the increase in the number of stock exchanges, the number of active stockbrokers has also increased during the last decade. There are today over 5,000 active stockbrokers all over the country, as against about 1,250 ten years ago. Stockbrokers in India, as elsewhere, are encouraged to amalgamate into corporate entities for which the statute was specially amended in July, 1987. As this amendment requires a majority of the directors of the corporate entity also to be members of the stock exchange in their individual capacity, it is now proposed to amend the statute further, enabling enrollment of a corporate entity director as a member without the requirement of any individual director being a member of the stock exchange.

Indian stock markets continue to operate in the conventional style of face-to-face trading with bids and offers made by open outcry. The stock exchanges at Bombay, Calcutta and Ahmedabad are basically quote-driven markets with the jobbers standing at specific locations in the trading ring called trading posts and announcing continuously two-way quotes for scrips traded at the post. As there is no prohibition on a jobber acting as a broker and vice-versa, any member is free to do jobbing on any day. In actual practice, however, a class of jobbers have emerged who generally confine their activities to jobbing only. It is worth noting that in highly volatile scrips, the spread is by far the narrowest in the world, being just about -0.1 to 0.25 percent, as compared to about 1.25 percent in respect of alpha stocks, i.e., the most highly liquid stocks, on the London Stock Exchange. The spreads, however, widen as liquidity decreases. This is basically because of the high velocity of transactions in active scrips. It is significant that about 1,500 securities get traded on any given trading day on the Bombay Stock Exchange. The markets in the rest of the country are mainly order driven markets with the buyers and the sellers transacting directly with each other.

We in India are very stringent on disclosure requirements for companies seeking listing on stock exchanges. The listing agreement, which a company is required to execute with the stock exchange before enlistment, and the provisions of the Companies Act provide for detailed ongoing disclosure requirements by a listed company.

At the Bombay Stock Exchange, settlement of transactions by way of delivery of securities and payment of price takes about a fortnight. This is primarily due to the system of settling transactions in a batch mode. It is now proposed to have an on-line system of processing transactions reported directly from the screen to be operative along with the automation of the trade. This will help reduce the period required for settlement of transactions. It is planned to reduce in the first instance the period of trading from 14 days to 5 days, Monday to Friday, with the settlement being affected the following week. Subsequently, a move to a rolling settlement system of T+5, i.e., the settlement being affected on the fifth trading day following the date of transaction, eventually to be replaced by T+3, as recommended by the Global Group of Thirty.

The Indian stock markets have displayed a remarkable degree of poise and stability, mainly due to the checks and balances built into the system, and the various timely and effective measures taken by the Government and stock exchange authorities from time to time. As per a study conducted by the Bombay Stock Exchange, the average annual fluctuations in the All India Index of prices of ordinary shares of the Reserve Bank of India was only 25.1 percent during the period 1980 to 1989, which was on par with the corresponding figures of 22.0 percent for the London Stock Exchange and 23.9 percent for the New York Stock Exchange, and well below the average of 30.2 percent of 15 leading countries.

The cardinal objective of regulation of stock exchanges the world over is protection of the interests of investors, and that is the objective in our country, too. The stock exchanges in India have on their own evolved a number of measures to alleviate the grievances of investors and to grant them a progressively greater degree of protection. A Customers' Protection Fund was set up at the Bombay Stock Exchange in October 1986 on the lines of the Securities Investor Protection Corporation of the U.S.A. The Fund has over Rs. 4 million to its credit as of today and it is being administered only for the benefit of clients of defaulting members of the exchange and their beneficiaries in respect of genuine investment claims.

The Bombay Stock Exchange has made significant progress in its modernisation and computerisation programme. Our project consultant, CMC Limited, has prepared a technical report for implementation of the programme in four phases beginning from the 3rd quarter of 1992 and ending with the first half of 1994. The total investment outlay of this project will be about Rs. 730 million. The system will support on-line processing, and at the same time facilitate real-time display of trade information, so as to inject complete transparency to trading. It would also enable the setting up of a value-added information service, which would be useful to the members and more particularly, the investors and media.

We are also planning to immobilise securities in India. The Bombay Stock Exchange has, in association with the Bank of India, Ltd. — a leading nationalised bank of the country, which currently runs the clearing House of the Exchange — established BOI Shareholding, Ltd. This will initially act as a depository in respect of shares involved in carry-forward transactions in specified shares worth about Rs. 5 billion, with the shares moving by book-entries only. Later on we plan to develop a certificateless society, as has already been done in Norway, Denmark and France, and as is being planned in the U.K. with the development of TAURUS. We are making serious attempts to put this proposal into operation.

The Bombay Stock Exchange, along with the Delhi, Calcutta, Madras and Ahmedabad Stock Exchanges, has jointly appointed Arthur Andersen & Associates, a leading firm of management consultants, to study and develop a blueprint for establishment of a National Stock Market System in the country. The National Stock Market System would, in the normal course, enable an investor in one part of the country to trade at the best market price with an investor in any other part of the country, through the members of the stock exchanges, and subsequently clear and settle the trade in an efficient and cost effective manner. A.A. & A. have submitted a draft report on the feasibility of having such a system in India and they are shortly expected to commence work on the technological study and the implementation plan of the National Stock Market System. We have also prepared draft capital adequacy norms for members which we plan to introduce shortly in consultation with the Securities and Exchange Board of India — the securities regulatory body in our country.

Investment in Indian stock markets, until now, was not allowed to foreigners except through offshore mutual funds. However, foreigners can now invest in the Indian primary and secondary markets through the intermediation of foreign institutions such as pension funds, mutual funds, investment trusts, asset management companies, nominee companies and incorporated/institutional portfolio managers or their power of attorney holders, after these foreign institutions register with the Securities and Exchange Board of India and comply with certain guidelines. The foreign institutional investors will also be required to file another application with the Securities and Exchange Board of India addressed to the Reserve Bank of India for seeking various permissions under the Foreign Exchange Regulation Act of India. The Securities and Exchange Board of India permission and the Reserve Bank permission will be available from the Securities and Exchange Board under a single window approach. The permission to the foreign institutional investor would enable it to:

(1) Open foreign currency denominated accounts in a designated bank;

(2) Open a special non-resident rupee account to which could be credited all receipts from the capital inflows, sale proceeds of shares, dividends and interest;

(3) Transfer sums from foreign currency accounts to the rupee account and vice-versa, at the market rates of exchange;

(4) Make investments in securities in India out of the balances in the rupee account;

(5) Transfer repatriable (after tax) proceeds from the rupee account to the foreign currency accounts;

(6) Repatriate the capital, capital gains, dividends, incomes received by way of interest, etc., subject to the designated branch of a bank — the custodian being authorised to deduct withholding tax on capital gains and arranging to pay such proceeds at market rates of tax and remitting the net exchange.

In conclusion, I would like to state that the Indian stock markets are on the verge of a takeoff from a closed economy to one which is partially liberalised and is in the process of further liberalisation. We are witnessing a slow move toward integration with global markets which we believe has to and will take place soon, and we feel the liberalisation measures announced recently have heralded the move already. We are planning to incorporate new ideas and technologies to further serve and protect the interest of investors, the benefits of which will be for all to see in the coming years. We are evolving a suitable policy and institutional framework which can facilitate a low cost security issue mechanism and encourage investor participation by instilling greater confidence. We are also planning to design a framework for cross-border listing of securities of SAARC countries in consultation with the exchanges of concerned countries. In this regard we are planning to organise a conference of SAARC stock exchanges in Bombay in early 1993 to exchange ideas thereto and design a suitable mechanism.

The growing commitment of countries in South Asia to a free market economy and the democratic plurality adopted by them have focused the need for greater regional cooperation among SAARC countries. We in India look forward to greater cooperation between countries of the region so as to harmonise laws relating to capital markets of the region and we hope we are able to make a beginning in this regard at this conference.

RECENT DEVELOPMENT IN THE KUALA LUMPUR STOCK MARKET

by

Salleh A. Majid
General Manager of the Kuala Lumpur Stock Exchange

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INTRODUCTION

The Malaysian stock market has seen several significant developments over recent years. It has evolved and developed over the years to be rated today as the top bourse in ASEAN in terms of market capitalization with a value of M$203.7 billion as at September 11, 1992. (Please refer to Table II attached)

The Malaysian market is quite different from its counterparts in Asia. It offers a good cross section of the country's economic activity. This is reflected in the 356 companies which are currently listed on the Kuala Lumpur Stock Exchange's Main Board and Second Board. (Please refer to Table I attached)

MARKET SIZE (Please refer to Tables I-V)

Market size has seen a dramatic increase since the yesteryears of the 1980s with total market capitalization representing approximately 80 percent of our current GNP. Last year the KLSE had a total market capitalization of more than U.S. $62 billion. In fact, the total market value of the KLSE accounts for more than 38 percent of the combined market value of the stock markets in the ASEAN region.

Reflecting substantial trading activity in the equities market, trading volume which totalled 515.6 million units valued at M$2.02 billion in 1973, soared 580 percent to 10.2 billion units valued at M$18.5 billion in 1989 and to 13.2 billion units worth M$29.5 billion in 1990. Turnover amounted to 12.3 billion units valued at M$30.1 billion in 1991. As at September 11, 1992, turnover has recorded 8.0 billion units valued at M$23.4 billion.

In terms of funds raised, M$1.60 billion was raised by 39 new issues, while rights issues raised a further M$1.67 billion last year.

One of the key factors that contributed to making the KLSE what it is today, was and still is the remarkable performance of the Malaysian economy, growing at an average annual rate of 9.0 percent for the period 1987-1991. Another factor was, of course, the progressive changes that the KLSE has undertaken in the recent years.

The KLSE began to play a more vital role since the delisting of Malaysian incorporated companies from the Stock Exchange of Singapore (SES) with effect from January 1, 1990 resulting in the KLSE becoming the sole official market for Malaysian stocks.

Before I go on to the more exciting developments that have taken place in the market, let me just dwell a while on the regulatory structure of the securities market.

REGULATORY STRUCTURE

Administration of the securities industry is governed by the Securities Industry Act, 1983 (SIA 1983), and the law relating to companies is contained in the Companies Act 1965 (CA 1965).

The SIA comes under the purview of the Ministry of Finance and the regulators are as follows:

THE KLSE

The KLSE is a self-regulating organisation with its own Memorandum & Articles of Association. It has a set of rules which govern the conduct of its members in securities dealings. Its responsibilities also cover the surveillance of the market and the enforcement of its listing requirements.

THE REGISTRAR OF COMPANIES (ROC)

The ROC is empowered to administer and regulate the SIA 1983, ensuring that stock broker companies comply with the provisions thereunder. Under the SIA 1983 and CA 1965, the ROC has regulatory oversight over companies, directors, stock broker companies, individual deals in securities, investigations of potential violations and prosecutorial functions.

THE CAPITAL ISSUES COMMITTEE (CIC)

The CIC is the informal watchdog committee to oversee the securities industry. The SIA 1983 gives it legal backing to act as a consultative body to advise the Minister of Finance and the ROC on all relevant matters. The CIC has the functions of imposing administrative disciplinary sanctions and investigation of the financial and dealing position of stock broking companies.

THE FOREIGN INVESTMENT COMMITTEE (FIC)

The FIC implements guidelines on regulation of acquisition of assets or interests, mergers or takeovers of companies and businesses, and is responsible for major issues on foreign investment.

THE PANEL ON TAKE-OVERS AND MERGERS (TOP)

TOP ensures that all take-overs and mergers are conducted in an orderly manner. It also ensures the protection of the interest of minority shareholders as provided under the Code.

RELATIONSHIP BETWEEN THE AUTHORITIES

The Stock Exchange maintains close relationship with the Registrar of Companies (ROC) and the Capital Issues Committee (CIC) in its supervision.

Close liaison is needed between the KLSE and these regulatory bodies pertaining to securities dealings. For instance, by virtue of the ROC being the custodian of the Securities Industry Act, it is important for the KLSE to provide relevant information on the market to the ROC.

In addition to the above, the Executive Chairman of the Stock Exchange has regular meetings with our Minister of Finance concerning our equities market.

Over the years, there has been increasing awareness to sustain a good relationship between the regulatory bodies for well coordinated planning and monitoring against violations of the acts. This will move to check against market manipulations, company haphazardness and malpractice in the future.

SECURITIES COMMISSION

The year 1992 will see the establishment of the Securities Commission which is to act as a "watch dog" commission over the activities of the securities industry. All the regulatory bodies will be "housed" under the commission, hence streamlining the current securities laws and regulations. This will certainly lead to a more efficient capital market and also to greater confidence among the local and foreign investors in Malaysia.

ECONOMIC AND POLITICAL OVERVIEW

Development in Malaysia has been commendable in relation to the sluggish experience of other countries in the region. Last year, in the midst of slowdown in global economic activities, Malaysia was fortunate to record one of the highest, if not the highest GDP growths in the world with a relatively low inflation rate. The GDP growth in 1991 was 8.8 percent with an inflation rate at 4.4 percent.

Our Current economic forecasts suggest that while growth in real terms will be slower in the coming months, Malaysia is still expected to experience GDP growing at 8.0 percent in 1992. This stems from a pick-up in economic activities of the OECD countries in the second half of the year. The OECD countries are projected to clock a growth rate of 1.8 percent and 3.3 percent for 1992 and 1993 respectively.

Much has been said about our buoyant economy. Now, the consequences to such are:

- rising inflation
- high interest rates
- stronger ringgit
- rising wages
- pressure off the trade account

Although inflationary pressures are growing, our present tight monetary policies should keep inflation in check while stable prices in major OECD countries and a strong ringgit will blunt external inflationary forces.

The recent inflation figures have been encouraging as a consequence of Bank Negara's effectiveness in curbing excessive consumer spending. For the first seven months of this year, the inflation rate on average was at 4.5 percent. At present, Malaysia is facing inflation at 4.9 percent due to the recent surge in the Consumer Price Index to over 7.0 percent.

In light of this, policies will remain tight and we will continue to exercise fiscal and monetary restraint and pursue structural reforms to keep inflation at bay. Another area which is helping to reduce inflationary pressure is lower prices due to the now stronger ringgit.

At the height of the present interest rates, the inflow of foreign funds, the need to encourage investments and slower loan growth will limit upside pressure on interest rates.

Inflation and the current deficit should subside in 1993, just as GDP growth begins to reaccelerate on the back of rising world trade. The current account balance is expected to show a remarkable improvement in 1992 with our current account deficit estimated at around M$10 billion this year compared with M$12 billion in 1991.

It is comforting that during the first five months of 1992 imports slowed down to 2.7 percent, compared with an 8.2 percent growth in exports. If this trend should carry on for the rest of the year, the deficit in current account of the balance of payments could be reduced to 7.8 percent of GNP compared with 10.1 percent last year. On top of that, the sharp increase of investments in imports of capital goods (which largely caused the current account deficit) should translate into higher output and exports in the coming years.

The new National Development Policy (1991-2000) has set the pace for greater emphasis on growth and is committed to the maintenance of foreign equity guidelines, especially for manufacturing and services. The year 2020 has also been marked as the year for the country to achieve developed nation status — our VISION 2020. Equally important is that the private sector will be the main engine of growth.

As such, our plans and vision will certainly propel our stock market into the forefront of progress and thus we expect to see further changes in the years ahead.

DEVELOPMENTS IN THE STOCK MARKET

While the equities market witnessed some major developments in the sixties and seventies, it was really the late eighties that saw some far-reaching changes.

Among some of the developments that have brought the Kuala Lumpur Stock Exchange (KLSE) to its present level of sophistication are:

- Computerisation of the clearing system with the setting up of a clearing house, SCANS (March 1984) and introduction of the Fixed Delivery and Settlement System (February 12, 1990).
- Real-time information dissemination via MASA (August 12, 1987) and MASA II (June 1990).
- The advent of corporatisation (1986) and with it greater professionalism and enhanced investment research within the industry.
- Implementation of SCORE (System On Computerised Order Routing and Execution) on May 15, 1989, which was completed on November 10, 1989. This semi-automated trading system has meant the complete conversion of the KLSE's traditional open outcry system of trading, thus doing away with the trading floor. Even more significant is that the switch to SCORE has brought about substantially higher trading volumes — to as high as 200 million shares a day.
- The de-listing of Malaysian incorporated companies from the Stock Exchange of Singapore (SES) with effect from January 1, 1990. There were some skeptics at that time who predicted that the Malaysian market will fade away but the significant growth registered by the KLSE since then clearly indicates otherwise. Indeed, the KLSE is now the biggest bourse in the ASEAN in terms of market capitalization with a value of M$203.7 billion as at September 11, 1992. (Please refer to Table II attached).
- Minimum paid-up capital of M$20 million (U.S. $8 million) requirement for all stockbrokerage companies in order for brokering companies to be better capitalised and financially strong to meet the needs of the growing securities industry and the challenges of the increasing globalisation of the market.
- Branches of stockbrokerage companies.
- Privatization — this has led to the listing of several state-owned enterprises thus further enhancing market depth and liquidity (e.g., Telekom, Proton and Tenaga Nasional).
- Privatization programmes have helped to broaden and deepen the stock market. For instance, the privatisation of two large utility companies, namely Telekom Malaysia and Tenaga Nasional, has attracted a considerable amount of foreign funds into the stock market. The two

giants together account for more than 26 percent of the total market capitalization of the KLSE.

In terms of attracting investors, Malaysia again ranks number one. There were 3.10 million investors in the 5 ASEAN stock markets. The KLSE had 1.2 million or more than 38 percent of all ASEAN investors. Malaysia has a stock market participation rate of 6.9 percent and it is possible that participation rates may rise as a result of more state assets being privatised.

- Setting up of Rating Agency Malaysia (RAM) to provide independent credit ratings for corporate debt securities. This is part of the initiatives taken by the Malaysian authorities to boost the private debt securities market in Malaysia.

- Extension of trading hours — this is the latest move by the KLSE in its efforts to provide better trading accessibility to investors. Trading hours were extended by 90 minutes with effect from July 22, 1992 with the new trading sessions now being from 9:30 a.m. to 12:30 p.m. (10:00 a.m. to 12:30 p.m. previously) and from 2:30 p.m. to 5:00 p.m. (2:30 p.m. to 4:00 p.m. previously).

  The extension in trading hours is also in line with a similar move by the Stock Exchange of Singapore (SES) effective July 27, 1992. In view of the two markets' proximity, this enables Singaporean investors to also have access to Malaysian shares during the extended hours.

THE FUTURE

Having talked about the present status of the Malaysian market, let me move on to what is in store in the years ahead, especially in the wake of the increasing level of globalisation in the securities industry.

The KLSE's vision is to become a world-class stock exchange, buffering unique investment opportunities in a fast developing capital market within the industrialising Malaysian economy.

This calls for that even greater investment in technology -- skills and professionalism

- CDS: The introduction of the Central Depository System will mark a major milestone for the KLSE. It will result in an extremely efficient settlement and clearing system. A mock run was first conducted on the proposed CDS in July and some fine tuning is being done. Some minor changes to smooth its operations will be made and implemented in the coming second mock run. CDS will be implemented in stages with the Phase One covering new issues expected to be launched at the end of the year.

- Automatic Price Determination: We are in the planning stage of upgrading our present trading system. We have set up a task force to look into further improving the present SCORE trading system with a view to fully automated trading by the end of the year.

- New building: The KLSE will have its own modern building in the heart of Kuala Lumpur in the next three years.

- Setting up of the Securities Commission (SC): The authorities are working toward setting up a single regulatory agency for the securities industry by the end of the year. The Securities Commission Bill will be tabled in the Parliament later this month.

The setting up of an SC should be good for the capital market in that it will do away with the current structure of several regulatory authorities. This single agency will further ensure the orderly development of the securities market with more efficient, consistent and effective regulation thus giving rise to even greater confidence in the Malaysian capital market.

- The Kuala Lumpur Options and Financial Futures Exchange (KLOFFE) has been given approval in principal to introduce trading in equity options and financial futures. KLOFFE has said that trading in these derivative products is likely to commence soon. The successful implementation of these derivative products should further enhance liquidity in the underlying stocks.

- Privatization: With the privatization exercise gathering greater momentum, one can expect even more state-owned enterprises seeking listing on the KLSE.

  While it has been a general policy that foreigners are not allowed to participate during the initial public issue exercise, the foreign tender portion of Tenaga Nasional shares may be an indicator that in the future, it is highly possible that foreigners may be allowed to participate in a similar manner during large privatization issues.

- Communications Enhancement: Three main areas of concern we are addressing are infrastructure requirements, internal/external communications, and office automation/management information systems.

- Disaster Recovery: In view of the increasing automation of all operations, a comprehensive recovery system is being sought especially in the areas of operation — our trading facilities which include the surveillance system, the central depository and the database.

CONCLUSION

Overall, it can be said that Malaysia is probably one of the most open with its free entry to foreign investment and unrestricted repatriation of capital and income from shares. Besides, there is no capital gains tax in Malaysia. Not only is Malaysia able to provide for cross-border ventures, international alliances are common between domestic and foreign firms.

For a highly efficient capital market, the KLSE, the Malaysian stockbrokering industry and government authorities are constantly on the alert towards developing the Malaysian securities market and leading the way to a fully industrialised nation.

With positive factors such as a robust economy, sound infrastructure, and a stable political climate, it is evident that investment opportunities in the Malaysian economy, in general, and the securities market in particular, are immense. The future of the Malaysian equities market certainly looks bright.

TABLE I

NUMBER OF COMPANIES LISTED ON THE KLSE BY COUNTRY OF INCORPORATION						
YEAR	MAIN BOARD			SUB-TOTAL	SECOND BOARD	GRAND TOTAL
	M'SIAN	S'PORE	OTHERS			
1973	155	69	38	262	-	262
1974	163	67	34	264	-	264
1975	167	67	34	268	-	268
1976	173	64	27	264	-	264
1977	177	59	20	256	-	256
1978	180	57	16	253	-	253
1979	185	56	12	253	-	253
1980	182	56	12	250	-	250
1981	187	55	11	253	-	253
1982	194	56	11	261	-	261
1983	204	56	11	271	-	271
1984	218	56	8	282	-	282
1985	222	56	6	284	-	284
1986	227	55	6	288	-	288
1987	232	54	5	291	-	291
1988	238	53	4	295	-	295
1989	249	53	3	305	2	307
1990	268	-	3	271	14	285
1991	289	-	3	292	32	324
2.1.92 - 11.9.92	307	-	3	310	46	356

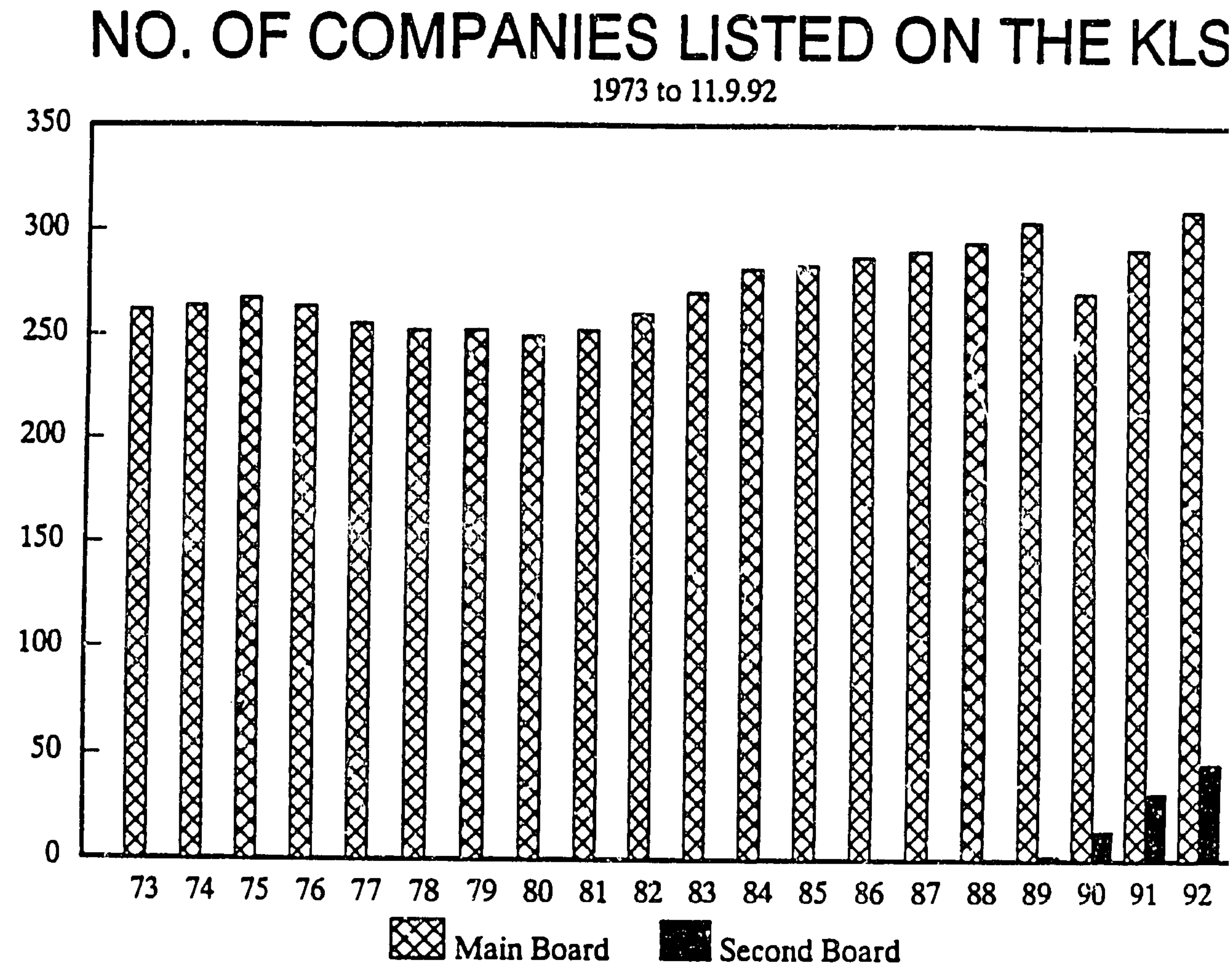

NO. OF COMPANIES LISTED ON THE KLS
1973 to 11.9.92
350
300
250
200
150
100
50
0
73 74 75 76 77 78 79 80 81 82 83 84 85 86 87 88 89 90 91 92
Main Board
Second Board

TABLE II

AS AT YEAR END	MARKET CAPITALISATION (M$ billion)			NOMINAL VALUE (M$ billion)		
	MAIN BOARD	SECOND BOARD	TOTAL	MAIN BOARD	SECOND BOARD	TOTAL
1973	13.3	-	13.3	3.8	-	3.8
1974	8.1	-	8.1	4.3	-	4.3
1975	11.7	-	11.7	4.8	-	4.8
1976	12.7	-	12.7	5.0	-	5.0
1977	13.7	-	13.7	5.2	-	5.2
1978	18.3	-	18.3	5.9	-	5.9
1979	24.6	-	24.6	6.5	-	6.5
1980	43.1	-	43.1	7.9	-	7.9
1981	55.4	-	55.4	10.7	-	10.7
1982	52.9	-	52.9	13.6	-	13.6
1983	80.3	-	80.3	16.3	-	16.3
1984	69.3	-	69.3	20.4	-	20.4
1985	58.3	-	58.3	22.6	-	22.6
1986	64.5	-	64.5	23.5	-	23.5
1987	73.9	-	73.9	26.6	-	26.6
1988	98.7	-	98.7	29.4	-	29.4
1989	156.0	0.1	156.1	34.3	0.03	34.3
1990	131.1	0.6	131.7	35.1	0.2	35.3
1991	159.9	1.5	161.3	41.2	0.5	41.7
As at 11.9.92	201.8	1.9	203.7	49.5	0.8	50.3

KLSE TOTAL MARKET CAPITALISATION & NOMINAL VALUE
FROM 1973 TO 11.9.92

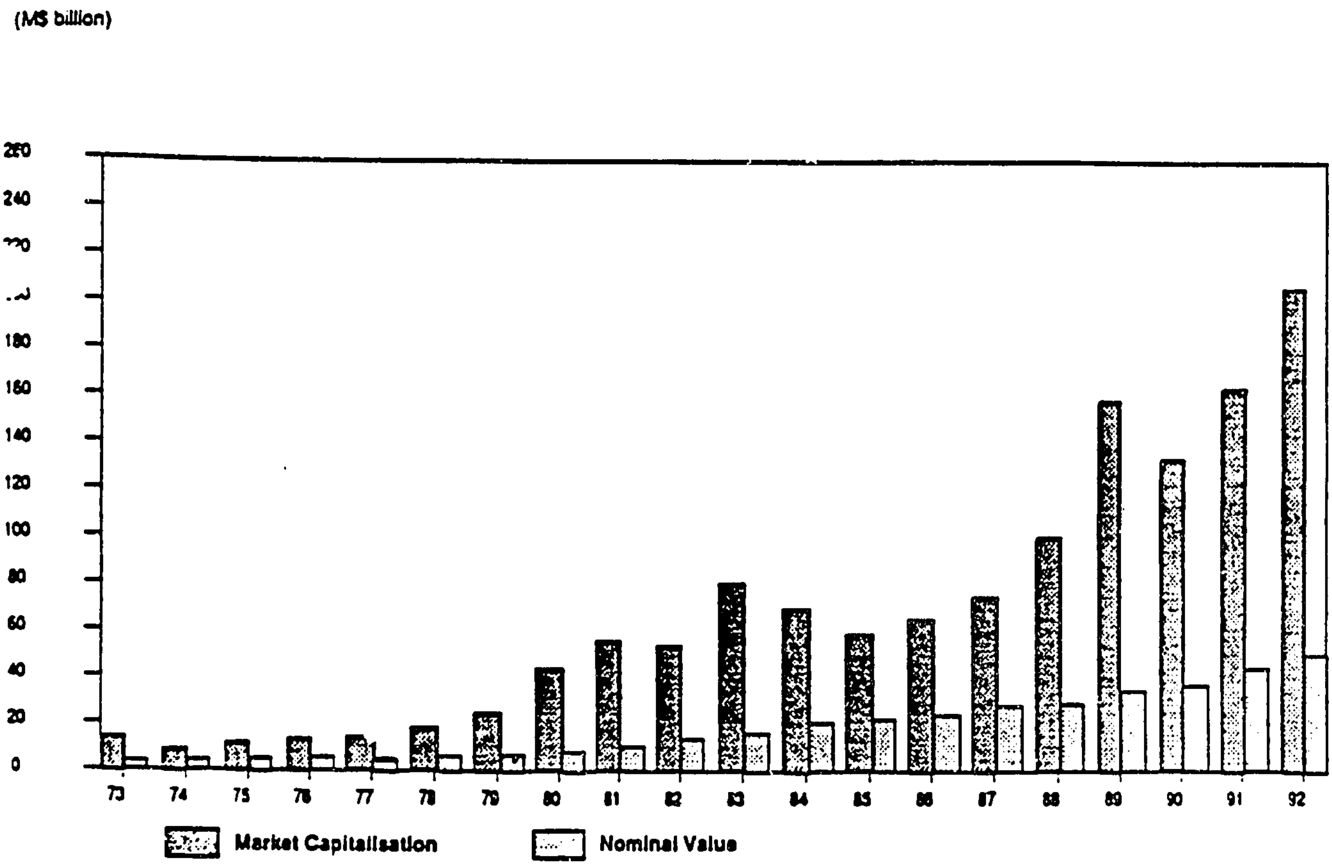


TABLE III

YEAR	VOLUME (billion units)			VALUE (M$ billion)		
	MAIN BOARD	SECOND BOARD	TOTAL	MAIN BOARD	SECOND BOARD	TOTAL
1973	0.5	-	0.5	2.0	-	2.0
1974	0.4	-	0.4	0.7	-	0.7
1975	0.6	-	0.6	1.3	-	1.3
1976	0.4	-	0.4	1.0	-	1.0
1977	0.6	-	0.6	1.0	-	1.0
1978	1.1	-	1.1	2.5	-	2.5
1979	0.6	-	0.6	1.6	-	1.6
1980	1.5	-	1.5	5.6	-	5.6
1981	1.6	-	1.6	8.1	-	8.1
1982	1.1	-	1.1	3.3	-	3.3
1983	2.3	-	2.3	7.9	-	7.9
1984	1.9	-	1.9	5.7	-	5.7
1985	2.9	-	2.9	6.2	-	6.2
1986	2.3	-	2.3	3.4	-	3.4
1987	5.3	-	5.3	10.1	-	10.1
1988	4.0	-	4.0	6.8	-	6.8
1989	10.18	0.02	10.2	18.4	0.06	18.5
1990	13.1	0.08	13.2	29.3	0.22	29.5
1991	12.1	0.28	12.3	29.2	0.85	30.1
2.1.91 - 11.9.92	7.8	0.19	8.0	22.8	0.6	23.4

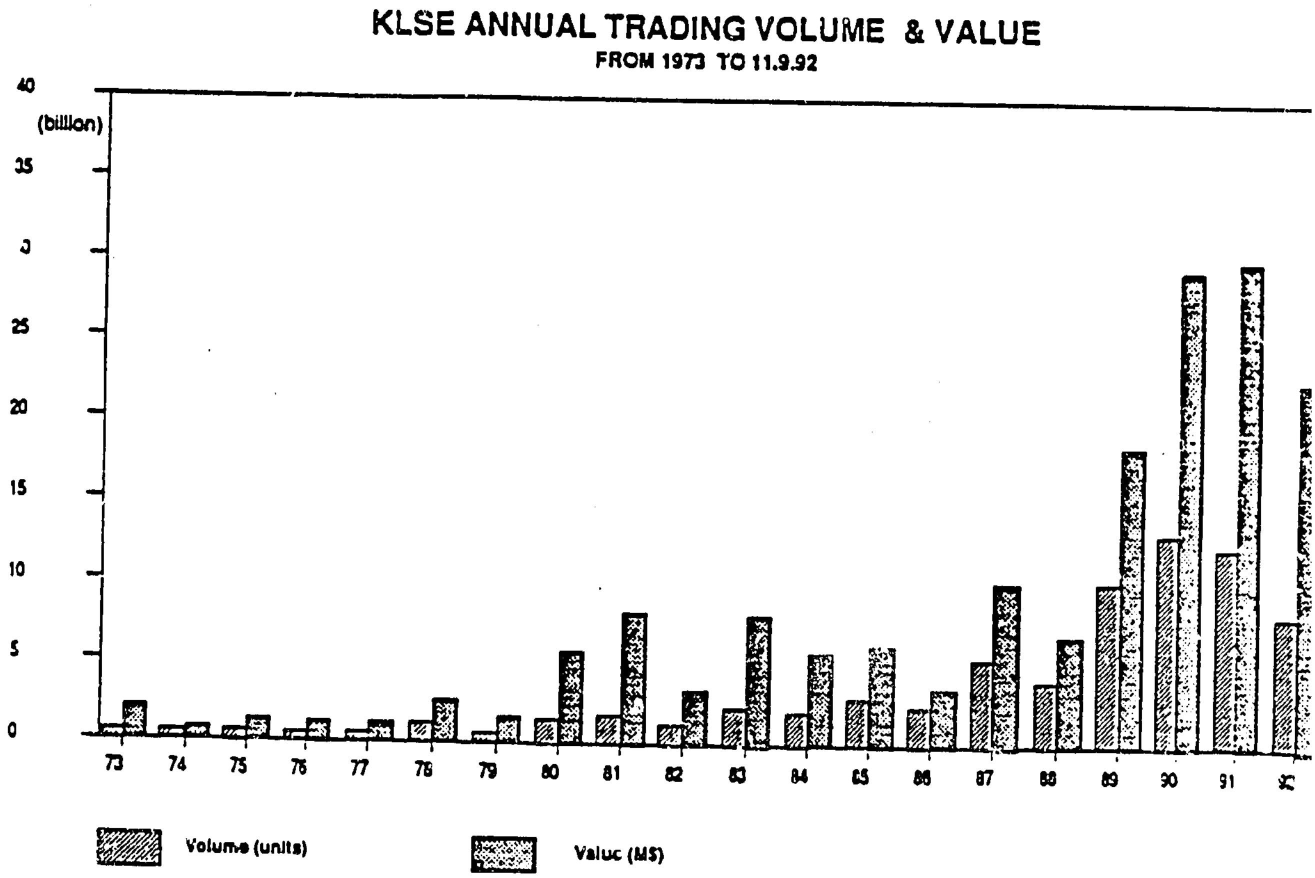

KLSE ANNUAL TRADING VOLUME & VALUE
FROM 1973 TO 11.9.92
(billion)
40
35
25
20
15
10
5
0
73
74
75
76
77
78
79
80
81
82
83
84
85
86
87
88
89
90
91
Volume (units)
Value (M$)

TABLE IV

YEAR	DAILY AVERAGE VOLUME (mil units)			DAILY AVERAGE VALUE (M$ mil)		
	MAIN BOARD	SECOND BOARD	TOTAL	MAIN BOARD	SECOND BOARD	TOTAL
1973	3.1	-	3.1	12.2	-	12.2
1974	1.6	-	1.6	2.9	-	2.9
1975	2.5	-	2.5	5.3	-	5.3
1976	1.7	-	1.7	4.0	-	4.0
1977	2.4	-	2.4	4.2	-	4.2
1978	4.6	-	4.6	10.4	-	10.4
1979	2.6	-	2.6	6.7	-	6.7
1980	6.0	-	6.0	22.6	-	22.6
1981	6.7	-	6.7	32.8	-	32.8
1982	4.4	-	4.4	13.3	-	13.3
1983	9.2	-	9.2	32.0	-	32.0
1984	7.6	-	7.6	23.3	-	23.3
1985	11.9	-	11.9	25.7	-	25.7
1986	9.2	-	9.2	13.6	-	13.6
1987	21.4	-	21.4	40.8	-	40.8
1988	16.3	-	16.3	27.6	-	27.6
1989	41.5	0.10	41.6	75.7	0.25	76.0
1990	53.3	0.32	53.6	119.6	0.89	120.5
1991	48.5	1.13	49.6	117.5	3.40	120.9
2.1.92 - 11.9.92	45.8	1.09	46.9	133.3	3.59	136.9

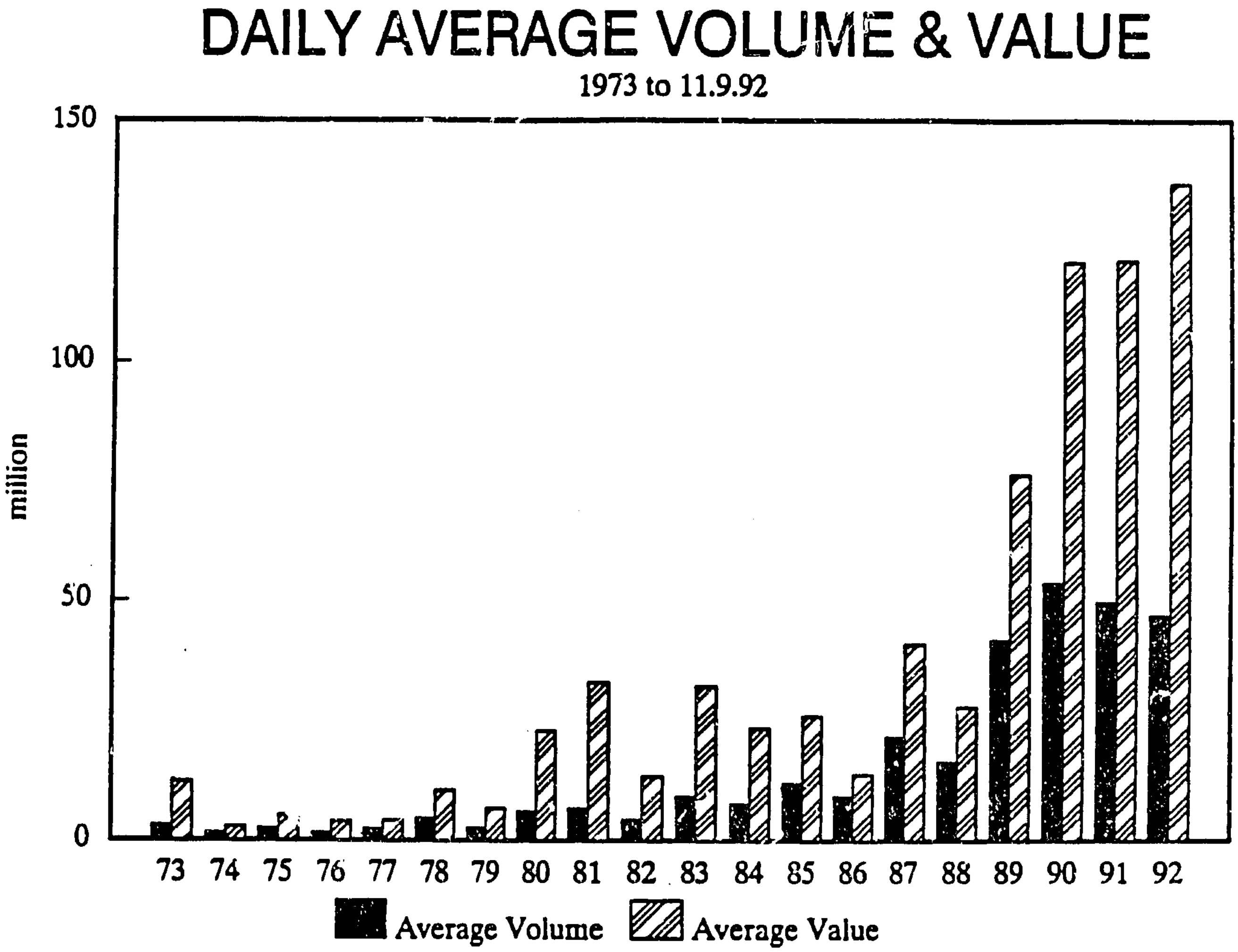
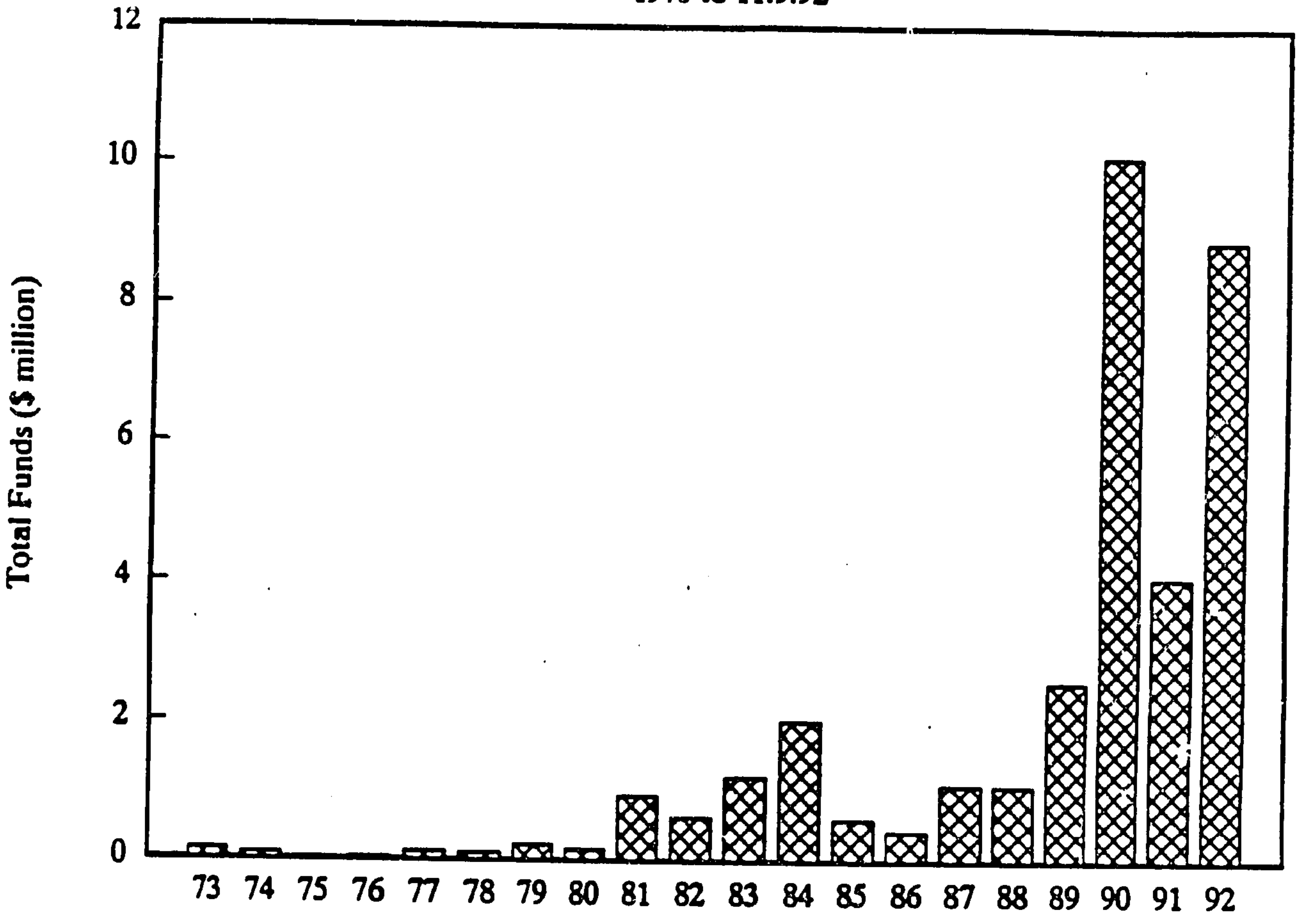

DAILY AVERAGE VOLUME & VALUE
1973 to 11.9.92
150
100
50
0
million
73 74 75 76 77 78 79 80 81 82 83 84 85 86 87 88 89 90 91 92
Average Volume
Average Value

TABLE V

FUNDS MOBILISED BY MALAYSIAN COMPANIES						
YEAR	PUBLIC ISSUE	RIGHTS ISSUE	SPECIAL/PTE PLACEMENT/ RESTRICTED ISSUE	SUB-TOTAL	OFFER FOR SALE	GRAND TOTAL
			M$ million			
1973	95.7	37.2	8.3	141.2	0.0	141.2
1974	12.4	49.6	4.1	66.1	19.6	85.7
1975	13.0	9.5	0.0	22.5	5.7	28.2
1976	0.0	22.0	13.5	35.5	0.0	35.5
1977	0.0	95.1	2.9	98.0	21.8	119.8
1978	5.4	24.5	22.8	52.7	46.4	99.1
1979	1.7	134.3	62.2	198.2	16.0	214.2
1980	2.1	103.2	31.8	137.1	14.0	151.1
1981	103.7	598.0	200.1	901.8	28.7	930.5
1982	182.7	286.8	131.6	601.1	27.7	628.8
1983	140.5	638.5	406.0	1,185.0	25.9	1,210.9
1984	174.4	1,347.4	461.4	1,983.2	24.3	2,007.5
1985	164.2	357.5	81.8	603.5	0.0	603.5
1986	24.0	298.4	97.0	419.4	7.5	426.9
1987	95.8	393.7	386.2	875.7	220.5	1,096.2
1988	53.3	789.3	136.3	978.9	111.7	1,090.6
1989	128.5	1,313.4	166.9	1,608.8	960.2	2,569.0
1990	2,597.1	5,503.0	389.8	8,489.9	1,670.5	10,160.4
1991	230.3	1,672.6	793.6	2,696.5	1,367.2	4,063.7
As at 11.9.92	3,624.8	3,492.4	167.4	7,284.6	1,648.8	8,933.4
TOTAL	7,649.6	17,166.4	3,563.7	28,379.7	6,216.5	34,596.2

FUNDS MOBILISED BY M'SIAN COMPANIES

1973 to 11.9.92



REVIEW OF THE PHILIPPINE STOCK MARKET PERFORMANCE 1991 - FIRST EIGHT MONTHS OF 1992

Report of the
Makati Stock Exchange, Inc.

Presented by

Irving I. Ackerman
Governor/Treasurer of the Makati Stock Exchange, Inc.

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THE MARKET IN 1991

In 1991, the Philippine stock market witnessed sharp and volatile fluctuations of share prices brought about by the series of adversities that struck the country. The market commenced the year in review on a bearish note in view of the outbreak of the Persian Gulf war on January 17. The Middle East crisis initially slackened trading activities. However, share prices shortly recovered with the eventual liberation of Kuwait.

While the market was still reeling from the harsh effects of the Gulf crisis, negative events occurred in succession which added more strains on the economy already limping from previous man-made and natural disasters. Foremost of these were: the eruption of Mt. Pinatubo in mid-June; the attempted ouster of Soviet President Miknail Gorbachev in a coup in August; the RP-U.S. military bases talks and subsequent rejection of the bases treaty in September; the flash flood precipitated by typhoon Uring which hit Ormoc City and killed thousands of people, and the mini-crash in Wall Street, both of which occurred in November.

Despite all these unfavorable developments, however, the Philippine equities market emerged as one of the world's most resilient as well as the top performing equity market in the Asia-Pacific region in 1991. The composite index of the Makati Stock Exchange (MKSE) gained a phenomenal 502.20 points or 76.74 percent for MKSE to close the year at 1,156.64 index points. Likewise, the Exchange's peso turnover increased noticeably by 41.44 percent to ₱21.72 billion. During the year, market capitalization expanded considerably to ₱269.4 billion or by a hefty 67.85 percent from its 1990 level of ₱160.5 billion. Consequently, the stock market's percent share to the country's Gross National Product (GNP) rose by more than six percentage points to 21.49 percent.

Another significant development of 1991 was the creation of the Capital Market Development Council composed of the Secretary of Finance, Governor of the Central Bank, Chairman of the Securities and Exchange Commission, and the Presidents of the Financial Executives Institutes of the Philippines, the Bankers Association of the Philippines, the Investment Houses of the Philippines, the Makati Stock Exchange, Inc., and the Manila Stock Exchange. The council aims to:

A. Recommend policies for the development of capital, and translate such policies into concrete actions and results.

B. Identify impediments to capital market development through an extensive evaluation of policies, laws, rules and regulations affecting the capital market, and recommend necessary reforms, amendments, changes and modifications to eliminate such impediments.

C. Endeavor to evaluate and recommend monetary and fiscal polices which complement each other and are conducive to capital development.

D. Endeavor to stimulate medium and long-term investments into productive enterprises by addressing various issues affecting the capital market such as, but not limited to, securities trading practices, listing of securities in the stock exchanges, taxes on financial instruments, disclosure of material information, efficiency of financial transactions, creation of an efficient bond market, duplication and fragmentation in securities regulation, standardization of transaction documents, accounting and financial reporting standards and other concerns which influence investor confidence.

E. Encourage the simplification of regulatory procedures to ensure the timeliness of registrations or approvals, which is critical in dynamic financial markets.

F. Propose necessary legislative programs, supported by its studies and analyses, for consideration of Congress. And, suggest for the guidance of other concerned agencies of government relevant policy measures that will be conducive to capital market development.

THE FIRST EIGHT MONTHS OF 1992

Inspired by the improvements in the local political and investment climate, the Philippine stock market[1] sustained its bullish pace in the first eight months of 1992. In January, the market barometer of the two Exchanges netted an impressive monthly gain of 121.80 index points or 10.53 percent for Makati Stock Exchange, Inc. and 104.10 points or 9.04 percent for Manila Stock Exchange. However, the market shortly underwent some corrections and consolidation due to uncertainties as to the outcome of the May 1 election, the continued drought in Mindanao and, the severe power outages which resulted in decreased productivity of most companies.

During the first eight months of 1992, Makati Stock Exchange, Inc. registered a value turnover of ₱30.78 billion while the Manila Stock Exchange generated ₱22.86 billion for an aggregate value turnover of ₱53.64 billion. The January to August peso turnover of both Exchanges surpassed their total transaction in 1991 by a remarkable 41.71 percent for Makati Stock Exchange, Inc. and 29.23 percent for Manila Stock Exchange. On the other hand, compared to the same period last year, Makati Stock Exchange's value turnover for the first eight months of 1992 was larger by a remarkable 110.20 percent or ₱16.14 billion while for Manila Stock Exchange by 95.32 percent or ₱11.16 billion. Average daily turnover likewise improved from ₱86.87 million in 1991 to ₱187.69 million for MKSE and from ₱70.76 million to ₱137.72 million — considerable growth rates of 116.05 percent and 94.63 percent, respectively. Moreover, market capitalization at the end of August 1992 expanded to ₱347.0 billion.

This remarkable rise in market turnovers and capitalization may be attributed to the relatively higher share prices and the listing of new stocks. During the period in review, there are six companies which made public offerings and were listed on the stock exchanges, namely: Manila Electric Company (Meralco), Cebu Property Ventures and Development Corporation (CPVDC), International Container Terminal Services, Inc. (ICTSI), Easycall Communications, Inc. (ECPCOM), Union Bank of the Philippines (UNION) and ABS-CBN Broadcasting Corporation (ABS-CBN). Total Funds raised from these new listings amounted to almost ₱13 billion, at least half of the ₱26 billion raised in 1991.

Of the six, Meralco, ABS-CBN and ICTSI were well received by investors. Meralco's listing proved to be very successful, even sending the stock market soaring high. From its offering prices of ₱118.00 per share for Class "A" and ₱121.00 for Class "B", Meralco's stock price surged to ₱184.00 and ₱287.50, respectively. Likewise, ABS-CBN and ICTSI impressively followed the same trend. From ₱15.00 to ₱32.00 and ₱6.70 to ₱25.00.

The secondary offering of the Philippine National Bank (PN-B) for an additional 10 percent of the bank's outstanding capital stock also took place during this period. Once again, the offering was successful, during which for the first time the "Open Pricing" formula and the "Greenshoe Option" mechanism — common practices in the United States — were employed.

[1] There are two (2) existing stock exchanges in the Philippines today, the Makati and Manila Stock Exchanges. The Makati Stock Exchange, Inc. (MKSE) was incorporated on May 27, 1963 but started formal operation only on November 16, 1965. Manila Stock Exchange (MSE) on the other hand was incorporated in 1927 and started operation on August 8, 1927.

OUTLOOK FOR THE REST OF THE YEAR

We are optimistic that the prospects for the Philippine economy and stock market remain bright for 1992. The factors that augur well for their improvement are:

1. The passage of a new Foreign Investment Law which allows foreign investors a 100 percent equity stake in domestic ventures, except those listed in the Constitution and special laws, provided that foreign investors adhere to a three-year transition period. Foreign ownership had previously been limited to 40 percent.

2. The passage of tax reform measures to reduce the country's fiscal deficit. The tax measures include a simplification of the income tax system, a withholding tax on wage income, stronger penalties for tax evasion, and transfer tax reforms that rationalize inheritance taxes and taxes on donors.

3. The recent approval by the International Monetary Fund (IMF) of the country's economic stabilization program.

4. The liberalization of the foreign exchange by the Central Bank.

5. The extension of the life of the Asset Privatization Trust by the Government.

6. The growing gross international reserves of the Central Bank which gave strength to the Philippine Peso vis-a-vis the U.S. dollar. As of end-August, it appreciated markedly by ₱3.71 from its year ago level of ₱27.00 to ₱23.29 per dollar.

7. The lifting of the remaining 5 percent of the import levy.

8. The softening of interest rates which was manifested by the continuous decline of Treasury Bill rates. From a high of 28-42 percent (all maturity) in January 1991 to just 16-20 percent in August 1992.

9. The development and production of the West Linapacan oil discovery in Northwest Palawan starting mid-1992.

10. The slow down in inflation rate. It decelerated substantially from last year's annual average rate of 18.71 percent to a single-digit of 8.86 percent in August this year.

11. The high hope of the people for a bright change in the country's economy under the Ramos administration.

The long delayed unification of the two stock exchanges seems to have become a reality with the organization of the Philippine Stock Exchange as mandated by the President of the Republic of the Philippines, President Fidel V. Ramos. In his speech during the Philippine Securities and Exchange Commission Institute Seminar held at the Philippine International Convention Center on July 28-30, 1992, he openly declared that it is the policy of his administration to unify the two Exchanges. The process of unification is now taking place.

We, in the Philippine stock market, are of the view that with the continued robust expansion of the domestic market, the country shall soon become a significant factor, not only among the emerging markets in the Asia-Pacific region, but in the global arena as well.

GROWTH & RECENT DEVELOPMENT IN STOCK EXCHANGES IN PAKISTAN

by

Firozuddin A. Cassim
Ex-President, Karachi Stock Exchange (Guarantee) Limited

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There are at present three Stock Exchanges in Pakistan. Their respective sizes in terms of membership, listing and market capitalization are as follows:

Table A

Location	Year Established	Membership Ind.	Corp.	Total	No. of Cos. Listed 31-8-1992	Listed Capital	Market Capitalization (In billions)
Karachi	1949	196	4	200	616	Rs. 54.307	Rs. 181.7296
Lahore	1971	129	-	129	524	Rs. 46.333	-
Islamabad	1992	73	-	73	81	-	-

To fully comprehend the impact of the recent policy changes on the shares market, it is necessary to very briefly review the past trends vis-a-vis economic idealogy and policies pursued then by the government. Since Karachi has always been the center of activity, I shall confine myself only to this market.

From 1947 to 1971

During this period Pakistan economic policy was guided by the free market economic system. During the 1950's, while industrial development was being encouraged, the major emphasis was, however, on agriculture and trade. It was between 1958 and 1970 that the major thrust toward industrialization and growth of capital markets took place. The stock exchange also grew in proportion and the number of companies listed went up from 13 in 1949 to 318 by the end of 1971 and listed capital increased from Rs. 37.000 million to Rs. 4.439 billion. The stock exchange developed not merely as an equity market, but also played a role as a major financial institution in the capital markets, particularly in the trading of bonus vouchers, a paper for foreign exchange conversion. During this period two institutions for the support of the capital market were set up through government statutes. They were the National Investment Trust Limited (NIT) — an open end mutual fund started in 1963, and the Investment Corporation of Pakistan (ICP) in 1966. These two institutions were given defined roles for mobilization of savings and their diversion to the stock market and related financial activities. The growth of the stock exchange during this period was most satisfactory and it was during this period that regulatory legislation was also introduced through SEAP Ordinance in 1968, and SEAP Rules in 1971, which sought to protect the rights of shareholders and to organize the activities of the members of the stock exchanges, and to lay down the reporting requirements for companies seeking listing and those already listed on the exchanges.

1971 to 1977

In 1971 Pakistan underwent a major political change resulting in the loss of the Eastern Wing of our country as the now independent nation of Bangladesh. The elected government which took over sought to introduce a new social and economic order by abandoning the private sector oriented development policies, and instead adopting the socialistic or "mixed economy" pattern, i.e., a larger role for government in economic activity to ensure a more equitable distribution of wealth. As a result, on January 1, 1972, the major industrial sectors were brought under state control through take-over of companies (which included 18 companies listed on the stock exchange) and on January 1, 1974, the financial and other sectors were brought under state control through nationalization of commercial banks, life insurance businesses, petroleum businesses, along with other smaller segments of the economy such as cotton ginning and rice husking. Compensation for shares acquired was paid through issue of 15-year bonds, bearing interest at 1 percent above the bank rate. Naturally the stock exchanges had very little role to play in this set up, and during this period only 13 new companies were listed.

1977-1985

The government changed again in July 1977 through Martial Law. The new government immediately reversed the ownership of cotton ginning and rice husking units to the previous owners. Although promises of denationalization of other sectors were made, nothing substantial took place except passing of an ordinance known as "Transfer of Management Ordinance" in 1979. I suppose it was probably due to the geopolitical situation in our region, especially the Afghanistan issue that took up most of the government's resources and, therefore, very little attention toward change of economic policy was given except assurances that there would be no further nationalization. This situation continued up to 1985.

1985 to 1990

During this period a policy tilt toward encouraging the private sector role was introduced and new instruments were launched, giving the stock markets a wider role to play in the capital markets. Major changes were the introduction of bearer bonds issued by the government as public debt, bonds issued by autonomous bodies such as WAPDA, and the relaxation of exchange control through the issue of Foreign Exchange Bearer Certificates. On the industrial policy side, the notable development was the permission to the private sector to undertake industrial ventures which were hitherto confined to state control. Participation of the private sector in the financial system was encouraged by allowing set up of investment banks and leasing companies and an attempt to Islamicise the economy through a new medium of defined Islamic activity in the form of modarabas, was launched, apart from the attempt to eliminate interest from the domestic banking activities, through changes in the documentation of loans and deposits, being based on profit and loss sharing schemes.

For the development of the capital markets, the major policy changes were: (A) exemption of dividend income from income tax in the hands of individual shareholders (this has subsequently been diluted and dividend income is now subject to a 10 percent deduction of income tax at source), and (B) a program of Rs. one billion disinvestment of shares of public sector enterprises. Capital gains on shares being already exempt from tax, equity investment was brought to par with other risk-free and tax-free government saving schemes. Although the disinvestment program did not materialize, the stage was again set for the stock markets to play an expanding role in the financial sector of the country.

In 1988, after the tragic plane crash resulting in the death of General Zia, the elected government which followed continued to pursue the policies of the previous government, particularly with regard to disinvestment of public sector shares to the general public. A 20 percent offering of Pakistan International Airlines (PIA) shares was made in 1989. But the disinvestment policy of this government did not envisage transfer of management control — it was aimed at broadbasing ownership of shares of state enterprises.

The growth of the stock exchange during the period 1977 to 1990, particularly after 1985, can be seen from the following table:

Table B

Year Dec.	No. of Listed Co.	Listed Capital	Market Capitalisation	SBP Index Base 1980-81 = 100	Annual Turnover No. of shares (in millions)	KSE 50 Cos. base 1982
1980	314	7.630	6,316	168.64*	25.785	-
1985	362	13.588	23,792	166.65	69.942	-
1987	378	16.890	38,647	228.39	157.298	1429
1988	403	18.162	43,530	262.67	169.263	1554
1989	438	22.522	52,786	277.28	214.572	1670
1990	487	28.056	61,750	308.53	215.397	1572

* Base year 1969 - 70 = 100

1991 to Date

The real revolution in the role, scope and dimension of the stock markets began toward the end of 1990 when the present government took office. For the first time in the history of our country a businessman and industrialist is at the helm of affairs and following the present universal trend of free market economic ideology the government, in February 1991, announced a set of major policy changes. Of these related to stock markets are:

1. Privatization of state enterprise units including commercial banks.

2. Permission to the private sector to set up commercial banks.

3. Permission to foreign investors to buy and sell freely on the stock exchanges with full repatriation facilities resulting in the floatation and listing of Pakistan Funds.

4. Removal of exchange control regulations by allowing Pakistanis and foreigners to have foreign currency accounts, and through issue of foreign currency paper, most notably the Dollar Certificates.

5. Auctioning of government bonds and creation of secondary bond markets.

Before presenting the market reaction to these policy changes, I would very briefly like to enlighten you on the basic implementation of these policies. So far as privatization is concerned, two banks have already been sold and handed over to the new managements. It is very encouraging to note that one of these banks was bought by the management and employees. Similarly, about 50 industrial units have been privatized, with a leading tractor manufacturing company also having been bought over by the management. It may be noted that the change in management to the private sector has already brought about a substantial improvement in the productivity of the privatized units. Apart from the privatization of the financial industrial sector, the utility sector is also being broad based through disinvestment of shares held by the government or government controlled institutions.

In my opinion, the process of privatization has been quite fair and transparent, although there may be opinions expressed and published to the contrary by vested sources. The government proposes, and rightly so, to continue and complete this program.

The privatization policy has given a new dimension to stock market activities, particularly in respect of placement of the shares with foreign investors and listings of these companies on the stock exchanges at prices at which transfer of management has taken place.

So far, as permission to foreign investors is concerned, specific Pakistan Funds which have been floated are:

1. Pakistan Fund — By CITICORP — Listed in Hong Kong.

2. Credit Lyonnaise: An open-end fund.

3. Pakistan Fund Morgan Grenfell — Still to be launched.

4. Pak Growth Fund.

5. Pak Special Situation Fund.

Other funds which have invested in shares through the stock exchange are:

1. Fidelity Investment.

2. Barring Investment.

3. Schrodder Investment.

4. G.T. Asset Management.

5. Genesis Management.

6. (Saudi) Aggad Investment Ltd.

It is estimated that almost $200 million worth of investment has come into the stock market. The deregulation measures adopted by the government, particularly with regard to removal of exchange control regulations and free transferability of foreign currency, have been the main sources of confidence to foreign investors.

The policy of free market economy has been applied to the entire monetary system, and the government, which was hitherto a privileged borrower, has now started auctioning of government bonds at market rates. Secondary markets are gradually beginning to develop, and along with the other instruments, like Bearer Dollar Certificates, bond trading will also become a source of considerable activity on the stock exchanges.

On the deregulation side, the government has also allowed free pricing of issues and has removed restrictions on the issue of shares at premium, subject to certain parameters and broad guide-lines. These are necessary until the market is sophisticated enough to analyze this concept rationally.

The effect of these measures on the Stock Exchange has been tremendous, as is evident from the following table:

Table C
PROGRESS AS ON 31-08-1992

	1-1-1992 to 31-08-1992	1-1-1991 to 31-12-1991	1-1-1990 to 31-12-1990
1. No. of Companies Listed	616	542	487
2. Listed Capital	Rs. *54.308 bn.	Rs. *37.024 bn.	Rs. *28.056 bn.
	US $2.172 bn.	US $ 1.481 bn.	US $ 1.282 bn.
3. Market Capitalization	Rs. 181.729 bn.	Rs. 189.500 bn.	Rs. 61.750 bn.
	US $ 7.269 bn.	US $ 7.580 bn.	US $ 2.822 bn.
4. KSE-100 Index (Base 1-11-1991)	1148.87	1672.78	1572
5. No. of New Companies Listed	74	61	49
6. New Capital Listed at face value	Rs. 12.491 bn.	Rs. 5.297 bn.	Rs. 4.048 bn.
7. AMOUNT OF FUND MOBILIZED			
7.1.	New Issues	New Issues	New Issues
a. No. of Companies Listed	74	61	49
b. Capital offered to general public including NIT at par	Rs. 4.689 bn.	Rs. 2.402 bn.	Rs. 1.877 bn.
Premium amount	Rs. 2.543 bn.		
	Rs. 7.232 bn.		
c. Subscription received	Rs. 20.125 bn.	Rs. 15.206 bn.	Rs. 13.724 bn.
7.2.	Right Issue	Right Issue	Right Issue
a. No. of Companies offered right	74	35	38
b. Amount offered at par	Rs. 3.206 bn.	Rs. 1.295 bn.	Rs. 0.793 bn.
Premium amount	Rs. 1.790 bn.		
	Rs. 4.996 bn.		
8. TURNOVER			
a. Total Turnover of shares in million	468.794	616.892	255.397
b. Average daily turnover in Million.	2.9	2.6	1.1

* These figures also include stock dividends and the effect of conversion of debts into equity, which do not form part of mobilization of capital. We have taken the figures at par although there are certain issues which were offered at premium.

The Karachi Stock Exchange peaked to a market index of 1706 on 7/1/1992 within a period of less than 12 months. It has come down by about 30 percent since then. This decline should not be considered a collapse, on the contrary, it is a corrective measure of the over-heating that had taken place due to over-estimation of foreign investors activity by local investors. It may be pertinent to point out that increased listing and trade volumes led to tremendous growth in the number of small shareholder participants in the stock market activities. In my opinion, the number of such investors has increased almost threefold, and could today be estimated at around 1.5 million.

The fundamentals of the Pakistan economy are strong and there are plenty of opportunities to share in the development of our country for both local and foreign investors.

The outburst in pricing and trading volumes, no doubt, created certain problems for the exchange, particularly relating to physical handling of shares. The Corporate Law Authority and the stock exchanges have acted very quickly to correct these issues and have already made certain changes and programmed many others. The most important of these is the setting-up of the central depository system, for study of which our team has already visited Sri Lanka in the middle of this year. We are examining various other possibilities. God willing, we will be able to set up the central depository system quite soon to ease the problems of investors and gear the market for more efficient service. A company — "Central Depository Company of Pakistan Ltd." — is being incorporated with the following pattern of shareholding:

Karachi Stock Exchange	30 percent
Citibank	20 percent
International Finance Corporation	10 percent
Muslim Commercial Bank Limited	10 percent
Lahore Stock Exchange	5 percent
Investment Corporation of Pakistan	5 percent
Pakistan Industrial Credit & Investment Corporation	5 percent
Habib Bank Limited	5 percent
Islamabad Stock Exchange	5 percent

Studies for further facilities for clearing and settlement of securities have been carried out through the courtesy of ADB and IFC.

With the clearing system (already in operation) and the establishment of the CDS, the next move will be toward computerized trading.

The KSE has also established information network outlets to facilitate local and foreign investors. KSE trading information, apart from being transmitted to Lahore and Islamabad, is also on Reuter.

The KSE also proposes to come out with detailed company analysis useful to investors. A Computerized Research Cell has been set up and is in the process of compiling data.

On the regulatory and legislative side, the CLA, stock exchanges, and others concerned have been asked to give their recommendations on the Companies Ordinance 1984 and the SEAP Ordinance.

All these changes should lead to increased investor confidence and better and more sophisticated services by brokers.

SBP INDEX

DATE	SBP INDEX BASE YEAR 1980-81=100	DATE	SBP INDEX BASE YEAR 1980-81=100
02-1-1991	308.05	01-1-1992	798.41
30-1-1991	310.16	29-1-1992	731.74
27-2-1991	317.28	26-2-1992	672.06
27-3-1991	324.57	31-3-1992	712.78
30-4-1991	369.36	29-4-1992	742.76
29-5-1991	383.67	27-5-1992	749.86
26-6-1991	387.67	25-6-1992	762.46
		(Base year 1990-91 = 100)	
31-7-1991	474.32	30-7-1992	166.57
28-8-1991	486.80	27-8-1992	156.99
25-9-1991	183.78	03-9-1992	154.25
30-10-1991	499.10		
27-11-1991	613.43		
24-12-1991	718.17		

(1980-81 = 100)

30-7-1992	673.75
27-8-1992	635.01
03-9-1992	623.92

KSE INDEX

DATE	KSE-50 INDEX 1982	DATE	KSE-100 INDEX 1-11-1991
01-1 1991	1580	30-12-1991	1672.78
30-1-1991	1562	01-1-1992	1685.51
27-2-1991	1548	29-1-1992	1395.74
31-3-1991	1582	29-2-1992	1252.63
30-4-1991	1737	31-3-1992	1269.05
30-5-1991	1772	29-4-1992	1462.19
30-6-1991	1855	31-5-1992	1487.17
30-7-1991	2226	29-6-1992	1545.01
28-8-1991	2212	30-7-1992	1311.30
30-9-1991	2187	31-8-1992	1177.67
30-10-1991	2269	13-9-1992	1150.34
30-11-1991	2958		

Annexure-I (A)

Year Dec	No of Listed Cos	Listed Capital	Market Capitalisation Pak Rs	US$	SBP Index Base year 1980-81=100	KSE-50 Index base 1982	Annual Turnover Qnty. in Million	Value Pak Rs. in billion	US$ in bill.
1980	314	7,630.200	6,360 900	—	168.64*	—	25.785	—	—
1985	362				166.65	—	69.942	2 826	—
1987	378	16,889 800	38,646.800	—	228.39	1429	157.298	7.162	—
1988	403	18,161 800	43,530.200	—	262 67	1554	169.263	7.622	—
1989	438	22,521 900	52,785 600	2466.78	277.28	1570	214.572	9.325	.436
1990	487	28,056 200	61,750 300	2,822.5	308.53	1572	255.397	17.211	.787
1991	542	37,042 300	189,518 300	7,580.7	749.41	1672.78***	616.892	55.842	2.234
31-8-1992	616	54,307.851	181,728 747	7,269.1	** 154.25	1148.87***	468.794	59.349	2.374

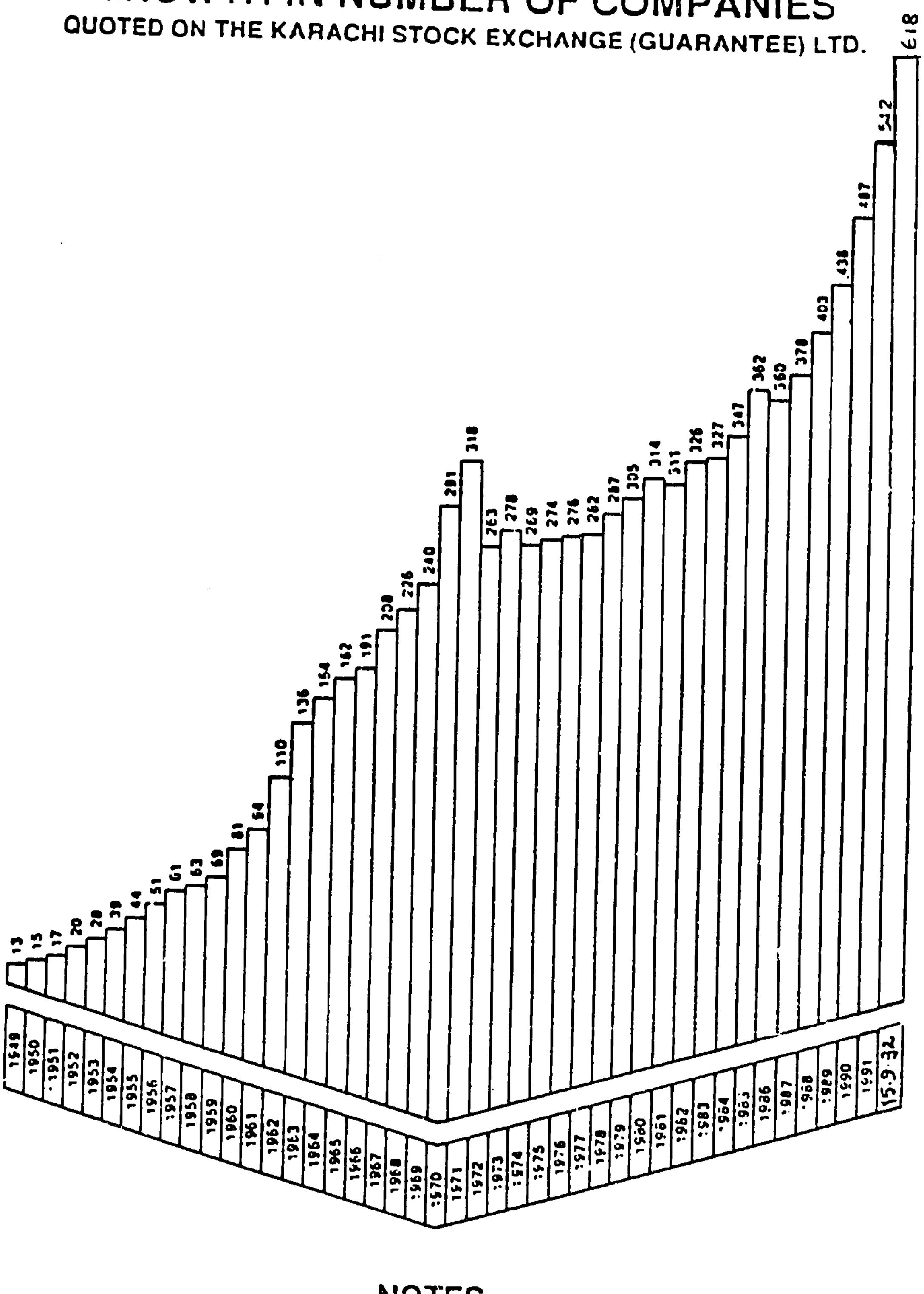
* Base year 1969-1970=100

** Base year changed to
1990-91=100
1980-81=623 92

*** KSE-50 Index changed
to KSE-100 from 1.11.1991
30-11-1991 KSE Index 50 = 2958
31-12-1992 —Do— = 3446
31-08-1992 —Do— = 2903

GROWTH IN NUMBER OF COMPANIES

QUOTED ON THE KARACHI STOCK EXCHANGE (GUARANTEE) LTD.



NOTES

The 60 Companies registered in East Pakistan (Bangladesh) have been excluded from 1972. The 12 Banks nationalised in 1974 have been excluded from 1972 bave been excluded from 1974. M/s. Attock Oil Co. Ltd. & Northern Foundry and Engg. Works Ltd. have been excluded from 1976. M/s Pakistan National Oil, Premier Oil and G.T. Surgical Ltd. have been excluded from 1977. M/s Gull Shipping, Pakistan Shipping Lines, Chittagong Steamship and Mohammadi Steamship Company have been excluded from 1978. M/s. Isakhel Estate Farms have been excluded from 1979. NSC & PSC merged into P.N.S.C. in 1980. M/s Allied Tex., Baluchistan Tex., Ferozsultan Ind., Automotive Equipment, Chemphar Pakistan Business Men's Ins., Arag Ind., and Twin Tower Modaraba have been excluded from 1983. M/s. Multan Electric and Rawalpindi Electric have been Excluded from 1985. M/s. Alsar Tex., Allied Paper Bawany Ind., Fakir Spinning, H. Sh. Mohammad Hussain & Khairpur Tex., Kohinoor Cotton, Madina Tex., Panjab Cotton, Zeenat Tex., and Paintex Ltd. have been excluded from 1986. M/s. Olympia Blended Fibre have been excluded from the above report from 1988. M/s. Lipton (Pakistan) Ltd. M/s. Sui Gas Transmission Company Ltd., and P. Lerner & Sons Chemicals Ltd. have been excluded from 1989.

On Account of delisting, M/s. Olympia Blended Fibre Mills Ltd. have been excluded from 1988 and M/s. Chemicals Ltd. M/s. National Match Factory Ltd. M/s. Pakistan Paper Corporation Ltd. M/s. Ghafur Textile Mills Ltd. M/s. Sailee Development Corporation Ltd. and Panjdarya Ltd., have been excluded from 1991 in the above report. During 1988, the Capital of M/s. Bankers Equity Limited was reduced from Rs. 10,339.20 lacs to Rs. 3,339.20 lacs.

TURN-OVER OF SHARES
(1 9 9 2)

JANUARY	...	8,35,05,550
FEBRUARY	...	5,43,74,575
MARCH	...	4,25,53,615
APRIL	...	4,82,13,715
MAY	...	5,93,33,340
JUNE	...	4,98,03,290
JULY	...	6,61,29,680
AUGUST	...	6,48,84,360
		46,87,98,125

MONTH	1987	1988	1989	1990	1991
JANUARY	1,67,88,760	1,96,98,375	1,90,24,740	3,42,54,680	28,760,120
FEBRUARY	1,91,87,730	1,96,20,655	1,80,72,760	1,87,58,340	26,339,980
MARCH	1,21,72,820	2,01,90,210	1,80,04,300	2,01,91,700	42,792,570
APRIL	1,28,37,540	1,46,84,185	1,59,37,570	1,75,21,015	62,598,530
MAY	1,03,36,205	1,14,28,445	1,45,18,180	1,40,03,440	41,779,945
JUNE	98,37,970	1,34,27,805	1,69,38,825	1,95,58,040	27,523,030
JULY	96,63,585	86,15,525	1,78,54,300	2,63,25,745	75,950,415
AUGUST	1,28,38,550	1,62,22,610	2,04,26,185	1,91,16,690	58,898,315
SEPTEMBER	1,69,94,555	1,03,95,450	1,98,20,640	2,01,36,060	45,586,785
OCTOBER	1,28,31,635	1,05,53,160	1,84,60,950	1,66,84,555	46,709,895
NOVEMBER	1,14,12,530	76,90,340	1,93,01,080	2,41,62,320	73,737,900
DECEMBER	1,23,96,670	1,67,36,265	1,62,12,780	2,48,84,120	86,236,750
TOTAL	15,72,98,550	16,92,63,025	21,45,71,710	25,53,96,705	616,892,235

▲ IN READY SECTION

▼ IN CLEARED LIST SECTION

JANUARY	2,84,61,200	2,16,97,200	38,29,800	37,45,400	57,80,700
FEBRUARY	1,65,27,500	2,29,32,100	25,05,400	35,68,900	22,05,700
MARCH	1,1[illegible]1,900	1,44,03,100	45,04,800	20,15,400	27,78,200
APRIL	1,75,[illegible]6,700	1,10,20,400	25,37,300	6,10,700	17,37,400
MAY	74,94,100	1,25,73,800	22,22,200	24,79,300	4,60,300
JUNE	2,30,10,900	2,09,85,800	27,63,200	31,49,100	3,63,700
JULY	1,06,40,300	39,14,800	17,92,200	14,58,900	45,000
AUGUST	91,89,100	40,29,100	13,10,300	1,89,99,500	-
SEPTEMBER	1,73,60,400	38,33,600	98,44,200	2,74,26,100	-
OCTOBER	68,65,500	29,69,100	94,65,200	1,74,19,200	-
NOVEMBER	1,05,10,300	37,68,600	1,26,49,500	58,41,600	-
DECEMBER	1,45,85,600	64,59,500	65,52,200	69,89,700	-
TOTAL	17,39,93,500	12,85,87,100	5,99,76,300	9,36,76,800	1,33,71,000

K.S.E. LISTED COMPANIES in 1990.

(in millions)

GROUP	No. of Cos.	REVENUES	TAX	NET PROFIT	F.Asset/ Invest.	NET WORTH	P-E	1990 EPS	YIELD %
MUTUAL FUNDS	22	159	0	134.7	604	595	7.37	2.49	9.90
MODARABA COMPANIES	24	1139	0	155.6	1,491	925	11.59	1.62	20.40
LEASING COMPANIES	9	1,060	0	229.0	2,551	756	5.14	6.25	23.89
BANKS	8	7,206	98.5	284.2	7,607	3,046	15.68	3.06	11.69
INSURANCE	30	2,211	81.2	257.5	1,700	1,551	9.27	4.99	8.23
TEXTILE SPINNING	115	23,510	41.5	944.8	13,072	5,296	11.68	2.94	5.43
TEXTILE WEAVING	12	1,492	9.5	20.2	1,375	648	30.87	0.55	1.66
TEXTILE COMPOSITE	29	13,125	135.3	240.9	5,902	2,903	8.31	4.67	9.75
WOOLLEN INDUSTRY	8	717	13.9	8.5	256	78	7.48	0.62	1.83
SYNTHETIC & RAYON	14	3,357	36.5	290.4	1,620	2,250	7.20	5.47	7.65
JUTE INDUSTRY	9	2,203	31.7	52.2	1,000	493	5.47	1.00	2.97
SUGAR & ALLIED	30	12,309	419.7	666.9	5,388	3,495	5.29	4.30	9.15
CEMENT INDUSTRY	10	4,700	177.4	93.6	3,372	1,723	4.14	1.06	4.78
TOBACCO	7	11,994	88.7	141.2	578	676	NM	(0.51)	8.03
FUEL & ENERGY	11	67,007	1,149.0	1,530.0	25,245	10,770	8.67	5.06	13.98
ENGINEERING	15	4,308	31.4	(63.3)	1,744	505	NM	(0.93)	1.36
AUTO & ALLIED	18	13,106	222.9	351.8	159	1,701	5.11	3.95	7.00
CABLE & ELECTRIC.	14	4,520	94.4	78.1	675	835	14.11	1.19	10.09
TRANSPORT & COMM.	3	19,843	395.0	77.3	10,412	8,544	10.78	0.24	0
CHEMICAL & PHARMA.	34	15,522	678.6	897.6	3,450	3,896	10.15	4.71	7.64
PAPER & BOARD	13	2,841	114.0	154.2	1,702	957	4.73	2.79	6.69
VANASPATI & ALLIED	16	6,237	54.1	21.5	219	275	NM	(0.77)	5.07
CONSTRUCTION	4	30	0	(7.1)	57	7	10.40	0.30	0
LEATHER & TANN.	6	3,311	47.5	77.[illegible]	672	693	10.97	3.00	6.74
FOOD & ALLIED	18	9,060	319.0	330.4	1,173	1,007	15.18	5.96	12.14
GLASS & CERAMICS	8	709	35.9	34.1	649	339	6.27	0.77	4.08
MISCELLANEOUS	20	3,003	42.7	42.9	879	667	7.90	1.30	9.70
1990 Total (27 Groups Average:	515	230,807	4,267.9	7,060.8	87,709	55,121	9.75	2.51	7.82

NOTES:

1. The above is cosolidated statement of the individual Industry Studies.
2. Price Earning Ratios are on various dates, and Average is for 24 Groups only.
3. In Pak Rupees.

FIRST INTERFUND MODARABA

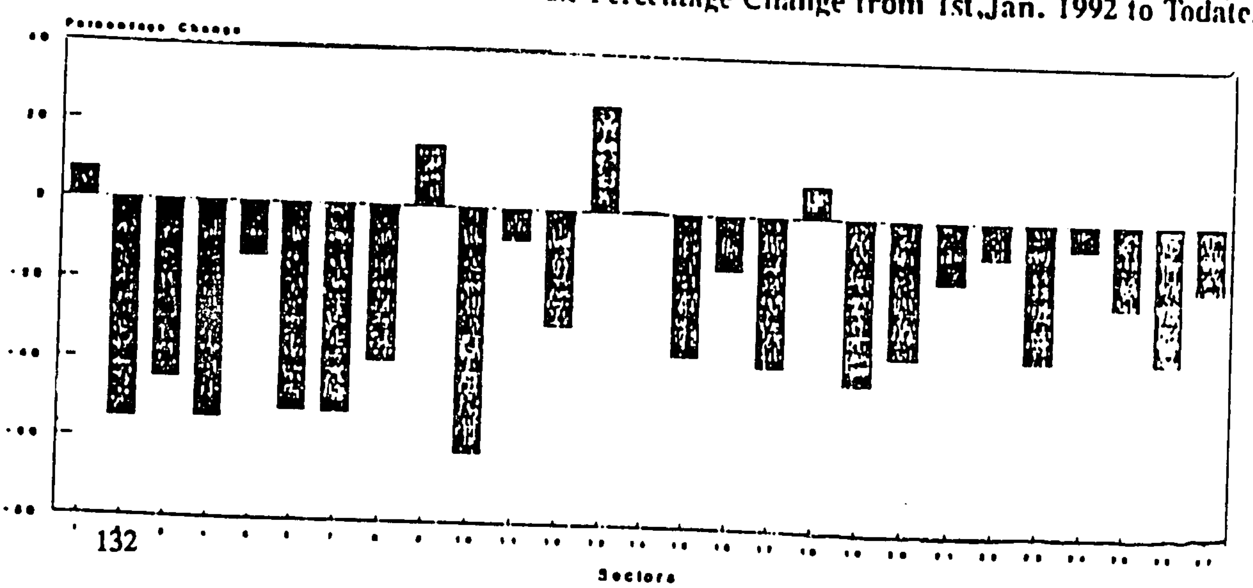
Sector Wise Index

Sept-23, 1992

Sector Name	Issued Capital	Market Capitalization	Last Week Index Sep 9	This Week Index Sep 17	Absolute Change	Percentage Change
1 MUTUAL FUNDS	700,000,000	2,297,800,000	13,077.35	12,922.75	(149.60)	(1.14)DOWN
2 MODARABA COMPANIES	4,124,361,999	4,850,250,148	7,197.03	6,520.40	(676.63)	(9.40)DOWN
3 LEASING	1,112,286,560	2,845,767,976	11,027.35	10,239.13	(788.22)	(7.15)DOWN
4 INVESTMENT COMPANIES/BANKS	5,125,271,700	13,804,982,695	18,016.26	16,875.27	(1,140.99)	(6.33)DOWN
5 INSURANCE	628,094,944	3,793,858,522	6,582.94	6,424.07	(158.87)	(2.41)DOWN
6 TEXTILE SPINNING	8,061,084,475	13,328,101,316	7,574.06	6,919.55	(654.51)	(8.64)DOWN
7 TEXTILE WEAVING	1,776,733,000	1,467,593,940	4,977.00	4,575.46	(396.54)	(7.98)DOWN
8 TEXTILE COMPOSITE	2,680,479,184	8,432,044,807	13,305.69	12,346.81	(958.88)	(7.21)DOWN
9 WOOLEN	166,236,490	334,378,467	16,914.37	16,340.07	(574.30)	(3.40)DOWN
10 SYNTHETIC & RAYON	2,799,743,410	9,663,389,221	40,303.53	39,085.63	(1,217.90)	(3.02)DOWN
11 JUTE	442,636,310	841,614,227	15,492.30	15,205.65	(286.65)	(1.85)DOWN
12 SUGAR & ALLIED INDUSTRIES	2,810,608,140	6,959,105,010	8,862.46	8,587.13	(275.33)	(3.11)DOWN
13 CEMENT	1,409,026,000	5,412,100,775	16,108.31	15,394.26	(714.05)	(4.43)DOWN
14 TOBACCO	504,792,410	1,340,029,887	12,506.18	12,239.22	(266.96)	(2.13)DOWN
15 FUEL & ENERGY	4,338,901,680	25,875,995,819	23,655.95	22,386.36	(1,269.59)	(5.37)DOWN
16 ENGINEERING	807,755,870	1,479,841,528	10,908.46	10,577.78	(330.68)	(3.03)DOWN
17 AUTO & ALLIED ENGINEERING	1,988,588,150	6,599,595,283	16,308.51	15,812.79	(495.72)	(3.04)DOWN
18 CABLES & ELECTRICAL GOODS	555,830,156	2,773,232,283	19,253.86	18,657.85	(596.01)	(3.10)DOWN
19 TRANSPORT & COMMUNICATION	4,121,333,000	6,968,726,515	15,674.58	14,317.50	(1,357.08)	(8.66)DOWN
20 CHEMICALS & PHARMACEUTICALS	4,865,228,960	29,817,758,701	14,647.90	14,085.28	(562.62)	(3.84)DOWN
21 PAPER & BOARD	766,083,215	3,169,853,783	20,475.08	20,324.02	(151.06)	(0.74)DOWN
22 VANASPATI & ALLIED	239,163,590	597,009,793	10,104.16	9,941.22	(162.94)	(1.61)DOWN
23 CONSTRUCTION	116,375,000	61,991,625	7,587.58	6,860.69	(726.89)	(9.58)DOWN
24 LEATHER & TANNERIES	255,317,692	1,496,119,928	13,188.34	13,045.05	(143.29)	(1.09)DOWN
25 FOOD & ALLIED	1,121,890,936	10,677,651,342	47,032.26	45,778.27	(1,253.99)	(2.67)DOWN
26 GLASS & CERAMICS	514,804,250	757,856,965	8,634.55	8,535.74	(98.81)	(1.14)DOWN
27 MISCELLANEOUS	982,732,010	2,136,156,803	17,485.97	17,150.44	(335.53)	(1.92)DOWN
	52,515,359,131	167,757,809,359				

Source: First Interfund Modaraba. Research Department.

Graphic Overview of Sector Wise Percentage Change from 1st.Jan. 1992 to Todate.



Sl No.	Name of Company	Profit Before Tax (Rs. in Mn)	Year Ending	Per Share Rs Pre-Tax Earning	Div. %	Bonus %	Total %
1.	Kohinoor Spinning Mills Ltd	31.321	30.9.88	48.186	200	-	200
2.	Crescent Sugar Mills & Distillery Ltd	99.783	30.9.88	38.995	50	25	75
3.	Universal Leather & Footwear Ind. Ltd	26.293	30.6.88	36.583	50	-	50
4.	Sapphire Textile Mills Ltd	88.659	30.9.88	36.187	85	-	85
5.	Ayesha Textile Mills Ltd	12.448	30.9.88	35.567	70	-	70
6.	Husein Sugar Mills Ltd	61.551	30.9.88	30.593	52.50	29.23	81.73
7.	Dewan Textile Mills Ltd	97.933	30.9.88	29.677	32.50	20	52.50
8.	Quetta Textile Mills Ltd	31.105	30.9.88	25.921	27.50	25	52.50
9.	Fateh Textile Mills Ltd	32.074	30.9.88	25.659	50	-	50
10.	Gulistan Textile Mills Ltd	45.317	30.9.88	24.208	25	25	50
11.	Crescent Textile Mills Ltd	113.295	30.9.88	21.680	57.50	-	57.50
12.	Shakarganj Mills Ltd	106.405	30.9.88	21.281	55	-	55
13.	Central Insurance Co. Ltd	23.094	31.12.88	20.994	40	14	54
14.	Pakistan State Oil Co. Ltd	343.973	30.6.88	20.138	40	10	50
15.	Ittefaq Textile Mills Ltd	42.372	30.9.88	18.685	75	-	75
16.	Shahtaj Sugar Mills Ltd	66.454	30.9.88	18.615	25	25	50
17.	Burshane (Pakistan) Ltd	24.168	30.6.88	17.754	50	50	100
18.	The Thal Industries Corporation Ltd	52.675	30.9.88	17.671	55	-	55
19.	International General Ins. Company of Pakistan Ltd	24.228	31.12.88	16.315	30	20	50
20.	Associated Industries Ltd	13.241	30.6.88	15.728	65	-	65
21.	Brooke Bond Pakistan Ltd	62.673	31.12.88	14.922	30	20	50
22.	Wazir Ali Industries Ltd	25.715	30.6.88	14.843	60	-	60
23.	Lever Brothers Pakistan Ltd	277.004	31.12.88	14.377	45	33.33	78.33
24.	Pakistan Oilfields Ltd	341.542	31.12.88	14.034	50	-	50
25.	Exxon Chemical Pakistan Ltd	190.162	31.12.88	12.698	70	20	90

ANNEXURE - IIIA

Sl No.	Name of Company	Profit Before Tax (Rs. in Mn)	Year Ending	Pre-Tax Earning Per Share	Distribution Div. %	Distribution Bonus %	Distribution Total %
1.	Associated Industries Ltd.	52.982	30.06.89	62.934	110	-	110
2.	Exide Pakistan Ltd.	33.234	31.03.89	13.527	45	10	55
3.	Millat Tractors Ltd.	111.819	30.06.89	24.124	45	10	55
4.	Singer Pakistan Ltd.	25.970	31.12.89	13.920	35	50	85
5.	Eastern Federal Union Ins.Co.Ltd.	17.453	31.12.89	17.452	10	100	110
6.	Universal Leather & Footwear Ind.Ltd.	21.111	30.06.89	14.686	25	100	125
7.	Pakistan Industrial Credit & Invesment Corporation Ltd.	198.127	31.12.89	12.133	25	20	45
8.	The Premier Sugar Mills & Distillery Co. Ltd.	159.670	30.09.89	42.578	50	-	50
9.	Pakistan Refinery Ltd.	164.210	30.06.89	27.368	30	50	80
10.	Dewan Textile Mills Ltd.	99.425	30.90.89	25.107	87½	-	87½
11.	Ayesha Textile Mills Ltd.	13.159	30.09.89	37.596	55	-	55
12.	Lever Brothers Pak. Ltd.	374.370	31.12.89	14.572	50	33.33	83.33
13.	Quetta Textile Mills Ltd.	34.184	30.09.89	22.789	30	33.33	63.33
14.	The Burewala Textile Mills Ltd.	82.445	30.09.89	22.127	70	-	70
15.	Sapphire Textile Mills Ltd.	60.530	30.09.89	24.706	65	-	65
16.	Grays of Cambridge (Pakistan)Ltd.	6.720	31.12.89	9.001	47½	-	47½
17.	Exxon Chemical Pak. Ltd.	243.471	31.12.89	16.257	80	-	80
18.	Fateh Textile Mills Ltd.	32.842	30.09.89	26.273	55	-	55
19.	Pakistan Oilfields Ltd.	273.171	31.12.89	11.224	90	-	90
20.	Kakakhel Industries Ltd.	22.907	30.06.89	18.325	62½	-	62½
21.	International General Ins. Co.of Pak. Ltd.	23.873	31.12.89	13.397	30	25	55
22.	Wazir Ali Industries Ltd.	36.546	30.06.89	21.094	60	-	60
23.	Dilon Limited.	28.287	31.12.89	22.479	50	-	50
24.	Brooke Bond Pakistan Ltd.	88.015	31.12.89	17.463	52½	-	52½
25.	The Prince Glass Works Ltd.	31.795	31.12.89	16.526	60	-	60

) Converted into Rs. 10/- per share.

LIST OF 25 TOP COMPANIES FOR THE YEAR 1990

Sl No	Name of Company	Profit Before Tax (Rs. in Mn)	Year Ending	Pre-Tax Earning Per Share Rs	DISTRIBUTION		
					Div. %	Bonus %	Total %
01.	Associated Industries Limited	48.637	June	57.770	110	–	110
02.	The General Tyre and Rubber Company of Pakistan Limited.	113.513	Dec.	21.935	55	–	55
03.	National Development Leasing Corporation Limited	116.474	Dec.	17.133	20	33.33	53.3
04.	Exide Pakistan Limited	44.955	March	16.635	60	25	85
05.	The Prince Glass Works Limited	42.058	Dec.	21.861	80	–	80
06.	Engro Chemical Pakistan Limited	228.800	Dec.	15.278	90	–	90
07.	Dewan Khalid Textile Mills Limited	43.727	Sep.	20.244	62.50	–	62.5
08.	Grays of Cambridge (Pakistan) Limited	14.634	Dec.	19.601	60	–	60
09.	Fazal Vegetable Ghee Mills Limited	11.224	June	25.509	50	–	50
10.	The Burewala Textile Mills limited	68.797	Sep.	18.464	60	–	60
11.	The Premier Sugar Mills & Distillery Company Limited	102.609	Sep.	27.363	40	–	40
12.	Kakakhel Industries Limited	18.524	June	14.819	62.50	–	62.5
13.	Habib Sugar Mills Limited	127.463	Sep.	15.174	52.50	–	52.5
14	Nafees Cotton Mills Limited	13.531	Sep.	8.990	–	70	70
15.	Pakistan Refinery Limited	113.561	June	12.618	30	33.33	63.3
16.	Pakistan Burmah Shell Limited	149.428	Dec.	13.862	45	14.29	59.2
17.	Brooke Bond Pakistan Limited	61.347	Dec.	12.172	50	10	60
18.	Pakistan State Oil Company Limited	364.487	June	17.635	40	10	50
19.	Burshane (Pakistan) Limited	24.421	June	11.960	50	10	60
20.	Bawany Sugar Mills Limited	81.386	Sep.	20.347	32.50	10	42.5
21.	Husein Sugar mills limited	49.410	Sep.	16.470	20	25	45
22.	Dawood Cotton Mills Limited	54.312	Sep.	10.918	60	–	60
23.	The Thal Industries Corporation Ltd.	57.643	Sep.	16.115	25	25	50
24.	Sunshine Cotton Mills Limited	25.586	Sep.	11.230	25	30	55
25.	International General Insurance Company of Pakistan Limited	23.097	Dec.	10.369	30	25	55

THE REGULATORY ENVIRONMENT IN PAKISTAN

by

M. Javed Panni
Chief (Securities), Corporate Law Authority
Islamabad, Pakistan

The major legislation which governs regulation of the corporate sector in Pakistan is:

1. Capital Issues (Continuance of Control) Act 1947
2. Companies Ordinance 1984
3. Securities & Exchange Ordinance 1969
4. The Monopolies and Restrictive Trade Practices (Control and Prevention) Ordinance 1970
5. Modaraba Companies and Modarabas (Floatation and Control) Ordinance 1980
6. Investment Companies and Investment Advisers Rules 1971.

The Regulating agency for the corporate sector and the securities market is the Corporate Law Authority (CLA). The major regulatory functions under these laws are as follows.

CAPITAL ISSUES (CONTINUANCE OF CONTROL) ACT, 1947

The control on issue of capital is designed to secure a balanced investment of the country's resources. This enactment is, therefore, used amongst other things, to broad base the equity of the company to prevent public participation in premature projects, over-capitalization and undue dependence on loan capital. Companies which are to have capital of less than 100 million rupees do not require permission to issue capital. Companies desiring to have issued capital of over 100 million rupees are required to obtain the consent of the Controller of Capital Issues. These companies are also required to go public and be listed on a stock exchange. The companies are required to offer at least 50 percent of the total capital to the general public including the National Investment Trust (15 percent). This is done for the purpose of broad basing the capital. Similarly, listed public companies are to obtain permission for the issue of rights shares to the existing shareholders. The Act is also used for specifying other conditions at the time of the issue of capital in order to achieve the objectives of the Law. The Capital Issues Act also prescribes obtaining the permission for:

(a) Public offer of sale of securities by the promoters/principal shareholders.
(b) Company desiring to offer capital to public having capital of less than 100 million rupees.

The Act lays down restrictions on remuneration of directors of companies (listed as well as unlisted) which show a loss for 3 years or more. It also regulates the issue of bonus shares with minimum reserve requirements.

COMPANIES ORDINANCE, 1984

The purpose of this Ordinance is to regulate the formation, working and winding up of companies. For regulation of listed companies, it provides major provisions with regard to:

1. Preparation of annual accounts within six months of the close of the accounting period and submission to the shareholders, the stock exchange(s) and CLA;
2. Holding of an annual general meeting of the shareholders within six months of the closing of the annual accounting period;
3. Preparation of half-yearly accounts within two months of the closing period and submission to the shareholders, the stock exchange(s) and CLA;
4. Filing with CLA beneficial ownership returns of shareholdings by the officers and principal shareholders of the company and reporting of changes therein;
5. Tendering of profits to the companies made by insiders by trading within a six month period;
6. Payment of dividend within 45 days of declaration;

7. Free transferability of shares.

SECURITIES AND EXCHANGE ORDINANCE, 1969

For regulating the stock market, protecting the interests of investors, and regulating dealings in securities, the Securities and Exchange Ordinance was enacted in 1969. The main functions of the Corporate Law Authority under this Law are:

(A) Registration of stock exchanges.
(B) Prescribing books of accounts to be maintained by Stock Exchanges as well as submission of annual reports.
(C) Listing of securities on stock exchanges.
(D) Enforcement of prohibition/restriction on stockbrokers as well as investors.
(E) Investigation into the affairs of stock exchanges and transaction on stock exchanges.
(F) Prescribing qualifications of the members of stock exchanges.
(G) Prescribing the manner of transaction of stock broker's business.
(H) Maintenance of books of accounts by the stock brokers.
(I) Regulation of business of Investment Advisers and Investment Companies (closed end mutual funds).

The regulations for functioning of stock exchanges are framed by the stock exchanges under the Securities and Exchange Ordinance. The stock exchanges ensure that listed companies are in compliance with listing regulations. Listing regulations of the stock exchanges lay down specific conditions for listing.

MONOPOLIES AND RESTRICTIVE TRADE PRACTICES (CONTROL AND PREVENTION) ORDINANCE, 1970

In addition to regulating the securities market, other areas are regulated by the Corporate Law Authority. The foremost law administered in this connection is the Monopolies and Restrictive Trade Practices (Control and Prevention) Ordinance, 1970. The promulgation of this law was necessitated as a result of the following of policies of economic development through the private enterprise system and the efforts to keep the balance between the objective of rapid capital formation and economic development on the one hand and of social justice and consumer protection on the other. The apparent conflict between the two aims had to be achieved through governmental regulations. In the present era it has become all the more necessary that a synthesis be evolved between rapid capital formation and economic development and social justice and consumer protection. The broad objective of the legislation is to provide for measures against undue concentration of economic power, monopoly power and restrictive trade practices. The law spells out the situation which shall be deemed to constitute undue concentration of economic power, unreasonable monopoly power and unreasonably restrictive trade practices. The scheme of the law is to prohibit these clearly defined situations and to collect information through the process of registration about these and other circumstances which are likely to lead to such situations.

MODARABA COMPANIES AND MODARABAS (FLOATATION AND CONTROL) ORDINANCE, 1980

Modaraba is an Islamic instrument which is a mutual fund for investing in any type of business including stocks. The Modaraba ordinance provides for a strict control over Modarabas. There are a number of authorities which control Modarabas and regulate them. The most important of them is, of course, the Registrar, who is responsible for registering the Modaraba management company and ensuring that the

Modaraba follows the rules and regulations prescribed by the law. The other authority is the Religious Board, which scrutinizes all Modaraba applications to ensure that no un-Islamic business is carried out by a Modaraba or a business which is against the tenets of Islam. To achieve this, it periodically examines the managerial policies and also prescribes the forms of lease agreement, Musharka agreement, etc. The Corporate Law Authority on its own also examines the Modaraba in the light of the prevailing economic situation and issues guidelines which are to be followed. For this purpose regular inspection of the Modarabas are carried out and the Modaraba management companies are to answer for any irregularities.

Recently the State Bank of Pakistan has been authorized to regulate non-banking financial institutions (NBFIs) and it has issued its prudential regulations which will cover all financial activities and for which all companies, whether Housing Companies, Modaraba Companies, Leasing Companies or DFIs, would all answer to the State Bank for their financial transactions.

CORPORATE LAW AUTHORITY

The overall regulatory control rests with the Corporate Law Authority. Its headquarters is at Islamabad with two main offices at Lahore and Karachi and branch offices at Peshawar, Quetta, Islamabad, Multan and Faisalabad. The main wings of the Corporate Law Authority are:

1. Corporate Regulation Wing:
   (a) Registrar of Joint Stock Companies who administers the Companies Ordinance, 1984, and acts as a registration office.
   (b) Securities and Exchange section which administers the Securities and Exchange Ordinance and Rules framed thereunder.
   (c) Controller of Capital Issues administering the Capital Issues Act, 1947.

2. The Monopoly Control Wing:
   (a) Administers the Monopolies and Restrictive Trade Practices Ordinance.
   (b) The Investigation Wing of the Corporate Law Authority.
   (c) The Registrar of Modarabas who administers the Modarabas Ordinance.
   (d) Administration Cell of Corporate Law Authority.

3. The Technical Wing:
   (a) Computerization.
   (b) Accounting.

RECENT DEVELOPMENT OF THE INDONESIAN STOCK MARKET

Presented by

Hasan Mahmud
President/Director of the Jakarta Stock Exchange

It is indeed a great honor for me to have the opportunity to discuss the development of the Indonesian capital market in this prestigious forum.

First of all, I would like to congratulate and express my appreciation to the Securities Exchange Commission of Sri Lanka for their initiative in organizing a Conference of Stock Exchanges in the South and Southeast Asia Region. Such initiative reflects the host's far reaching view regarding the increasing role which stock exchanges in this region will play in mobilizing international funds in the days to come. It also reflects a deep understanding of the importance of cooperation and exchange of information and experience among developing stock exchanges for their further development.

The year 1992 is an important one for the development of the capital market in Indonesia, because in this year the Government took a political and economic decision to privatize the Jakarta Stock Exchange. Privatization of the Jakarta Stock Exchange is based on the confidence that a private stock exchange will be more flexible in adjusting to the rapid development of the financial market. It will also be able to lead the capital market to a higher level of efficiency. Privatization of the Jakarta Stock Exchange also reflects the Indonesian Government's intention to extend a bigger role to the private sector in the development of the nation's economy, to give more power to the market mechanism, and to focus more on the government's role as the decision maker in directing economic development while at the same time creating a conducive climate for development of the private sector.

During the first quarter following its privatization, the performance of the Jakarta Stock Exchange — though rather slow — showed a positive trend. The number of companies listed at the Jakarta Stock Exchange has increased from 141 in early 1992 to 148 last August, and about 10 more companies are expected to go public by the end of the year. During the same period, market capitalization rose from Rp 16 trillion (U.S. $8 billion) to Rp 24 trillion (U.S. $12 billion). The Composite Stock Price Index (IHSG) increased 20 percent from 247 in early 1992 to 301 at the end of August 1992, with an average daily turnover of Rp 33 billion (U.S. $16.5 billion).

The development of the capital market in Indonesia faces a major constraint in the form of a savings-investment gap. On the one hand, in order to maintain economic growth a very large investment is needed. Indonesia possesses a very large range of industries with an even larger growth potential. The industrial sector ranges from manufacturing, trading, finance, hotel and property, to agribusiness, mining and plantation. Indonesia has 7,160 domestic companies, 2,250 joint-ventures and more than 200 state-owned enterprises which will be privatized by stages. On the other hand, national savings are still very limited, as income per capita is below U.S. $600. We cannot expect people with such a low average income to become investors in the capital market.

Within the framework of such limitations, the development of the capital market in Indonesia is directed to encouraging foreign investors in the capital market and at the same time fostering the development of local investors, particularly institutional investors such as pension funds, insurance companies and investment funds.

The efforts to draw foreign portfolio investment will only be successful when supported by attractive economic prospects and an efficient capital market. In increasing capital market efficiency, especially the secondary market mechanism, the Jakarta Stock Exchange has made a strategic plan which includes, among others, efforts to:

a. Increase market integrity by way of amending regulations, creating monitoring and surveillance systems, and developing the professionalism of stock exchange members.

b. Improve market transparency to provide better access for investors through automation of information dissemination, clearing, settlement, and trading, and developing accounting and reporting standards for issuers and stock exchange members.

c. Raise market liquidity by introducing additional instruments by developing the derivative market and creating derivative instruments which shorten the settlement period.

Finally, allow me to conclude with a few encouraging words for this forum. Globalization of the capital market has caused capital as a factor of production to become more mobile than goods and services. The heightened constraints on international funds on the one side, and the increase of emerging markets on the other, has caused fierce competition for such international funds. It is in this relation that cooperation among emerging markets will prove most fruitful if we support each other in increasing the efficiency of our respective capital markets. This will enable us to play a more decisive role in the economic development of our own countries.

SECTION 3

COUNTRY PAPERS CIRCULATED

THE DEVELOPMENT OF THE JAKARTA STOCK EXCHANGE BEFORE AND AFTER PRIVATIZATION

by

The Jakarta Stock Exchange Inc.

INDONESIA AT A GLANCE

Indonesia consists of 13,000 islands with 5 major islands namely Sumatra, Java-Bali, Kalimantan, Sulawesi and Irian Jaya. The capital city is Jakarta with a population of 8 million. It is expected that almost 60 percent of the supply of money circulates in the city of Jakarta. Nowadays, Jakarta is the most developing city in Indonesia and has the biggest population as well. The total population of Indonesia is 180 million and most of them live in rural areas and work in the agriculture sector.

THE JSE BEFORE PRIVATIZATION

The stock exchange is not a new phenomenon on Indonesian grounds. The first stock exchange dates back to 1912 when during Dutch occupation they established the Vereniging voor de Effectenhandel in Batavia, now Jakarta. Securities traded were stocks and bonds issued by Dutch companies and several American shares certificates. This exchange did not last long because of the First World War. In 1925 additional stock exchanges were opened in Surabaya and Semarang besides the one in Batavia. Again those exchanges were closed in 1942 because of World War II.

Attempts were made by the government to reactivate the stock exchange in 1950. Stock traded at that time were the ones issued by Dutch companies. This stock exchange had to be closed down again due to an unfavorable economic situation and the nationalization of Dutch companies.

With the reactivating of the capital market in 1977, the Capital Market Executive Agency (BAPEPAM), and National Investment Trust (PT DANAREKSA) were established. The Capital Market Executive Agency was established as the government entity responsible for both supervising and running the stock exchange, and a regulatory frame work was set forth. The main aim of the capital market was to mobilize funds through public participation in companies shares ownership and also to enhance equal distribution of income.

In the first few years, the stock exchange was as good as dormant, with only 23 companies listed from 1977 to 1983 with a total primary market value of Rp 40.43 million or U.S. $6.5 million. Average daily trading during this period peaked at only Rp 50.7 million or $7.7 million in 1982 (see attachment).

From 1983 to 1988 only one additional company listed shares on the exchange. And average daily trading rose at an equivalent of $145.000 (Rp 121.88 million) in 1988.

Indonesia went through a series of reforms, deregulations and policy adjustments beginning in 1983 with the complete overhaul of its tax system, customs reform, trade and tariff reform, monetary reform and relaxation in investment licensing requirements.

A series of regulations to increase activities in the capital market promulgated by the government followed by financial sector deregulation packages in 1987 and 1988 encouraged the development of the capital market:

- Listing requirements were made simpler so as to be more flexible;
- Foreigners were allowed to buy up to 49 percent of listed stocks;
- Price fluctuation is not limited;

- A boursa Parallel (OTC Market) was established;
- Time deposits became taxable just like dividends and other income from the capital market, which provide other alternatives to the investor;
- The privatization of the stock exchange;
- Banks and non-bank financial institutions became able to raise capital through the issuance of shares at the capital market.

From a sleepy institution, the Jakarta Stock Exchange came to life and in 1989 was the fastest growing stock market in the world. The number of companies listed became 57 in 1989 and rose to 138 by year end 1991. Market capitalization went up 800 percent in 1989 and reached over U.S. $20 billion in 1991.

The economic boom provided greater market liquidity in 1990 and greater wealth to the investing public. Existing regulation, however, hindered the effective development of an open, fair and orderly market. The rapid and dynamic changes in the capital market made the policy-makers aware that safety mechanisms to protect investors have to be ensured and promoting such a market is the challenge of the day. A new decree was promulgated in 1990 ensuring adequate protection for public investors. The new BAPEPAM (Capital Market Supervisory Agency) now functions as a regulatory body and the framework for privatizing the Jakarta Stock Exchange was set.

PRIVATIZATION OF THE JSE

The Jakarta Stock Exchange, Inc. was established in December 1991 and obtained its operating license from the Minister of Finance on March 18,1992. It was privatized through a sale to qualifying brokers who totally took over the management and administration of the stock exchange, previously run by BAPEPAM, on April 16,1992.

The Jakarta Stock Exchange is committed to creating an orderly, liquid, efficient, fair and transparent market for the trading of securities.

Its organizational structure consists of the Board of Commissioners, the Board of Directors and 13 Divisions. There are three Committees, namely the Securities Trading Committee, Securities Listing Committee and Membership Discipline Committee, which advise the stock exchange on related matters.

On September 1,1992 the Exchange had 185 members holding one share each, comprised of securities houses and broker-dealers companies. Some of the world's leading firms of underwriters and stockbrokers have formed joint-ventures.

The JSE's new series of rules and regulations includes:

A. Rules and Regulations regarding JSE memberships;

B. Rules and Regulations regarding Securities Listing on the JSE;

C. Rules and Regulations regarding Securities Trading.

To qualify for membership, a company shall satisfy the following requirements:

- Obtain a business license from BAPEPAM as a broker-dealer and/or underwriter;
- Hold one share of Jakarta Stock Exchange, Inc.;
- Certify not having ownership, management, or controlling relations with another member of the stock exchange;
- Appoint in writing at least one broker-dealer's representative and other personnel;
- Certify that the company is fully financially responsible for all activities performed by broker-dealers representative and/or other personnel on its behalf at the stock exchange.

Currently only companies established and domiciled in Indonesia may list their stocks or bonds on the stock exchange. Stocks and bonds listed on the stock exchange are divided into the following categories by industrial sector:

Industrial Sector		Stock	Bonds
1.	Manufacturing and Commercial	93	7
2.	Finance	34	7
3.	Hotel, Property, Real Estate & Construction	14	2
4.	Tours & Travel	2	-
5.	Mining	2	-
6.	Agribusiness & Related Products	1	-
7.	Plantation	1	-
8.	Transportation Services	3	-
	Total	150	16

Under the new rulings, companies which apply for share listing shall be required to meet the following conditions:

- The registration statement either for public offering or for public company has been declared effective by BAPEPAM;
- The company has been established and in operation for at least 3 years;
- The company's financial report has been audited by an accountant registered at BAPEPAM and has received an unqualified opinion for the latest fiscal year;

- Show operating profits and net earnings for the last two consecutive years;

- Their minimum assets are Rp 20 billion (U.S. $10 million), with minimum equity capital of Rp 7.5 billion and paid-up capital of at least Rp 2 billion;

- Market capitalization of paid-up capital of a company that has made a public offering is at least Rp 4,000,000,000. (four billion Rupiah); a public company shall have at least Rp 2,000,000,000 (two billion Rupiah) in paid-up capital.

For bond listing, the requirements which differ from those for shares are:

- The face value for bonds to be listed is at least Rp. 25,000,000,000.- (twenty-five billion Rupiah).

- The period between the declaration that the registration statement is effective and the request for listing does not exceed 6 (six) months, and maturity dates of the outstanding bonds are at least 4 (four) years.

Listing fees consist of:

- Initial listing fee of 0.05 percent (5 thousandths) of the securities listed, or at minimum Rp 10 million;

- The annual listing fee is 0.1 percent (one thousandth) of the securities listed, or at minimum Rp 10 million.

There are also rules for de-listing of companies, which is considered as the final action of the JSE regarding the default of companies which meet the criteria for de-listing.

THE MARKET

The market conditions for the months of July and August 1992 were generally characterized by the declining prices of some leading stocks. The Composite Stock Price Index (CSPI) at the end of July 1992 reached 317.186 and then it went down to 301.279 in August, which means a decrease of 5.01 percent. Market capitalization of the total listed stocks at the end of August 1992 was Rp 24.051,91 billion, increasing thus Rp 3.578,91 billion or 17.48 percent from the end of April 1992.

Average trading value per day for eight months of 1992 reached Rp 32.803,66 billion, an increase of 39.11 percent.

Average trading volume per day for eight months of 1992 reached 7.580,02 thousand shares, while in 1991 the amount was only 4.113,43 thousand shares, an increase of 84 percent.

COMPUTERIZATION OF THE JAKARTA STOCK EXCHANGE

Since the first week of September, the JSE has utilized two mini-computers HP-825, designed to assist back office transactions on the trading floor.

This computer system can reduce settlement problems, such as back log on back office administration, failure to pay and failure to deliver stocks. The system produces transaction notes and daily reports.

This system is designed to meet the rising demands on clearing of the settlements and deliveries of the stocks traded, together with the payments under the existing system and also produces a standard Stock Exchange Transaction Report (called LTAB or transaction report between JSE members). This report will be used as a monitoring device to control the failure of the settlement process and will provide the actual and accurate information.

CLEARING AND SETTLEMENT

On September 7, 1992, the Central Clearing, Settlement and Depository Body named PT Kliring Deposit Effek Indonesia (abbreviated PT KDEI) was born. At this moment the management is still waiting for its operating license from the Minister of Finance. The shareholders comprise seven government banks (majority), the JSE and the SSE (Surabaya Stock Exchange).

The operation of this institution is scheduled as follows:

- Until January 1993, the operation of "clearing" will be executed by the clearing division of JSE, Inc. At this stage settlement is carried out by brokers and they report to the clearing division of JSE, Inc. — PT KDEI only monitors the operation;

- From February 1993 to September 1993, the operation of "clearing and settlement" will be fully operated by PT KDEI. At this stage it is expected that the following shall be performed:

  — trade-netting, settlement by book-entries and money settlements;
  — introducing immobilized securities for new issuers;
  — quarantor of trade.

- In October 1993, immobilized securities shall already be actively operated. At this stage clearing, payment and settlement of securities are executed by PT KDEI.

STRATEGIC PLAN

The JSE Inc's. goal is making the market efficient, fair, orderly, economical and competitive. An efficient market is fostered by "full disclosure" of relevant information about each security, centralized matching of bids and offers, and low cost dissemination of market information.

The strategic plan to fulfill those targets are as follows:

1. Strengthen commitment of all parties involved toward the end objective;

2. Make use of expertise from outside in drafting plans and rules;

3. Build an intense relationship with potential investors, such as insurance companies, pension funds and potential issuers, public companies and investment funds;

4. Continuous research and development to find new products instruments, new services and new systems;

5. Build a better image internationally, international cooperation, public relation and publications, improvement of expertise.

FUTURE DEVELOPMENTS

1. The JSE Inc. is expected to move to the new building in March/April 1994. It is also expected that by that time the JSE Inc. has implemented the set-up toward efficient stock trading through automation and computerization, including the trading room and settlement counters, dissemination of information on the trading situation through a local area network of computers;

2. The computerized system will cover transaction and communication systems of the JSE Inc;

3. Promote the listing of stocks, bonds and other securities of prospective corporations;

4. Enhance trading on the bond market and develop new derivative products such as options, bond futures and stock index futures;

5. Upgrade the quality of underwriting and back office brokerage firms through tightening of regulations and evaluation of companies;

6. Disseminate financial statements and business information of listed companies to the public through publications and electronic communication;

7. Streamline supervision of trading, clearing and settlement procedures of securities firms;

8. Provide educational courses regarding securities market regulations for securities firms as well as for the staff of the JSE Inc.;

9. Speed up the implementation of the surveillance system so as to identify and reduce manipulation and fraud in securities transactions for protecting the investors. Also facilitate the real-time warning and surveillance system so that trading can be suspended when stock price volatility exceeds a given range;

10. Upgrade and expand the computer-assisted trading system to include coverage of derivative products, review and revise regulations and procedures concerning listing, clearing and settlement;

11. Promote contacts with the international securities community

12. Study the feasibility of international electronic linkage with other stock exchanges so as to further the internationalization of the securities market.

DEVELOPMENT OF STOCKS TRADED ON THE JAKARTA STOCK EXCHANGE FOR THE PERIOD OF 1977 - AUGUST 1992

YEAR / MONTH	TOTAL OF TRADING STOCK VOLUME (thousand)	TOTAL OF TRADING STOCK VALUE (Million Rp)	TOTAL OF TRADING DAYS	AVERAGE per Trading Days STOCK VOLUME (thousand)	AVERAGE per Trading Days STOCK VALUE (Million Rp)	STOCK PRICE COMPOSITE INDEX (%)	MARKET CAPITALIZATION (billion Rp)	NUMBER OF ISSUERS LISTED	Trading Turn Over (%)
1977	14.58	153.11	98	0.15	1.56	98.000	2.73	1	5.6
1978	19.45	218.54	250	0.08	0.87	114.990	4.05	1	5.8
1979	119.31	1,333.50	249	0.48	5.36	110.030	23.93	4	1.8
1980	1,656.29	5,733.41	251	6.60	22.84	103.540	[illegible]1.04	6	12.0
1981	2,891.35	7,651.70	254	11.38	30.12	100.260	48.60	8	15.2
1982	5,018.53	12,624.78	249	20.15	50.70	95.000	99.25	13	12.8
1983	3,507.75	10,107.64	250	14.03	40.43	85.620	102.66	23	7.4
1984	1,218.83	2,139.30	246	4.95	8.70	67.680	93.19	24	2.1
1985	1,866.87	2,972.65	244	7.65	12.18	66.530	89.30	24	3.2
1986	1,431.92	1,816.01	247	5.80	7.35	69.690	94.23	24	2.4
1987	2,523.37	5,184.10	246	10.26	21.07	82.580	1,193.00	24	4.3
1988	6,944.58	30,591.96	251	27.67	121.88	305.120	479.50	24	9.6
1989	96,064.05	990,364.21	248	387.36	3,993.40	399.690	4,358.50	57	21.86
1990	701,790.83	7,300,833.26	243	2,888.03	30,043.76	417.790	13,347.18	123	39.42
1991	1,007,791.17	5,777,387.42	245	4,113.43	23,581.17	247.390	16,438.00	139	27.02
January	48,170.10	316,418.91	21	2,293.81	15,067.57	383.020	12,490.30	125	2.88
February	80,608.80	638,958.59	19	4,242.53	33,629.37	391.330	14,470.16	126	4.28
March	62,599.70	478,245.81	20	3,129.95	23,912.25	408.110	15,331.48	128	3.28
April	75,446.59	603,260.77	17	4,439.18	35,485.88	413.710	15,770.59	128	3.84
May	73,899.44	530,794.05	21	3,519.00	25,275.90	397.600	15,525.00	129	3.73
June	67,248.51	510,127.81	20	3,362.40	25,508.35	346.270	15,222.79	129	2.82
July	116,704.78	665,648.48	23	5,074.09	28,941.22	339.960	15,769.88	135	3.92
August	71,115.54	374,656.73	22	3,232.50	17,029.82	300.980	14,886.85	137	2.53
September	79,622.29	327,127.48	31	3,791.54	15,577.50	249.187	13,094.20	136	2.54
October	84,465.33	349,623.35	23	3,672.41	15,201.02	226.684	11,856.04	138	2.65
November	97,465.31	357,463.53	21	4,641.21	17,022.07	243.041	12,978.99	138	2.96
December	150,444.78	625,062.11	17	8,849.69	36,768.36	247.390	16,438.00	139	4.03
1992	1,227,965.68	5,314,193.31	162	7,580.03	32,803.66	301.279	24,051.91	148	3.95
January	157,855.52	635,371.24	22	7,175.25	28,880.51	282.241	19,832.40	141	4.10
February	194,005.69	790,965.51	20	9,700.28	39,548.28	280.995	19,882.92	141	4.97
March	114,290.34	527,761.44	21	5,442.40	25,131.50	278.688	20,071.36	141	2.89
April	109,689.32	496,312.44	17	6,452.31	29,194.85	277.274	20,473.00	141	2.71
May	145564.87	685,691.53	20	7,278.24	34,284.58	295.468	21,717.31	141	2.99
June	199,119.98	996,176.97	20	9,956.00	49,808.85	313.558	24,598.55	145	4.46
July	112,832.41	574,843.26	22	5,128.75	26,129.24	317.186	24,560.15	147	2.43
August	194,607.53	607,070.91	20	9,730.38	30,353.55	301.279	24,051.91	148	3.95

DEVELOPING SHANGHAI STOCK MARKET IN THE 1990s

by

Shen Rui Xing
Shanghai Securities Exchange

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I am very honored to have the opportunity to deliver my speech at the conference. My presentation can be divided into three parts, the first of which is "The Emergence and Development of the Shanghai Stock Market." The second is "The Present Operation System of the Shanghai Securities Exchange (SSE)," and the last one is "The Future Development of the SSE."

THE EMERGENCE AND DEVELOPMENT OF THE SSE

In 1986, China's first OTC market was set up in Shanghai, which was the beginning of the stock market in China. A few years later, Shanghai's stock market had seen gradual and sound development with the strong impetus of the Deepening Reform in China. As the outcome of this development, December 19th, 1990, saw the successful establishment of the Shanghai Securities Exchange, which symbolized an entirely new step toward the development of the Shanghai Stock Market at the beginning of the 1990s.

The world has been well aware of the existence of the SSE, due to its diligent efforts to develop its market scale and to consummate its operation system, although it has been established only for less than two years. Now there are 30 listed stocks, among which are 9 "B" shares and 21 "A" shares, 3.7 times the number a year ago. The total market capitalization reaches 30 billion (RMB), an increase of over 20 times. The value per day is 300 million, 10 times the value a year ago. From January to August, the accumulative trading value came to ¥22 billion, 14 times the value last year. It is expected that at the end of the year, the total number of listed shares will have expanded to 50.

The fast development of the Shanghai stock market is also characterized by the rapid expansion of the number of investors and member firms. In 1990 the number of individual investors only amounted to 30,000, but now there are over 700,000 individual investors. The number of member firms has increased from 29 in 1929 to 137 this year. Among those, 102 are members from 25 provinces and cities all over China.

On February 21st this year, the first "B" share "Shanghai Vacuum and Electron Device Co." was listed on the SSE. There are nine "B" shares listed on the SSE market. The total market capitalization of "B" shares comes to 4 billion (RMB). Thousands of foreign investors have participated in the Shanghai "B" share market. They are foreign securities firms, investment banks, fund organizations and individual investors.

In order to follow the standard practice "B" share clearing bank, custodian banks are available. Besides, nominee's account is allowed in the Shanghai "B" share market. All these make foreign investors feel easy when they trade Shanghai "B" shares.

THE PRESENT OPERATION SYSTEM OF THE SSE

The Shanghai Securities Exchange has a highly computerized operation system which is made up of the following subsystems: automatic matching, scripless trading, automatic transfer and central clearing, etc. This system has been running successfully for more than a year, laying a strong technical base for the rapid development of the Shanghai Securities market.

INFRASTRUCTURE

There are 212 seats on the SEEs trading floor, and by October the total number of seats will reach more than 600. The Electronic Computer used by SSE belongs to a PC network which is composed of 250 users of short-distance terminals and over 400 long distance terminals. In order to meet the needs of the future development of the market, SEE has already subscribed to the HP 9000 super small-sized computer. In the coming three months the total number of users will be increased to over 1000. The SSE is preparing to build a new Securities Exchange Tower in Pu Dong which can accommodate 2000 seats. It is expected that this building shall be set up within the coming three years.

AUTOMATIC MATCHING

All dealings on SSE's market are matched automatically by the computer. The trading orders are transmitted by telephone from the member firms to their floor traders who put the orders through the terminals on their booths into the matching system and the computer, according to the principles of price priority and time priority, matches the orders based on double-auction. The matching system also has some subsidiary functions. For instance, it can process cross-trading during the business hours. Also, it can correct, withdraw orders, off-set wrong transactions, and supervise all trading made on the floor.

SCRIPLESS TRADING

All transactions on SSE's floor are done in a scripless way, so the listed companies no longer need to print physical certificates which have already been replaced by a modern computer database. The number of stocks held by share holders is recorded in the computer database and the back up of the daily transaction records is produced and put in two different places, so as to guarantee the safety of the database. Every shareholder has a share account, but this account does not show the current balance of the shareholder. If there is a transaction, SSE will provide the shareholder with a "Transaction, Transfer and Delivery Slip" which records the latest balance of his shares, thus the shareholder can get rid of the troubles in safe keeping physical certificates and in transporting certificates when delivery comes. Once an investor opens a share account with the SSE and produces his shareholder's code when placing orders, he can freely trade any stocks listed on the SSE. When he sells out his stock, the computer system, in order to prevent him from selling short, will first check his balance and accept his orders only if his balance is sufficient to support his selling.

AUTOMATIC TRANSFER

The transfer system of the SSE is based on a highly computerized and scripless trading system. All the balance and transaction records are kept in the computer, which makes the automatic transfer come true. Once a transaction is matched and the transaction instruction is sent to the computer, the automatic transfer system will transfer the ownership of stock by book entry. Besides the automatic transfer, a manual transfer is also available. It can adjust the balance of an investor when he wants to inherit shares from his relatives or friends or to send shares to somebody else if he wants. Of course, it can also freeze his account if his share account is lost or stolen.

THE CENTRAL CLEARING

The clearing in the Shanghai Stock Market is done by the SSE. The clearing is divided into two parts, the primary clearing and the secondary clearing. The former is done among the member firms, while the latter is carried out between the member firms and the investors. On T+0 the computer nets the capital balance of each member firm out, then the capital transfer is done by an appointed bank in a book-entry way. On T+1 comes the secondary settlement, which is done between the member firms and the investors. The computer will calculate the amount of money one must pay or receive, the commission, stamp duty, etc. and produce the "Transaction, Transfer and Delivery Slip," which records his quotation, transaction time, agent, shares traded, volume, latest balance and fees in great detail. When the member delivers the slip to him, he will easily know his transaction and his current balance.

In September this year the SSE will set up an entirely new capital transfer system in the "A" share market. A computer network will be produced among the SSE, the brokers and the bank. As soon as a transaction has been struck, the bank will automatically transfer capital in accordance with the transaction information provided by the SSE. Both the capital and securities settlement and delivery can be finished on T+0.

THE FUTURE DEVELOPMENT OF THE SSE

The 1990s are the years during which China's national economy will develop at high speed. In order to keep up with the rapid development of the nation's economy, the SSE will go all out to build the Shanghai Stock Market into a fair, stable, highly efficient market, and to restore the position of financial center as Shanghai used to be. In order to realize this historical task, the SSE will expand the market size by increasing a number of high quality listed companies, it is forecasted that within the next two years the total number of listed companies will be over 200. Besides, the SSE will do all it can to introduce high technology, so as to improve its operation system and to create a safe and highly efficient operation system. Take the automatic matching system for example, the most up to date HP computer will be put into operation at the end of this year. It will match 100,000 transactions per day, ten times the present capacity. Four years later, the SSE will move to Pu Tong when a huge Securities Tower is finished. This Tower can accommodate over 2000 seats, which can provide enough space for a minimum of 500 member firms.

China belongs to the class of developing countries, and the SSE has the same difficulties as only emerging market have. And it faces the same challenges. But the SSE is never afraid of the difficulties and welcomes the challenges. With the support and help of our colleagues and friends both at home and abroad, through diligent work and hard struggle, the SSE is confident that it must have a bright future.

MEXICAN STOCK EXCHANGE

by

Efran Caro Razu
Director, International Affairs Division
Bolsa Mexicana De Valores

BRIEF HISTORY

The Mexican Stock Exchange was founded in Mexico City in 1894. The few shares which were listed in the market's early years were mainly those of banks and industrial and mining companies.

Traditionally, the Mexican financial system and market trading had been dominated by banks, family groups and other insiders. By 1975 there were fewer than 5,000 active investors, and daily trading rarely exceeded U.S. $1 million.

In 1975 new securities legislation was issued, strengthening the regulatory powers of the National Securities Commission (NSC), as well as the securities market. A massive publicity campaign by the Exchange brought 25,000 new investors into the market, which in turn stimulated new issues and a rise in the market. In May 1979, the market reached its peak and was not particularly active again until early 1981, following the introduction of a new series of incentives.

However, when international oil prices started to fall in June 1981, this triggered devaluation fears, capital flight and economic recession. Stock prices collapsed, and trading volume fell almost to nil. Two successive devaluations in 1982, followed by the imposition of exchange rate controls and the nationalization of the banks created further shock waves. It was not until later in 1982 that the stock market failed again.

Since then the market has shown a good performance. Between January and September 1987 the Bolsa Mexicana de Valores 35-stock index soared by some 629 percent in pesos (329 percent in U.S. dollar terms) making it the world's fastest-growing stock market in real terms. During the final three months of 1987 the leading market index fell from its October 5 record high of 387,000 points to less than 90,000 before recovering somewhat to end the year at 105,670 points.

1988 was a very good year, and the index rose 100 percent to 311,532. With the peso free exchange rate static throughout the period, it also rose by 100 percent in U.S. dollar terms putting the Mexican Stock Exchange back among the best performers in the world.

The key factors affecting the market were the October 1987 crash, the implementation of the anti-inflationary pact signed by all economic sectors, and also the debt restructuring which was largely responsible for the development of three of the best-performing sectors: drinks, conglomerates and steel.

Another excellent year followed in 1989, and the index rose to 418,926, with a 98.04 percent yield in pesos (65.45 percent in U.S. dollar terms). The major factors supporting this performance were the continuation of the stability and growth pact, which kept interest rates down, improved economic conditions, the restructuring of the public debt with the international private banking system, and the impetus of the privatization programme introduced by President Salinas de Gortari's Government.

During 1989 the market-maker role was established, under the Securities Market Act, in order to improve market performance. Market-makers have not been introduced yet, but the project is well advanced. There are three rating agencies: CAVAL-Calificadora de Valores, DICTA-Dictaminadora de Valores and DUF & PHELPS de Mexico, who have been authorized to give commercial paper issues ratings from "A" to "E". A rating system for stock liquidity has also been introduced.

In 1990 a bill was approved by Congress to restructure the banking system, create and regulate financial groups, and amend the Securities Market Act.

The Privatization of banks allows foreign investors (except foreign government investors) to acquire 30 percent of their stock through Series "C" shares, provided that a single purchase does not exceed 5 percent of the paid-up capital. Foreign investment in brokerage firms has also been approved — 30 percent of their capital can be in foreign hands, provided that no more than 10 percent is in the hands of a single investor.

SETTING AND CLEARING

- Transactions for the moment can only be made in cash or on a spot basis.
- Settlements of stocks and bond transactions are on the second business day after the trade.
- Government bonds settle the next day.

COMMISSION RATES AND OTHER CLIENT COSTS

For variable income instruments, the brokerage commission for transactions up to MXP 200 million is 1.7 percent of transaction value. For transactions above this, the rate is 1.0 percent and can be negotiable.

Fixed income instruments attract a charge of 0.25 percent on any transaction.

TAXATION AND REGULATIONS AFFECTING FOREIGN INVESTORS

On the Capital Market, capital gains from variable-income instruments are exempt from taxation. For cash dividends, the tax rate is 10 percent if they are produced by taxable profits.

Since 1991, the interest withheld for money market and fixed income capital gains is 20 percent on the first 12 percentage points, the remainder being exempt. This regulation applies only for commercial paper, bankers acceptances and debentures.

Foreign investors can acquire securities of Mexican companies quoted on the Mexican Stock Exchange in three different ways:

1. Buying free subscription shares;
2. Through the "Neutral Trust Fund" framework;
3. By purchasing ADRs of Mexican companies quoted abroad.

Buying free subscription shares and series "B" is the most traditional method by which foreign investors have acquired securities of Mexican companies quoted on the Exchange. The great difference between this and the other mechanisms is that it offers foreign investors the same ownership and corporate rights that Mexican investors have, the only limitation being a certain maximum percentage ownership which is regulated by the National Foreign Investment Commission.

The "Neutral Fund" framework (series "N" shares) rests upon the Regulation for Foreign Investment, which provides for the establishment of a trust through which foreign investors may acquire shares previously restricted to ownership by Mexican nationals (series "A"), represented by Certificates of Ordinary Participation (CPOs).

CPOs issued by fiduciary institutions through a trust wherein ownership is formed by representative shares are quoted on the Stock Exchange. These certificates only incorporate the pecuniary rights derived from the shares forming the trust's patrimony, i.e., the CPOs represent ownership but not corporate (voting) rights.

American Depositary Receipts. Foreign investors may buy shares of Mexican companies quoted in the investor's country by purchasing ADRs. These are negotiable receipts covering the issuer's shares that are held in custody at an authorized institution (in the case of Mexico, the S.D. INDEVAL) in an account in favor of a bank or institution which issues the ADRs.

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NEW SYSTEMS IN THE EXCHANGE

The Mexican Stock Exchange has achieved all the globalization and modernization projects implemented since 1990. Such projects were appointed to the centralized effort for optimizing the services and to raise the quality level standards in each and every organizational area, also the strategies of globalization were strengthened, answering the foreseen tendencies in the international stock markets.

The International Securities Information System (SIBI) was carried out to facilitate the assistance to the requests made by international exchanges, for establishing Agreements of Exchange of Information and the Operative Transaction Automated System (SATO) was implemented to foster a more efficient, clear and trustable market.

PROSPECTIVE DEVELOPMENTS

To maintain its competitiveness at the international level and to give permanence to foreign investment the Mexican Stock Exchange along with the National Securities Commission and the Mexican Association of Brokerage Firms have undertaken a double process: the widening and restructuring of the existing markets and the creation of new ones. Regarding the creation of new markets we should mention the projects for the development and implementation of the intermediate and derivative product market. The first one to allow the quoting of small and medium size companies in the market, and the second to offer investors a wider range of instruments through the issue of warrants on the Exchange index and on some 10 to 12 leading stocks.

AMONG OTHERS

- The U.S. Securities and Exchange Commission (SEC) recognized the Mexican Stock Exchange as a "Designated Off-Shore Securities Market".
- 18 Mexican companies were given the category of "Ready Market" by the SEC.
- The Mexican Stock Exchange currently holds the chairmanship of the FIBV Emerging Markets Subcommittee.
- The Spanish government authorized Spanish citizens to invest in Mexican securities.

COUNTRY PAPER: SINGAPORE

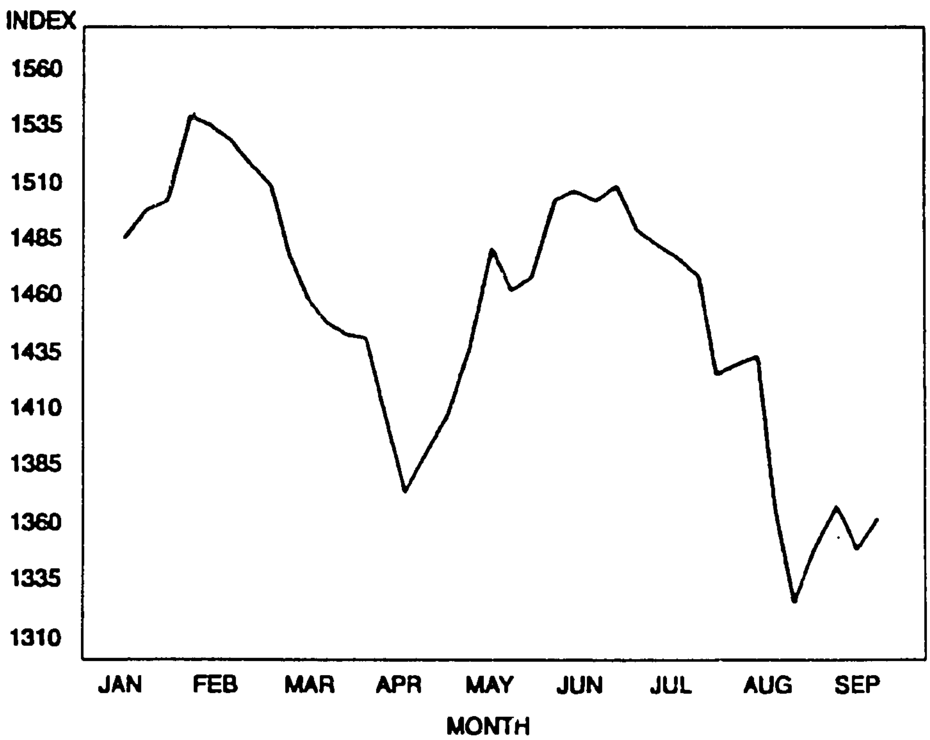
DEVELOPMENTS IN THE SINGAPORE STOCK MARKET

The Singapore stock market began 1992 on a positive note. The Straits Times Industrial and Commercial Index (the Index)[1] opened at 1479.35 on January 2, 1992 and rose to a high of 1545-92 on January 27, 1992 amid strong institutional buying interest and a decline in domestic interest rates.

However, the rally was not sustained and the Index slipped below the 1,500 mark towards the end of February. Thereafter, share prices on the Singapore stock market were generally weak, and the Index drifted in the 1,300 to 1,500 range. Investors' sentiments were dampened by persistent worries about the slowdown in Singapore's economic growth, a spate of disappointing corporate results, and a weak Tokyo stock market.

The steepest fall in share prices occurred in August. The release of a lower GDP growth rate for the second quarter of 1992 prompted some foreign fund managers to liquidate their holdings in Singapore stocks in favour of other regional stocks. This bout of selling sent the Index to an intra-day low of 1,269.35 on August 19, 1992, before closing at 1312.11. The Index has since traded in a range from 1,380 to 1,330. It closed at 1,339.75 on September 25, 1992, down 9 percent from the level at the beginning of the year.

STRAITS TIMES INDUSTRIAL & COMMERCIAL INDEX
WEEKLY AVERAGE - JAN 92 TO SEP 92



[1] The Straits Times Industrial and Commercial Index is an unweighted index that tracks the share price movements of the 30 leading industrial and commercial companies listed on the SES Main Board.

STATISTICS

Some relevant statistics on the Singapore securities market are shown in the following table.

	1987	1988	1989	1990	1991	August 1992
No. of Listed Companies	328	339	347	188	202	213
Total Mkt. Value (S$b)	279.3	285.9	325.1	255.8	259.0	252.6
Daily Trading Vol (S$m)	90.6	50.9	156.6	147.6	121.7	107.9

DEVELOPMENTS IN THE SECURITIES INDUSTRY

International Membership

In line with international trends, the Stock Exchange of Singapore Ltd (SES) has liberalised its entry rules and allowed 7 foreign securities companies, from the UK, Japan and France, to become full members under the new International Membership scheme. Previously, foreign institutions were only allowed to own a maximum of 49 percent of a member company.

As International Members, the companies are allowed to deal (in transactions of any size) with, or on behalf of, their related companies and non-residents of Singapore, and to deal with, or on behalf of any resident in Singapore, in transactions of not less than S$5.0 million per transaction.

Trading Systems

Since 1989, the SES has abolished its trading floor. All transactions of SES securities are executed through a fully-automated trading system known as the Central Limit Order Book (CLOB) system. As the name suggests, CLOB maintains an order book for each SES-quoted stock and matches buy and sell according to price and time priority. In addition to the quick and efficient execution of customers' orders, CLOB provides for greater transparency in displaying orders and prices.

Conversion to Book-Entry (Scripless) Settlement

In early 1987, the SES established a central depository system (CDS) for the clearing and settlement of securities transactions on a book-entry, or scripless, basis. Under the CDS, securities are immobilised at the central depository. Presently, the securities of some 80 listed companies have been immobilised at the central depository.

Options

The SES plans to commence trading of options on SES-listed stocks towards the end of this year. Tentatively, 6 blue chip stocks whose scrips have been immobilised for scripless settlement would be selected as the underlying securities for options to be written and traded. The introduction of such options will provide investors with increased opportunities to invest in Singapore stocks.

Extension of Trading Hours

In July 1992, the SES extended its trading hours by 90 minutes to enable international investors (in particular, those based in Europe) to trade in SES-quoted securities during the exchange's operating hours. The new trading hours are: 9:30am - 12:30pm and 2:30pm - 5:00pm (previously, 10:00am - 12:30pm and 2:30pm - 4:00pm).

THE ROLE OF CAPITAL MARKETS AUTHORITY IN THE KENYAN SECURITIES MARKET

BACKGROUND

The Kenyan Financial system is made up of one central bank, 19 commercial banks, 30 non-bank financial institutions, 36 insurance companies, several pension funds, 4 development finance institutions and over 900 savings and credit cooperatives.

The history of the Kenyan securities market dates back to the 1950s when the Nairobi Stock Exchange was formed. However, the money and capital markets became active only after the Government instituted a study which was undertaken by the International Finance Corporation (IFC) and the Central Bank of Kenya in 1984. The study entitled "Report on the Recommendation on the Development of the Money and Capital Markets in Kenya" identified and recommended steps to be taken in order to activate and develop the securities markets in Kenya. The activation would not only involve the introduction of new instruments but secondary trading as well. High on the recommendations of the study in regard to long term financing needs to the private sector was the establishment of the Capital Markets Authority (CMA).

The Authority was finally established in 1989 under the Capital Markets Authority Act Cap 485A of the laws of Kenya. In brief, the Authority is charged with the role of developing and regulating the capital market in order to ensure increased activity, variety of instruments, and order and fairness in the market.

The Nairobi Stock Exchange (NSE) had been relatively inactive before the setting up of the CMA. This inactivity is attributable to the following factors *inter alia*:

- the NSE operated as a private members club little supportive of broader public scrutiny and participation.
- there was no trading floor, hence business was conducted in exclusion of the much needed transparency.
- general lack of relevant policy orientation to activate the issuing and subsequent trading of shares and other corporate securities.

NEW DEVELOPMENTS AT THE NAIROBI STOCK EXCHANGE

The establishment of the Authority (CMA) has enabled a number of significant supportive changes to take place in the Nairobi Stock Exchange and the general framework within which the exchange operates.

The Authority has caused the exchange to shed its former image of "private members club" operating under the Societies Act. This has been achieved by having the exchange registered as a limited liability company under the Companies Act. The exchange now conducts its business in a modern trading floor in full view of the public. This move has enhanced transparent dealings by brokers as well as investor confidence. A new trading system — the "Open Out-cry" continuous auction system of trading — has been adopted in contrast to the old "Call Over" system which was practiced earlier by the brokers in a local hotel. The exchange now has its own secretariat which does the day to day running of its business.

The Authority has also helped in putting in place an expanded coverage of market activities on a daily basis by the news and electronic media.

The Nairobi Stock Exchange is currently formulating new rules and regulations consistent with its new status, and in conformity with the CMA Rules and Regulations which govern the setting up of securities exchanges. Although the Authority has the last say in regulating the securities exchanges, and other market players, it operates on the principal of self regulation in respect of each of them.

The improved framework at the NSE is not only boosting the image of the exchange but is also aiding in getting the exchange to position itself better for the emergent challenges posed by the broad economic reforms currently being implemented by the government.

The number of brokers in the Kenyan market has remained at six for a long period. There are already a handful of new applications lodged with CMA and soon it should be possible for additional brokers to be licensed. The Authority is also taking necessary steps to encourage the development of underwriting services to facilitate public issues in the market.

There are 53 companies listed in the Nairobi Stock Exchange. The companies are categorized under agriculture, commercial services, financial and investments and industrial and allied. Market capitalization was £ 1,111,364,854 or U.S. $673,554,456 on June 31, 1992. Average price earning ratios (P/E) for the market has increased from 3.3 in December 1991 to 3.9 by August 1992. Volumes traded in the market have also increased from an average of 100,000 to 1,000,000 shares per month.

Although the money market has been fairly active dealing in treasury bills, negotiable certificates of deposit, inter-bank market funds, promissory notes and pre-export bills of exchange among others, secondary trading still needs to be developed. More instruments also need to be introduced.

The Authority is already studying the applications and prospectuses of several corporations. At least two of these companies, a housing corporation and a department store are expected to go public before the end of 1992. Privatizing some public corporations through the stock exchange will have a major impact in the Kenyan securities market; a market in which every public issue in the last 6 years has been over subscribed by between 2 to 6 percent.

The Authority in liaison with the NSE is studying the possibility of establishing a second tier market to accommodate companies not able to meet the relatively stringent listing requirements by NSE.

It should also be noted that the CMA has caused the Unit Trust Act of 1963 to be amended. Plans are at an advanced stage to initiate a major study that will hopefully help in bringing about the establishment of the first unit trust. This study is expected to come up with model rules and regulations for unit trusts, insurance units and co-operative units. Earlier on, the Authority instituted a study on "The Capacity of the Kenyan Market for Equities" which came up with useful recommendations that will be used by companies issuing securities in the market.

In its dealing with public issues, the Authority basically concerns itself with adherence to disclosure requirements in order to ensure that the investor is protected. Pricing which is a controversial subject in emerging markets, is left to the issuer and the brokers or underwriters handling the issue. In other words it is the policy of the Authority to let market forces determine the price at which securities are issued.

CLEARING AND SETTLEMENT ETC.

A new delivery and settlement system is gradually being put in place. At the moment, a maximum of one week and three days are allowed for delivery and settlement respectively. The system is still handled by the brokerage community but plans are under way to centralize it. The duration allowed for clearing and settlement is destined to be tightened as the banking system improves and becomes increasingly automated. The NSE intends to centralize this system soon.

Accounting Practices

Public companies are expected to adhere to the Kenyan Accounting Standards as laid down by the Institute of Certified Public Accountants of Kenya (ICPK) with respect to disclosure and reporting requirements. The Kenyan Companies Act Cap 486 also outlines minimum disclosure requirements for companies that must comply with the International Accounting Standards.

Currency Restrictions Relating to Foreign Investments in Equity and Bond Markets

Participation in Kenyan bond and equity markets is still regulated by the Exchange Control Act requirements, which restrict direct foreign participation particularly in the equity and bond markets. However, the introduction of the Foreign Exchange Bearer Certificates popularly known as "Forex-C" and the recent announcement of the Foreign Exchange Retention Scheme by certain categories of exporters, are clear advances toward the dismantling of the exchange controls. We expect more relaxation in the Exchange Control Act so that investors may participate more actively in our capital markets.

RECENT DEVELOPMENTS
IN THE KOREAN SECURITIES MARKET

INTRODUCTION

During the past decade, the financial and capital markets of the world have experienced substantial changes highlighted by securitization, deregulation and internationalization in the wake of sustained growth of the world economy, accelerating the degree of interdependence among countries.

Korea was no exception to this general trend and a variety of measures were taken to develop the securities market in line with the profound change in the capital market worldwide. Especially, there occurred some important developments in recent years. Among them, first of all, was the liberalization of interest rates. At the end of 1991, the Korean government announced the plan of interest rate deregulation and took a historical step toward liberalization of interest rates, deregulating part of the short-term loan rates an deposit rates of marketable instruments such as CDs. The interest rates of corporate bonds with less than two-year maturity were also deregulated.

By the end of 1993, after the second stage of the plan, a large part of bank and non-bank loans and deposits will be subject to optional interest rates. If circumstances permit, the liberalization of interest rates will be fully accomplished by 1997, according to the government's schedule.

Second, in terms of internationalization, since the early 1980s Korea has opened its capital market to foreigners step by step, focusing on indirect methods in the early stage, in response to worldwide trends toward an open-door economic system.

As the final scheme of opening markets, the year 1992 could be recorded as an epoch year in the sense of allowing foreign investors to buy stocks directly in the Korean stock market, though within a certain limit. The limit in foreigners' holding of Korean stocks would extend to a higher level and finally to no restriction at all, in the future.

Finally, Korea has devoted and continues to devote its efforts to maintain efficient, fair and orderly markets. It is necessary to enhance the efficiency and fairness of the securities market due to the current trend of liberalization and internationalization as well as the growing importance of the securities market in the national economy. In December 1991, therefore, there was a broad amendment to the Securities and Exchange Law, which is the principal source of Korean securities laws. Major contents of the revision included strengthening of insider trading regulation, establishment of the shelf registration statement system, and introduction of the "five percent rule".

Following are details of some of these developments with the latest trends in the stock market of Korea.

MARKET SITUATION

Since the mid-1980s, the Korean securities market has shown rapid growth with the government's encouragement and benefitted from strong economic growth and the emergence of an external surplus. While the stock market had an aggregate market value of ₩6.5 trillion (U.S. $7.3 billion) at the end of 1985, it closed 1989 at ₩95.5 trillion (U.S. $140.5 billion).

However, Korea has been experiencing severe economic hardships since the end of 1980s. In the previous year, although the growth rate of the GNP remained relatively high at 8.5 percent, much of the growth was accomplished by the expansion of domestic expenditures such as private consumption and construction investment. Consequently, in spite of government's various efforts to curb inflation, consumer prices rose by about 9.5 percent in 1991, the highest since 1982.

Moreover, recent wage hikes coupled with insufficient R&D investments of companies have caused the manufacturing industry to lose its international competitive edge over foreign industries. This weakening competitiveness of companies together with strengthened protectionism of major trading partners led to an increase in the trade deficit which has a significant meaning to the export-oriented Korean economy.

The stock market was also heavily affected by deteriorating economic environments. The Korea Composite Stock Price Index, which had dropped during the last two years, again experienced a double digit fall of 10.1 percent in 1991. Even in 1992, the stock market is still showing little sign of recovery and the index remains around 520, down nearly 50 percent from a high of 1007.77 in April 1989.

The recent sluggish securities market is expected to regain its previous vitality when the Korean economy completes its structural adjustments successfully sooner or later.

INTERNATIONALIZATION OF THE CAPITAL MARKET

In order to adapt effectively to world wide trends toward an open-door economic system, Korea has felt the need to liberalize its capital market. With steady progress in the liberalization of trade and foreign exchange, the Government declared a four-phase "Long-term Plan for the Internationalization of the Capital Market" in January 1981.

Since that time the Government has been promoting the internationalization plan gradually and progressively.

Securities Market Opening

In the early stage, international trust funds such as KIT (Korea International Trust) and KT (Korea Trust) were first established for foreign investors by domestic investment trust companies in the form of beneficial certificates in November 1981. Since then, trust funds have increased according to the government's policy to expand indirect investment vehicles. As of June 1992, 10 funds of U.S. $345 million are actively operating for foreign investors. In addition to this, the Government authorized domestic investment trust companies to establish matching funds of U.S. $300 million in June 1990, thereby enabling both domestic and foreign investors to enjoy benefits from the opening.

Also the Korea Fund, Inc., a U.S. closed-end investment company, which was established in August 1984 and listed on the New York Stock Exchange with an initial value of U.S. $60 million, invested at least 80 percent of its assets in Korean securities. Two foreign investment companies such as the Korea Europe Fund and the Korea Asia Fund were set up in March 1987 and in July 1990 respectively for similar investment objectives. As of June 1992, paid-in capital of the three investment companies amounted to U.S. $360 million.

Moreover, foreign bondholders were permitted to reinvest the proceeds from the sale of converted shares in other Korean equities from October 1992, and foreigners were finally allowed to invest directly in Korean stocks within certain limits on January 3, 1992. With market opening in the offing, the Commission made relevant rules and regulations which set out investment limits, investment registration, and method of transactions.

Securities Industry Liberalization

Foreign securities firms have been allowed to open representative offices in Korea on a reciprocal basis since 1981, in accordance with the basic long-term plan of 1981. Consequently, 31 foreign securities firms have established 26 representative offices and five branch offices in Seoul, while domestic securities companies have set up eight subsidiary companies and 42 representative offices in major financial centers such as New York, London, Tokyo, Hong Kong, and Zurich as of June 1992.

Also, since 1989, foreign securities firms have been permitted to take equity in domestic securities companies up to 10 percent of a securities firm. Total foreign equity in a securities firm may not exceed 40 percent. Until now three foreign securities firms including two Japanese companies have made direct investments in two domestic brokerage firms. However, the foreign firms' share is below 3 percent. In addition, domestic securities firms have participated actively in the establishment of offshore funds or management companies in tax havens since late 1991. As for the international business of domestic securities firms, underwriting and selling in overseas markets were, for the first time, licensed to big firms according to "the Measures for Expanding the Capital Market Functions" announced in July 1983. At the initial stage, they engaged in limited securities business overseas, such as participation in the underwriting groups organized for convertible bonds issued by domestic listed companies and sales of international trust funds established by domestic investment trust companies. Since September 1987, international securities business, especially underwriting, has been actively carried on, triggered by the Government measures which permitted securities firms to hold foreign currencies.

In July 1988, the Government for the first time allowed additional domestic institutional investors including securities firms, besides already qualified commercial banks, to invest in overseas securities within U.S. $30 to $50 million ceilings. As a result, investment in overseas securities by domestic securities firms, which totaled U.S. $9.7 million at the end of 1988, grew to U.S. $150 million by June 1992. However, corporations and individuals are not yet permitted to purchase overseas securities on account of unexpected economic changes, e.g., current account deficit in the balance of payments.

The securities firms' international business was steadily expanded to the brokering business in December 1988, and to the dealing business in 1991. Consequently, securities firms qualified to carry on international securities business fully stood at 22 among a total of 31 companies.

Issuance of Overseas Securities

In 1985, at the second stage of the Long-Term Plan of 1981, eligible listed companies were permitted to float such securities as convertible bonds (CB), bonds with warrants (BW), and depositary receipts (DR) in the international capital markets.

In collaboration with the Government, the SEC made rules and regulations concerning the issuance of overseas securities by domestic listed companies in November 1985. Since that time, issuances of overseas securities have steadily increased with diversified types of securities (i.e., BW and DR), totaling U.S. $1,871 million as of June 1992.

Through revision of relevant rules, significant improvement and relaxation were also made in the financial requirements for eligible companies, the use of proceeds, and adoption of the stock price review system of preventing intervention in the market.

To date, in a nutshell, the Government and the SEC have employed possible indirect investment vehicles and progressive methods in the course of capital market internationalization in order to minimize its adverse impact on the economy and domestic securities market.

AMENDMENT TO THE SECURITIES AND EXCHANGE LAW

The 10th amendment of the Securities and Exchange Law, passed by the 156th National Assembly on December 17, 1991, was promulgated on December 31, 1991 and fully entered into force from the same date. The amendment was established to make a comprehensive supplement to the securities regulation that needed to be overhauled in connection with the liberalization of the securities industry and the opening of the securities market to foreigners.

Regulation of Insider Trading

The provision for insider trading, previously prescribed as a type of market manipulation activity, is now provided separately under the explicit title "prohibition of insider trading", and located next to the provision titled as "recovery of short swing profit" in order to help understand the whole system of the regulation. Also, the securities subject to the regulation, the scope of insiders, and the concept of inside information are defined more specifically through the amendment.

While a trader who succeeded in proving that he made such a profit without ever making use of inside information could enjoy the benefit of exceptions from the recovery of the short swing profit before the amendment, the short swing profit must now be recovered by the corporation even if the trader proves that he has not made use of inside information provided, however, that such recovery requirement shall not apply to those attained from the certain transactions designated by the presidential decree promulgated under the law.

Officers and major shareholders (shareholders beneficially owning not less than 10 percent of the total number of shares issued and outstanding, and de-facto controlling shareholders who exercise substantial influence over the management of the corporation such as appointing or dismissing of officers) are required to submit a report on the current status of ownership within 10 days after he becomes an officer or a major shareholder and any change in the number of shares by the 10th day of the month immediately following the month during which the change occurred.

In order to inspect the unfair transaction under suspicion, non-member securities companies may be requested to provide or disclose information with respect to customers' transactions in the Korea Stock Exchange.

Violations of insider trading are punishable with a fine of not more than ₩20 million. However, if the amount is equal to three times the profit resulting from, or the loss avoided by, the violation of the provision exceeds ₩20 million, the ceiling on the amount of such a fine will increase up to three times such profit or loss.

Provision for the civil liability of insider trading, previously prescribed in connection with the market manipulation, is rearranged explicitly under an independent title of civil liability of insider trading to make clear the ground for civil remedy.

Corporate Disclosure

To simplify and accelerate the procedure of disclosure, the shelf registration statement system was installed. An issuer who has filed with the Commission a shelf registration statement regarding the securities to be publicly offered during the proposed issuing period specified in the shelf registration statement, pursuant to the provisions of the regulations of the Ministry of Finance, is exempted from filing a separate registration statement as to the specific issues or sales of the securities during such a period.

Moreover, the filing system was supplemented in order to ensure the efficiency and accuracy of the registration statement. First, the time limit to the filing of the amendment statement was extended from the effective date to the commencement of the subscription period. Second, the registration statement may be withdrawn by the issuer filing a withdrawal statement with the Commission before the effective date pursuant to the Commission rules. Third, the scope of the persons subject to civil liabilities is extended. Fourth, the scope of exemptions from the registration of issuers or the submission of registration statements is determined by the presidential decree, which added the House Redemption Bond to the scope of exempted securities in addition to the existing securities such as the beneficiary certificates issued by investment trust companies. Fifth, the effective date of the registration statement may be accelerated to the earlier date as the Commission may determine when it finds the contents of the registration statement easily understandable or widely known to the public. Sixth, a corporation in the process of incorporation which intends to make a public offering of securities is permitted to register with the Commission, and the documents regarding the settlement of accounts, which the registrant was obligated to submit, is removed from the requirements of the registration. Seventh, the Commission is empowered to define the concept of the public offering of securities to which the requirements of filing a registration statement apply.

The Korea Stock Exchange is also empowered to request a listed corporation to disclose whether there is any material inside information when there is notable fluctuation in the price or the trading volume of its securities.

Finally, a listed corporation which has subsidiaries is obligated to file a consolidated financial statement together with a certified public accountant's audit when filing an annual report. An additional 30-day period is granted for such corporations preparing consolidated financial statements.

All of these amended provisions are expected to improve the efficiency of disclosure in the securities market.

Introduction of the "Five Percent Rule"

Anyone who beneficially owns, in whomever's name, more than 5 percent of the total number of shares with voting rights issued by a listed corporation, shall file with the Commission and the Korea Stock Exchange a report of share ownership in the manner as determined by the Commission within five days from the first date on which there is any change in his share ownership by more than one percent of the total number of shares with voting rights.

On the other hand, persons listed in the presidential decree, including government, local autonomous entities, and trust companies, are exempted from filing the report. Institutional investors specified in the presidential decree are allowed to file a quarterly report in a simplified form instead of an occasional report in regular form.

COLOMBO STOCK EXCHANGE

COLOMBO STOCK EXCHANGE

COUNTRY PROFILE

Sri Lanka

POLICY CHANGES

AND

FISCAL INCENTIVES

Stepping Stones

1992 Complete abolition of Capital Gains Tax with effect from 26th August, 1992

1992 Complete abolition of the 100% Transfer of Property Tax on share purchases by non-nationals excluding a few companies.

Corporate Tax for quoted companies was reduced to 40%

All types of companies will pay tax at a uniform rate of 35% with effect from 01-04-1993

1991 Abolition of Welath Tax on Listed companies

1990 Announcement of the new Industrialisation strategy of the Government

Liberalisation of Investment in the stock market with the abolition of the 100% Transfer of Property

Tax on share purchases by non-nationals subject to the limitation that their aggregate shareholding should not exceed 40% of the issued capital

Relaxation of Exchange Control on inward remittances for share purchases and outward remittances of surpluses on dealings in listed shares.

1989 Abolition of the 100% Transfer of Property Tax on share Transfers between non nationals
Privatisation of the first Government owned Business Undertaking

1988 Repeal of the Business Acquisition Act

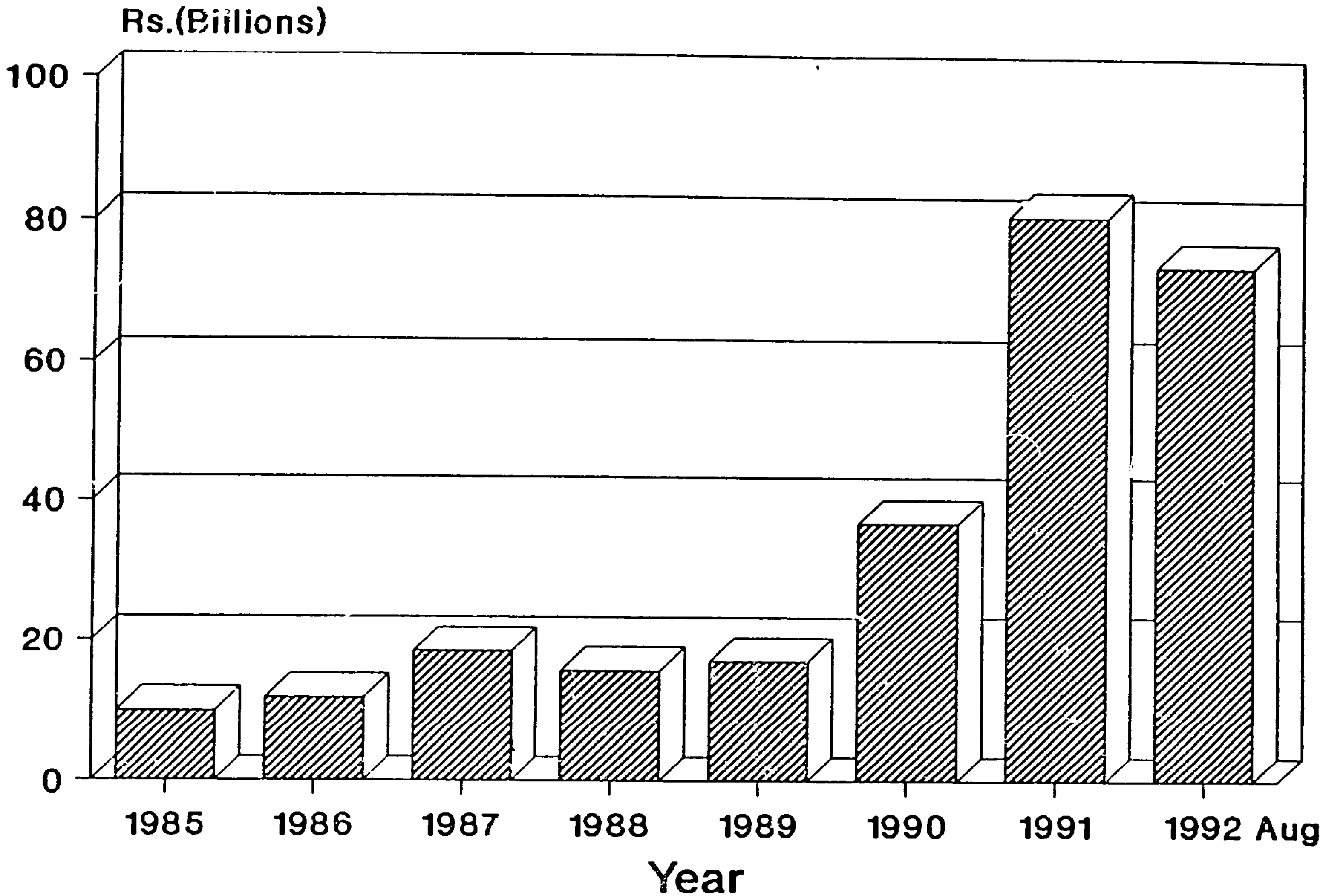
1987 Opening of Insurance Sector to local and foreign private sector participation

1980 Introduction of an income tax differential of 10% in favour of Listed Public Companies

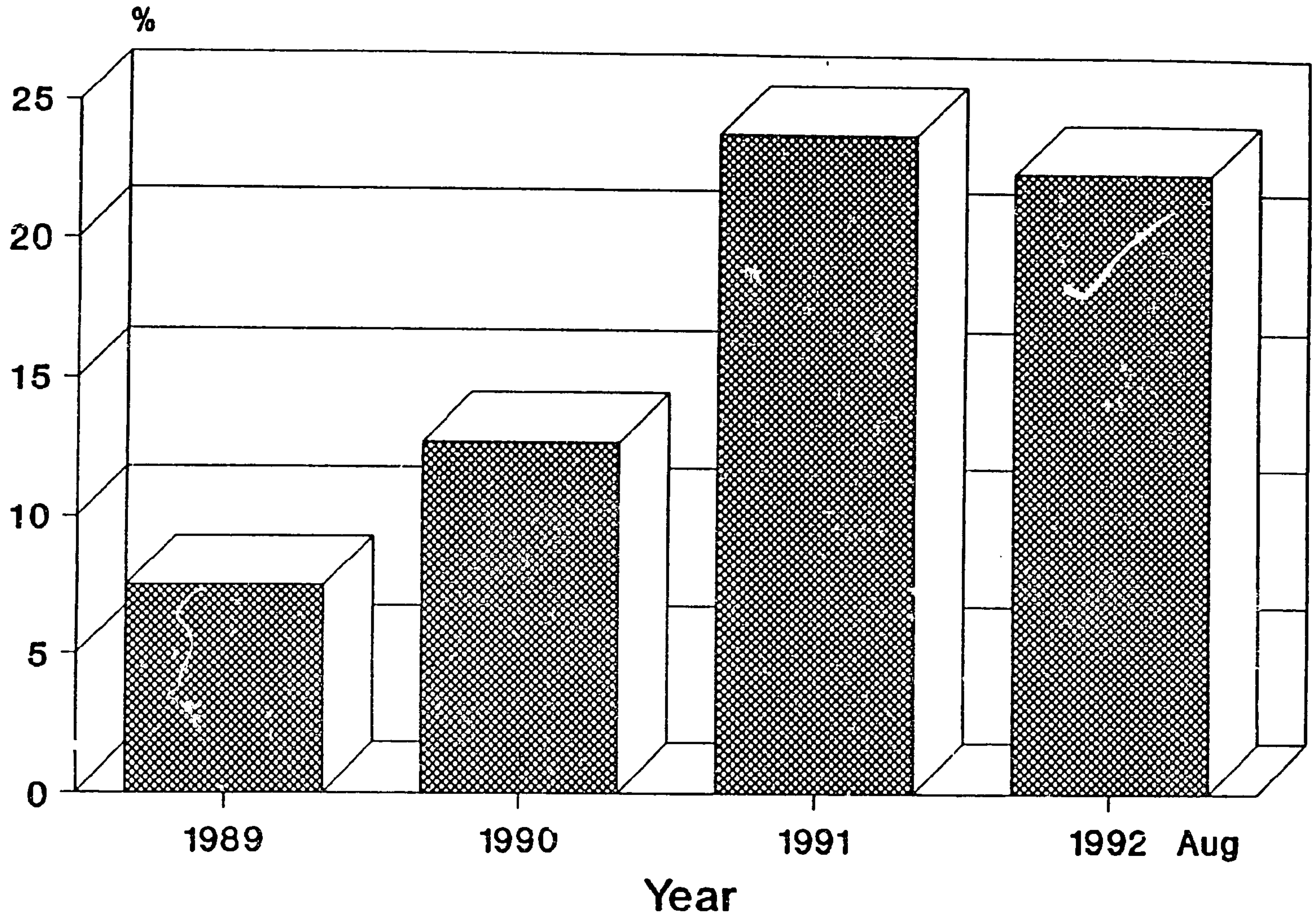
1979 Opening of the Banking Sector to foreign owned and private commercial Banks

MARKET PERFORMANCE

Market Capitalisation 1985 - 1992 August

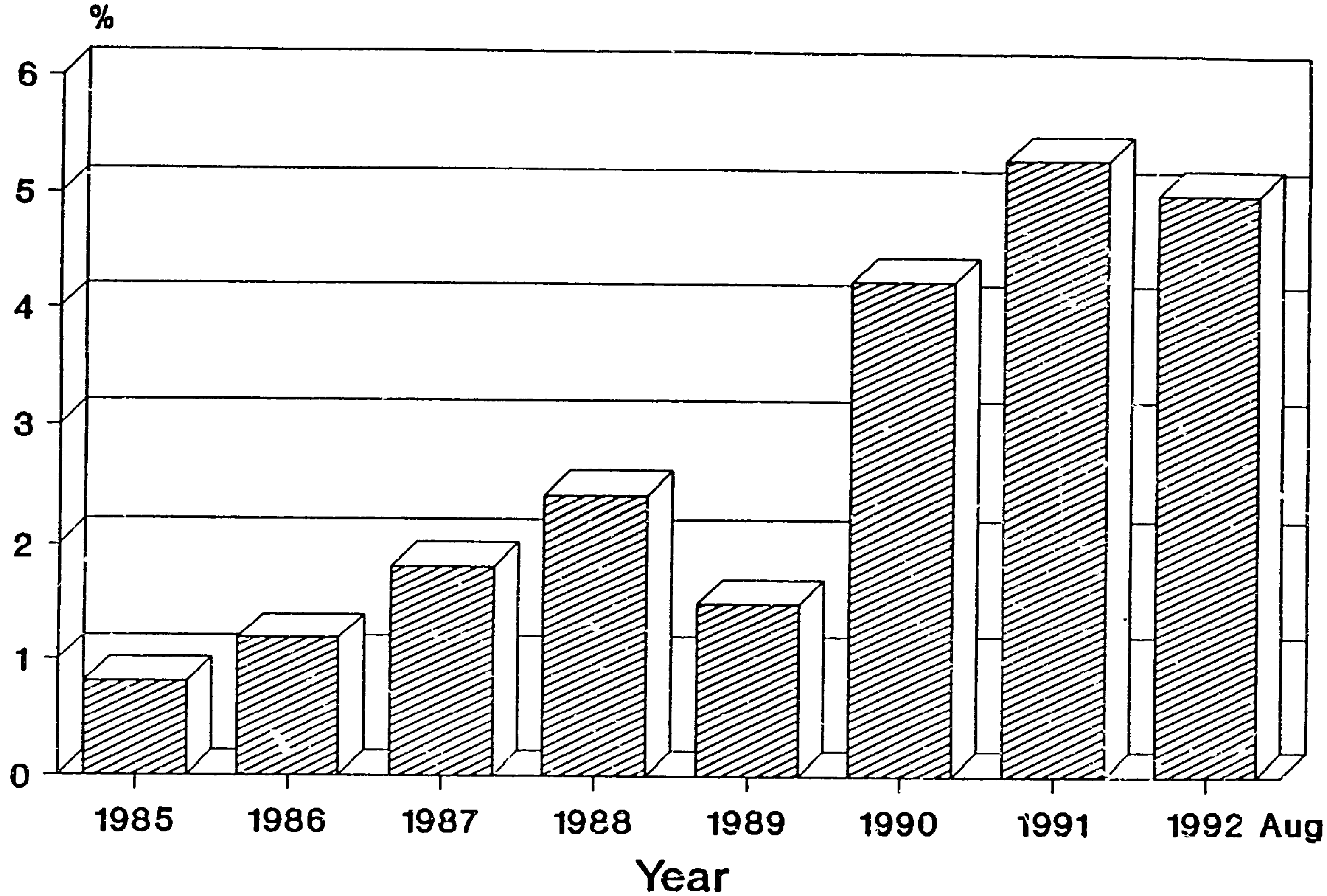


Market Capitalisation as a % of GDP



COLOMBO STOCK EXCHANGE

Trading Turnover as % of Market Capitalisation



Institutional & Infrastructural Changes

FORMATION OF THE SECURITIES AND EXCHANGE COMMISSION OF SRI LANKA

OBJECTS:

1. The Creation and Maintenence of a market in which securities can be traded in an orderly and fair manner

2. The protection of financial interest of investors.

3. The operation of a Compensation Fund

4. The regulation of the Securities Market and ensure that professional standards are maintained

FORMULATION OF A CORPORATE DISCLOSURE POLICY

1. Immediate Public Disclosure of Material Information

2. Thorough Public Dissemination.

3. Clarification or confirmation of rumours and reports.

4. Response to unusual market action.

5. Unwarranted promotional disclosure.

6. Insider Trading.

INTRODUCTION OF NEW REPORTING REQUIREMENTS

PERIOD	STATEMENT	RECEIPIENT/S	COMPLIANCE
Half Yearly	Profit & Loss unaudited	Exchange & shareholders	Before the expiry of three months from the end of the Half Year
Annual	Profit & Loss Balance sheet- unaudited	Exchange	Before the expiry of 4 months from the end of the Financial Year
Annual	Profit & Loss, Balance sheet- audited	Exchange & Shareholders	Before the expiry of 6 months from the end of the Financial Year

INTRODUCTION OF A NEW DELIVERY & SETTLEMENT SYSTEM

- Central Depository System (CDS)
- Central Certificateless depository record keeping system for individual share owners
- Clearing and settlement fully automated
- A hybrid of demobilisation and dematerialisation
- Book entry transfer of ownership
- Settlement cycle reduced from two weeks to trade day plus seven (T+7) Ultimately working towards T+3 by July 1994
- Few countries in the world with such a system
- Brokers are connected on-line to the CDS
- Brokers have utilised on-line system for mini-trading floor

ADMISSION OF NEW FOREIGN BROKERS from NOVEMBER 1992

- JARDINE FLEMING
- SMITH NEW COURT
- SASOONS
- DEVELOPMENT BANK OF SINGAPORE(DBS)
- CROSBY SECURITIES

FINANCIAL MARKETS AND FOREIGN INVESTMENT IN BRAZIL

BOVESPA'S OPERATIONAL AND SERVICES STRUCTURES

by

Gilberto de Souza Biojone, Filho
Chief Executive Officer, São Paulo Stock Exchange

BOVESPA'S OPERATIONAL STRUCTURE

BOVESPA trades securities issued by public companies and assets authorized by the Securities Commission-(CVM). Most transactions are concentrated on stocks of public companies. Stock rights and receipts, subscription bonus, Privatization Certificates and others are also traded.

TYPES OF MARKETS

Cash Market

Cash purchase or sale of a certain number of shares, executed at a price established on the open out-cry session or by means of the computer trading system (CATS). The seller delivers the shares on the business day following the closing of the deal and receives the cruzeiros concerning the sale on the next business day. The buyer pays the amount due and receives the shares on the second business day.

Forward Market

The purchase or sale (on the open out-cry session or through CATS) of a certain number of shares, at a fixed price, for delivery within a defined period, which has to be a multiple of 30 days and no longer than 180 days, from the day of execution of the trade, results in a contract between the parties. The settlement is made on the expiration day of the contract or before.

Options Market

A call option gives its holder the right to purchase the underlying stocks at the exercise price at any moment until the expiration day under the conditions established by BOVESPA. In case of put options the right of sale may only be exercised on the expiration day of the option.

Options on BOVESPA may be negotiated either on the open out-cry session or on the CATS system. The options always expire in even months, on the Monday nearest to the 15th.

TYPES OF TRADING

Trades on BOVESPA are made on the open out-cry session or on the CATS system.

Open Out-cry Session

BOVESPA's member brokerage firms and licensees have access to the trading floor to execute customers' orders, and to out-cry them by specifying the issuing company, the type of stock, the bid/offer price and the number of shares.

The most liquid stocks are traded on the open out-cry session from 9:30am to 1:00pm and from 3:00pm to 4:30pm.

Computer Trading System — CATS

The CATS system used by BOVESPA is an enhanced version of the Computer Assisted Trading System developed by the Toronto Stock Exchange. The system reproduces on screen the entire trading environment, displaying the entry and registry of bids and offers and their automatic closing through computer terminals. CATS ensures that the order will be executed at the established price or a better price, and that the chronological priority among bids/offers will be observed. On-line confirmation of execution is provided.

CATS also offers an efficient system of market information and provides management control and trading surveillance instruments, thus contributing to the exchange's maintenance of fair and orderly conditions, to enable the functioning of the market.

On CATS, the brokerage firms input orders in their computer terminals, introducing bids and offers and closing deals directly from their offices. These may be located anywhere in the country, making trades on the cash, forward or options markets. The system allows the brokerage houses the on-line/real-time inquiry about the transactions affected.

Due to the CATS system and to the creation of the CATS Licensee, BOVESPA made possible for brokerage firms from other regions in the country to have access to São Paulo market transactions at reduced costs.

Introduced in July 1990, the system was consolidated in 1991, when it was responsible for 36 percent of the trades and for 14 percent of BOVESPA's turnover.

The system is currently operated in two periods: from 9:30am to 1:00pm and from 3:00pm to 4:30pm.

GUARANTEES, RISK CONTROL AND MARKET SURVEILLANCE

Trades on BOVESPA are protected by guarantee mechanisms, being constantly monitored and under surveillance instruments and also submitted to risk control schemes. The main security devices are the following:

- Seats belonging to securities brokerage firms (members of BOVESPA) and to the clearing agents (members of Calipsa) must be pledged as guarantee for the benefit of BOVESPA before these participants start activities;

- With the purpose of guaranteeing the settlement of the transactions processed by Calispa, which manages an Operations Settlement Fund composed of a share of Bovespa Guarantee Fund's equity and of resources from the clearing agents;

- BOVESPA maintains a Guarantee Fund which aims at ensuring customers of the member brokerage firms, compensation for losses due to improper execution or to the non-execution of orders. Inauthenticity of the securities delivered to the client among other problems, is also covered;

- Risky positions on the term markets (writing options or purchasing or selling forward) must render guarantees, established on the basis of the volatility of the price of underlying stock (in case of options) and on the negotiability of the stock (on the forward market);

- The open positions maintained by investors, or group of investors trading jointly, are subject to operational limits determined by Calispa;

- Calispa makes analysis and risk control of trades, identifying customers or groups of customers acting jointly and also concentration of positions. Calispa also analyzes the financial capacity of the clearing agent;

- In order to guarantee orderly activities of the market, BOVESPA monitors the open out-cry and CATS transactions by means of a trading surveillance system. This system is based on price and quantity parameters and warns the Exchange in case of eventual deviations from the established trading patterns;

- All trades on BOVESPA are monitored by trading post supervisors and by the stock watch team;

- The surveillance of transactions also takes into consideration the trades of a particular stock in relation to the equity capital of the issuing company;

- Trades in excess of one of the parameters are submitted to auctions. The issuing companies are asked to disclose any relevant fact which is not the known to the market.

Settlement of Transactions and Securities Custody

Since November 4, 1991, clearing and settlement of transactions on BOVESPA have been performed by Calispa. The clearing agents of Calispa are brokerage houses which are — members of the São Paulo Stock Exchange. They are, therefore, allowed to settle their own transactions.

The clearing agent is responsible for the proper settlement of its transactions and of those executed by its contracting brokerage houses.

The licensee brokerage rims have to make a contract with the clearing agents for the settlement of their trades.

Calispa deals directly with the clearing agent only. The credits/debits are made to the account of the agent, transfered to the brokerage houses which deliver them to their customers later.

BOVESPA also provides a depository system. Calispa only clears and settles with securities which are under BOVESPA's custody. Since all shares in circulation are under nominative form, custody is maintained by BOVESPA mainly through book entry.

The physical settlement of transactions on the cash market occurs on the first business day (D1) following its execution (D0). The financial settlement happens on the second business day (D2).

The settlement of a common trade obeys the following timetable:

D+O

Day on which the transaction is closed
Sole day for options specification
Options coverage

D+1

Day of specification/respecification of transactions (cash and forward)
Physical settlement of transactions
Options margin deposit
"Potential defaulters" report

D+2

Financial settlement of the transactions
Financial coverage for defaulters
Margin deposits for forward contracts

D+3

Last day of regularization of the physical settlement of the transaction

Transaction Costs

The investor's direct operational costs on BOVESPA include the commission fee due to the brokerage firm, the registration fee, the trading charges and the ANA (Stock Trading Notice) fee which are due to BOVESPA.

The commission fee is a percentage of the total financial activity (purchases plus sales), which is made up by the orders executed on the investor's behalf, by a single brokerage firm, on the same trading day. And it is totally negotiated between the firm and its customer.

The Stock Trading Notice, issued by the Exchange, is charged according to the number of trading sessions on which the investor had orders executed, regardless of the number of transactions under his/her name.

The registration fee is charged by the Exchange for each transaction on the term market — options (0.2 percent) and forward (0.1 percent). There is also a 0.05 percent fee charged on each trade value.

SERVICES RENDERED BY BOVESPA

Private Telephone Operation System — SPOT

The SPOT network, BOVESPA's exclusive telephone service, interconnects the country's major financial institutions and companies, through 6,000 extensions. It is a supporting device fundamental to the execution and expansion of BOVESPA's trades, especially, when it is related to the licensee brokerage houses and the CATS trading system. In 1992, BOVESPA will enlarge the SPOT network and add 4,000 more extensions.

Services Network

BOVESPA's member brokerage firms and licensees are allowed access to the Exchange's Services Network. Such services, rendered by means of computer terminals, include the systems of client registration, customer specification regarding the transaction, and transmission/receipt of files directly from BOVESPA's mainframe. Additionally, the firm has access to the data banks of stock revenues, to the Exchange's daily information bulletin, to prices and values of on-line trading, and to general inquires, besides its custody position on BOVESPA.

Master Terminal

The master terminal is a mix of hardware and software comprising in a single terminal, the services that were previously rendered to the brokerage houses via several terminals, allowing access to information from the Broadcasting system, in addition to BOVESPA's and BM&F's Services Networks.

Broadcasting Signal

Devoted to the brokerage and software houses (vendors), the signals are transmitted by BOVESPA's mainframe, via telephone cables, to the users' editing equipment, which make screen reading possible. It informs stock prices and the behavior of the trading session, with no need of inquiry digitation, allowing the active surveillance of the price formation process and its trend.

Cordless Telephone

In 1982, BOVESPA was the pioneer in Latin America in the use of this kind of equipment on its trading floor. With it, floor operators can receive the clients' orders directly from their offices and execute them immediately.

Dial BOVESPA

By telephone and from any place in the country, the investor may follow up the prices of the most traded securities. The Dial BOVESPA is available 24 hours a day through the numbers: (5511) 200.1319 and 200.1519.

Information Center

BOVESPA Information Center (CIB) is open to public in general, especially to investors and students. It provides information about many markets, the transactions affected through audiovisual exhibition and monitoring of visits to the open out-cry trading floor. There are visitation programs specially devoted to children, high-school and university students.

Publications

BOVESPA Bulletin is edited and published daily in the market section of "Gazeta Mercantil," a newspaper of wide circulation in the Brazilian financial market. Information on the listed companies and trades executed on the Exchange's sessions is transmitted by telex, diskette and written papers to news agencies, specialized magazines and newspapers.

The Technical Report magazine is a monthly, bilingual publication which summarizes all the transactions affected during the period. BOVESPA also sponsors the publication of technical handbooks on capital market and produces educational leaflets on several markets and types of trading.

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Mr. Yasapala Ratnayake
Manager, Investment
Employees' Trust Fund Board

Mr. M.A.I. Rauff
Chief Broker/Analyst
Commercial Stock Brokers (Pvt) Ltd.

Janaka R. Rockwood
Chief Executive
CDIC Sassoon Cumberbatch
Stock Brokers (Pvt) Ltd.

Mr. Azeez Rumy
Director
Mackinnon & Keells Financial Services Ltd.

Mr. Rohan Samantha Silva
Manager, Operations
Ron Logics (Pvt) Ltd.

Mr. Vinodh Samarasinghe
Assistant Manager
Citibank N.A.

Mrs. Surekha Sellahewa
Manager, Surveillance & Enforcement
Colombo Stock Exchange

Ms. Patricia Anne Senoviratne
Executive - Admn. and Compliance
The Unit Trust Management Co. (Pvt) Ltd.

Mr. Auburn Senn
Floor Broker
JB Stock Brokers & Financial Services (Pvt) Ltd.

Mr. Rajesh Sethi
Manager, Merchant Banking Division
ANZ Grindlays Bank

Mr. Kithmani Soysa
Registrar
The Unit Trust Management Co. (Pvt) Ltd.

Mr. James W. Spain
Chairman
CML-Spain-Perry Fin. Services

Mr. Asitc Talwatte
Partner
Ernst & Young Consultants

Mr. Ram Mohan Tennakoon
Chairman, Lanka Tiles Ltd.

Mr. M.J. Thurairasalingam
Investment Controller
Ceylon Tobacco Co. Ltd.

Mr. Benny P. Tissera
Inspection Manager
Securities and Exchange Commission of Sri Lanka

Mr. Isuru Tillakawardena
Manager, Trading
Colombo Stock Exchange

Mr. Sarinda Unambooowe
General Manager
John Keells Holdings

Ms. Sujithra Vijayaratnam
Directress
JB Stock Brokers &
Financial Services (Pvt) Ltd.

Mr. Chandra Wijenaike
Chairman
Central Finance Co. Ltd.

Mr. Tissa Wijeyeratne
Former Chairman, Executive Consultant
Sinhaputhra Finance Ltd.

Mr. Anil Wickremasinghe
Investment Manager
CTC Eagle Insurance Co. Ltd.

Mr. Abhaya Wijeratne
Manager, Investments & Capital Market
Merchant Bank of Sri Lanka

Mr. V. Wijenathan
Asst. General Manager
Bank of Ceylon

Mr. Hiranya Wimaladharma
Deputy Manager, Merchant Banking
Division, ANZ Grindlays Bank

Mr. Jivaka K. Weeratunge
Joint Managing Director
C.K.N. Fund Management (Pvt) Ltd.

Mr. Eran Wickramaratne
Assistant Vice President
Citibank N.A.

Mr. Mallory Eraj Wijesinghe
Director
Bartleet Mallory Stock Brokers (Pvt) Ltd.

Mr. Anton Wijeyegoonewardene
Director
Colombo Stock Exchange

Mr. Anura R. Wickremasinghe
Director
Forbes & Walker Stock Brokers (Pvt) Ltd.

Mr. Ajit Carlyle Wanigasekera
Investment Advisor
Forbes & Walker Stock Brokers (Pvt) Ltd.

Mr. Sunil Gamini Wijesinha
Chairman
Employees' Trust Fund Board

UNITED KINGDOM

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Vice Chairman
S.G. Warburg & Co. Ltd.

UNITED STATES

Mr. Nihal Goonewardene
President
International Science & Technology Institute Inc. (ISTI)
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Mr. Bill Gorman
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