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**FINAL**

**SWAZILAND**

**DIAGNOSTIC STUDY OF  
FINANCIAL MARKETS**

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**U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT - SWAZILAND**

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# SWAZILAND

## DIAGNOSTIC STUDY OF FINANCIAL MARKETS

### EXECUTIVE SUMMARY

#### Report Structure

The report is divided into two parts: Part One, an evaluation of the financial environment in the region with emphasis on the comparative environments in South Africa and Swaziland, and; Part Two, an assessment of the stock exchange environments in both South Africa and Swaziland leading to recommendations for future systems developments in Swaziland followed by a suggested technical training approach and recommendations for promoting public awareness and education regarding stock exchange operations.

#### Principal Findings

The southern Africa potential for regional financial sector integration is significant, particularly in view of the near term capital markets developments in South Africa. The Johannesburg Stock Exchange (JSE) is moving towards establishing itself as the core African Stock Exchange Association (ASEA) stock exchange driving a southern Africa regional exchange network. It is accordingly in the best interests of Swaziland capital markets to protect their national sovereignty through a coordinated national capital markets development plan.

There is a short term opportunity to undertake a regional capital markets development program for which Swaziland could serve as the model. A number of sub-Saharan African stock exchanges will collaborate with the JSE, with the JSE serving as the central hub for a regional federation of stock exchanges.

To accomplish this will require an upgrade of the Swazi capital markets, including more involvement from the government as regards the initiation of a structured privatization program. Such a move to accelerate the disinvestment of government shareholdings in government controlled parastatals, as well as the introduction of internationally attractive government bond issues, could produce positive results relatively quickly. The privatization process would assist in financing a probable budget deficit while also creating more liquidity in the Swazi stock market through the attraction of foreign investors. In addition, there would be an increase in locally generated investment, such as by the insurance and pension fund sectors.

In order for the foregoing benefits to manifest themselves in a timely and efficient manner, a framework of legislation must be in place. This legislation can be modeled on the South African experience, but the completed product should be less complex and more appropriate, and acceptable, to the Swazi market participants. Controlled market evolution will result in ongoing market generated modifications over time.

The JSE has made a quantum leap in its approach to small business development facilities. This should assist in transforming the JSE's current primary focus from a mainly institutional market to a more equal institutional and retail mix of investors over the longer term. A wide range of public awareness and educational programs are being directed at the small business sector and the general public with the objective of increasing access to the JSE and to capital for business development.

Timing is a critical issue given the rapid developments in the much larger South African financial sector and its proximity to Swaziland. The development of indigenous capital markets in Swaziland could be overwhelmed by South African financial institutions if basic steps are not acted on in the near term. The development of capital markets in Swaziland is still very embryonic. Although progress has been slow to date, this situation can be turned into an advantage as very little of the existing legislation, systems and procedures has to be redone.

The climate in Swaziland must attract both local and international investors on a pro-active basis, and not remain dependent upon investment opportunities as a result of anti-South African sanctions related policies. Tax incentives are perhaps one of the most effective methods of increasing demand for securities, as one can easily see from the pressure on the South African government to abolish Marketable Securities Tax (MST).

Despite the fact that, as of 1994, no actual stock exchange exists as a physical legal entity, in the normally accepted sense, there is a Stock Exchange Committee (SEC) chaired by the Governor of the Central Bank of Swaziland. Swaziland Stockbrokers Limited (SSL) is still the only officially licensed stockbroking firm. SSL also constitutes and operates the *defacto* stock exchange. In addition to combining functions that are normally separated, the current financial markets legislation does not differentiate between commercial banking operations and capital markets operations. As a result, the SSL license is very similar to that issued to a commercial banking operation.

The overall stock exchange process although unusual is not unique within international financial markets. However, such a monopoly would probably be unacceptable in most developed markets due to the potential for conflicts of interest. Also, legislation covering compliance functions within stockbroking firms would require a separation of tasks, as would the rules and directives governing internal exchange surveillance activities to monitor and control offenses such as insider trading by market participants.

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Successful development of Swaziland capital markets will require the establishment of at least one more stockbroking firm also acting in a market making capacity and establishment of a separate Stock Exchange. Future steps should also address the lack of financing mechanisms for small and medium size enterprise growth. There would appear to be a market niche for an Swaziland Stock Exchange capital raising vehicle, such as the proposed Development Capital Market, to help meet this financing need.

Other operational improvements are desirable. Swaziland Stockbrokers Limited permanent staffing level is rather low, even considering the limited market activity. The current Swaziland Stockbrokers Limited facilities do not facilitate the generation of overseas investment. A number of international financial institutions visit the SSL and make comparisons with other emerging markets. A move to larger, more upmarket premises will also assist greatly in implementing the proposed development plan while facilitating training programs.

As the Swaziland markets develop, the need will arise for more sophisticated banking arrangements than those presently utilized by SSL, including custodial services and electronic transfer and cash management facilities. As a precursor to that step, it is recommended that a plan be developed, as soon as possible, to upgrade the hardware and software systems at SSL. The current rather basic technology facilities available to the stock market operations (SSL) can not handle the anticipated increase in trading volume and diversification of financial instruments.

A separate software needs evaluation should be conducted with a view towards future replacement of the existing Lotus based system and Multimate word processing package. An on-line local connection to Reuters financial markets information system, which is an industry standard, should be integral to any system upgrade. Communications facilities in Mbabane are more than acceptable due to the fiber optic cable into the South Africa facilities.

Technical assistance will be required in various areas essential to creating the proper enabling environment for a stock exchange and capital markets. In order to hire and train personnel, legislation and regulations must be in place providing the foundation.

All of the tactical objectives associated with the development of the Swaziland capital markets can be achieved in a cost effective manner by utilizing the programs and products already developed by the Johannesburg Stock Exchange (JSE). In particular, the JSE public awareness and education program in the short-term, the Venture Capital Market product modified to a local Development Capital Market product in the mid-term and the JSE series of electronic trading, settlement and scrip registry products in the much longer term.

## **INTRODUCTION**

### **Terms of Reference**

The USAID Swaziland Mission has been supporting the development of Swazi financial markets and instruments with technical assistance from USAID Washington, Africa Bureau, Office of Sustainable Development. The Africa Venture Capital Project has been participating in this work, especially as regards broadening of the financial environment so as to encourage private equity capital mobilization.

The Terms of Reference for this study called for the conduct of a needs assessment for training which would impact in three areas: strengthen the technical capabilities of the Swaziland Stock Exchange dealers and brokers; upgrade the Stock Exchange's trading systems, both hardware and software; and promote public awareness and education related to share trading. The study was carried out under the African Venture Capital Project, which is managed by Harvey & Company, Incorporated. Mr. Frank B.M. Hawkes was retained as the consultant. The field work was conducted between November 15-29, 1994.

### **Methodology**

Because Swaziland is a member of the Common Monetary Area (CMA), in conjunction with the Republic of South Africa, Lesotho and Namibia, there are no exchange control regulations which would affect the free flow of investment or goods and services across those countries' borders. It was therefore pertinent to examine the latest, very fast moving, developments in the South African markets to establish to what extent Swaziland could potentially benefit from such developments.

**Johannesburg, South Africa** - Visits were held with Members and Secretariat personnel at the Johannesburg Stock Exchange, prior to and upon return from Swaziland.

**Mbabane, Swaziland** - meetings were held with a representative cross section of local government and financial markets related executive personnel. These included the Chief Executive Officer and staff of Swaziland Stockbrokers Limited (SSL) which is the one and only registered stockbroking entity currently operating in Swaziland. SSL is in the relatively unique position of operating as the *de facto* stock exchange for all Swaziland stockbroking related business, which is currently conducted in an over-the-counter (OTC) environment.

Visits were also made to local USAID mission personnel and the U. S. Ambassador to The Kingdom of Swaziland. The co-operation received from Mr. Jack Royer of USAID, Mr. Arthur Fandam of KPMG and Mr. Andrew McGuire of SSL were

of material assistance in completing most of the objectives contained in the terms of reference in a timely and efficient manner and greatly facilitated the production of this report.

## **PART ONE**

### **THE REGIONAL FINANCIAL ENVIRONMENT**

The southern Africa potential for regional financial sector integration is significant, particularly in view of the near term capital markets developments in South Africa. The very fast moving developments in the South African financial and capital markets will have a "knock on" effect not only throughout the southern Africa region but also internationally. Therefore, the future development of Swaziland financial markets within a regional framework must be taken into consideration; as should the markets' close relationships to the South African markets and specifically the counterpart Johannesburg Stock Exchange.

The JSE is moving towards establishing itself as the core African Stock Exchange Association (ASEA) stock exchange driving a southern Africa regional exchange network. It is accordingly in the best interests of Swaziland capital markets to protect their national sovereignty through a coordinated national capital markets development plan. An adequately funded and professionally managed stock market in Swaziland could prove to be a critical catalyst to ensure such a plan is developed and acted upon in the near future.

#### **I. SOUTH AFRICA FINANCIAL ENVIRONMENT**

##### **1. Financial Sector Reform**

Following the April 1994 elections, a wide range of financial sector reforms are being prepared in South Africa, as summarized below.

The Stock Exchanges Control Act 1947, which is the legislation governing Johannesburg Stock Exchange (JSE) operations, is scheduled to be amended in April, 1995. At that time, the following reforms are expected to take effect: the financial rand will cease to exist as an investment currency; banks will be allowed to become stock brokers; foreign broking firms will be allowed to purchase up to a 30% stockholding in a local brokerage firm, increasing to 100% by late 1996; and, dual capacity trading and negotiated commissions will be permitted. It is currently forecast that current exchange control will be abolished in late 1996 or early 1997.

All of the foregoing changes to current, and indeed relatively recent (e.g. April, 1994), JSE related legislation, strategy, rules and directives appear to have been forced by the South African banks. The banks have been lobbying for some years for a South African "big bang" deregulation of the financial markets, similar to the United Kingdom

in October, 1986.

These reforms are already having a positive effect on both the JSE, and on other international organizations' strategies for investment in the region. International financial institutions are buying shareholdings in South African institutions, including JSE broking firms, and establishing joint ventures.

## **2. The Availability of Financial Capital**

The JSE has made a quantum leap in its approach to small business development facilities. This should assist in transforming the JSE's current primary focus from a mainly institutional market to a more equal institutional and retail mix of investors over the longer term.

Most of the South African banks are undergoing a restructuring program in order to meet the affirmative action requirements of the Regional Development Program (RDP). There have been and will most likely be further redundancies of staff at most of the large banking groups. The banking system is still bureaucratic and lending is undertaken on a very conservative basis.

Although many of the foregoing points also apply to a lesser degree in the merchant banking sector, they are not so prevalent as in the commercial banking sector. Merchant banks such as Investec and Rand Merchant are aggressive leaders within the financial sector.

## **3. Promotion of Public Awareness**

A wide range of public awareness and educational programs are being directed at the small business sector and the general public with the objective of increasing access to the JSE and to capital for business development.

The JSE Public Relations (PR) department is responsible for all matters pertaining to public awareness, education, training and development. Ms. Heather Ferreira, Departmental Manager, reports to Mr. Roy Andersen, Executive President. A Swazi, Mr. Siniors Nkosi, is in the number two position as the Communications Officer. Examples of JSE public out reach programs are as follows:

1. Television programs directed towards the majority of the South African population as regards: the purpose and function of capital markets; the role of the stock exchange in such markets; and, the potential, as well as the mechanism for investment in these markets as compared to alternative investment opportunities

currently available.

2. Educationally focused video tape based media relative to investment in capital markets.
3. Educational seminars conducted on a multi-language basis (including Zulu) tailored to specific segments of the population and investment community.
4. Specially prepared educationally focused investment games conducted in co-operation with Radio Metro, the most popular countrywide radio station. These games are directed at:
  - schools (both teaching staff and pupils - separate programs)
  - members of the general public.
5. The establishment of the Stock Exchange Education and Endowment (SEED) Trust to provide scholarships (bursaries) to matriculated students from disadvantaged backgrounds who wish to obtain university degrees, or technikon diplomas and who may wish to become stockbrokers thereafter.
6. Co-operation with local newspapers, such as *The Sowetan*, to publish JSE information and market data, as well as general business information on a weekly basis.
7. Production and distribution of a series of booklets explaining various aspects of the JSE and its capital markets. Topics include listing on the Development Capital Market (DCM) and the new Venture Capital Market (VCM). Both markets are geared towards the financing and development of small to medium sized majority owned businesses.

These booklets have been developed for the 80% of the population who are standard five readers (the last year of pre-high school) and thousands have been distributed free of charge.
8. Developing links with business groups such as: the Black Management Forum (BMF); the Foundation for African Business and Consumer Services (FABCOS); and the Association of Black Accountants (ABA). These organizations are invited to the JSE for meetings and presentations and JSE personnel visit these groups in the capacity of guest speakers.
9. Marketing local township equivalent of unofficial credit unions, (i.e. "stokvels"), to place their investment capital into the JSE markets.

## II. SWAZILAND FINANCIAL ENVIRONMENT

Timing is a critical issue given the rapid developments in the much larger South African financial sector and its proximity to Swaziland. The development of indigenous capital markets in Swaziland could be overwhelmed by South African financial institutions if basic steps are not acted on in the near term.

### I. Government Constraints to Investment

The development of capital markets in Swaziland is still very embryonic. Although progress has been slow to date, this situation can be turned into an advantage as very little of the existing legislation, systems and procedures has to be redone. However, there is a relatively short two to three year window of opportunity in which to get the basic necessary framework into place and the market entities up to an acceptable quality of operation.

Almost all interviewees expressed the opinion that preserving the integrity and sovereignty of Swaziland's markets is of paramount importance to the controlled local development of the financial system. They want to be in charge of their own destiny (and markets) and not be wholly dependent upon externally generated business from countries such as South Africa. Now that there is a majority government in South Africa, it is felt to be of critical importance for Swaziland to create its own investment climate. The climate in Swaziland must attract both local and international investors on a pro-active basis, and not remain dependent upon investment opportunities as a result of anti-South African sanctions related policies.

Tax incentives are perhaps one of the most effective methods of increasing demand for securities, as one can easily see from the pressure on the South African government to abolish Marketable Securities Tax (MST). Specific fiscal incentives which could be promoted through the Central Bank and MoF include:

- Elimination, or reduction of withholding tax on dividend earned on equity investments (currently 10%) to bring them significantly below the prevailing rate for competing investments.
- A tax policy that would allow investors to deduct some of the amount invested in capital market instruments, or at least in new issues, from income tax.
- Special tax incentives to promote participation in investment funds.

**A number of important steps can be taken by Swaziland authorities to promote capital markets development:**

- Legalize the status of an independent Swaziland Stock Exchange (SSE);
- Modernize both SSE and Swaziland Stockbrokers Limited (SSL) premises, staff, technology and operating procedures;
- Implement a public awareness and training program starting at the government level;
- Strengthen the legal environment with new laws including - Companies Act, Insurance and Pensions Act and Securities Act and related fiscal incentives;
- Implement an accelerated privatization program;
- Innitiate a Venture Capital Market (VCM) and Development Capital Market (DCM) structure.

## **2. Availability of Financial Capital**

The initiative for the formation of a local stock market in Swaziland was first promulgated by the Hon. Minister for Finance, Mr. B. S. Dlamini, in the budget speech of 1989/1990. A feasibility study was then undertaken in conjunction with the British Commonwealth Development Corporation (CDC) as regards the establishment of a primary capital raising vehicle for Swaziland.

Despite the fact that as of 1994 no actual stock exchange exists as a physical legal entity, in the normally accepted sense, there is a **Stock Exchange Committee (SEC)** chaired by the Governor of the Central Bank of Swaziland. The SEC has the principal responsibilities of market oversight and ensuring the maintenance of an orderly and efficient market. The SEC Management Committee is comprised of:

- The Governor of The Central bank of Swaziland;
- The Deputy Governor of The Central Bank of Swaziland;
- The Principal Secretary of the Ministry of Finance;
- One practicing Attorney;
- One practicing Auditor.

There is also a functioning **Listings Committee** which is chaired by the Deputy Governor of the Central Bank which has responsibility for:

- evaluation of new listing applications;
- reviewing and recommending possible new listings;
- monitoring and sustaining approved listings.

The *defacto* stock market commenced trading on an Over-the-Counter (OTC) basis in July 1990 with the listing of the first publicly offered company, Standard Chartered Bank Swaziland Limited. On approximately the same date, Swaziland Stockbrokers Limited (SSL) was capitalized at E500,000<sup>1</sup> and established under the supervision of the Central Bank of Swaziland as a registered financial institution, pursuant to the provisions of the Financial Institutions Order of 1975. SSL is still the only officially licensed stockbroking firm. Contrary to market norms and due to the current financial markets legislation, the SSL license is very similar to that issued to a commercial banking operation. To illustrate the potential conflicts, the approved listing procedures and rules utilized by the Listings Committee were produced by SSL.

At this early stage in the development of capital markets in Swaziland, a single firm, SSL, performs the functions applicable to a stockbroking firm, as well as acting as the exchange itself. That is, SSL staff:

- conduct primary trading on an agency basis within an order driven Over the Counter (OTC) type marketplace;
- prepare corporate research, compile market data and co-ordinate dissemination of same. and act as issuing broker during the company listing process;
- perform the listings review function (but it is the responsibility of the Stock Exchange Committee (SEC) to act as the approval body for the actual listing);
- Note: issuance of share certificates is conducted by the registrar from whom SSL collect certificates on behalf of shareholders who have subscribed via SSL.
- delivery of the certificates is done by hand from SSL to the subscriber.

The overall process although unusual is not unique within international financial markets. However, such as monopoly would probably be unacceptable in most developed markets due to the potential for conflicts of interest. Also, legislation covering compliance functions within stockbroking firms would require a separation of tasks, as would the rules and directives governing internal exchange surveillance activities to monitor and control offenses such as insider trading by market participants.

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<sup>1</sup> E = Emalangeni which is the local currency and is currently traded at par with the RSA Rand, i.e., as at November, 1994, \$1.00 is approx. equal to SAR/E 3.55 middle rate.

### 3. Functioning of the StockExchange

The market mechanism governing stock market transactions and operations is based around an over-the-counter market with SSL acting as the broker soliciting buyers and sellers for any instruments that are deemed tradeable in the existing highly illiquid market. SSL also acts in the capacity of and performs the main functions of a stock exchange.

The Swazi stock market is order driven and currently consists of agency trading only. All shareholding is currently localized, although non-resident shareholders are theoretically permitted providing exchange control approval is obtained through the Central Bank. Exchange control is also imposed for all non-CMA related transactions within the financial markets.

Brokerage is calculated on a sliding scale fixed commission basis; the range is from 1% for transactions of E100,000 and above down to 2% for transactions up to E49,999 with a middle rate of 1.5% on transactions of E50,000 to E99,999. Settlement is achieved via the medium of checks and is performed on a transaction by transaction basis. Trading hours are officially from 10.00 AM to 12.00 noon which is, coincidentally the "official" working hours of SSL CEO.

There are currently four listings on the market. Listings have been added at a rate of approximately one per annum since SSL inception in 1990. The market (capitalization) trades at between 0.0% and 0.3% on a monthly basis. The approximate averaged annualized figure is 0.1% as compared to the JSE's 3% - 5% and an exchange such as the NYSE at 30%. The relative financial capitalization figures are between E900,000m and E1,100,000m approx. Market turnover for 1994 is running at 1 - 8 deals a month, comprising between 600 and 515,000 shares for a value of E800 to E2,700,000 (E1 = ZAR1 = US\$3.5 at the middle rate).

A May, 1994 report produced by Hugh Cleland Associates, on behalf of the International Finance Corporation (IFC) recommended changes in the stock exchange operation. A response addressed to the Minister of Finance is now being drafted by SSL.

### 4. Future Development Scenarios

There are at least three possible scenarios applicable to the development of the financial/capital markets in Swaziland.

- *Do nothing and allow the JSE in South Africa to independently drive a southern Africa regional stock exchange federation development program.*

**Benefits:** Little, or no funds, would be expended in Swaziland.

**Limitation:** Swaziland would be seen as a satellite province of South Africa and not an independent sovereign state, with the implication that Swazi monetary and economic policy could be controlled, in effect, rather than purely influenced by, Pretoria.

- *Provide sufficient funding to allow for a minimal upgrade of the current Swazi stock market corporate entity and the establishment of a very basic, officially registered Swazi stock exchange.*

**Benefits:** Establishment of a registered stock exchange, referred to herein as the SSE, will probably be required under the forthcoming securities legislation. The Swazi market participants would be seen by the local government and the outside world to be doing something positive and tangible. The correct level of funding, together with timing of same is critical to providing positive, very tangible results.

**Limitations:** If not properly managed and controlled, the implementation of this scenario could prove in the long term to be just as much of a "market killer" as following scenario one above. A minimalist approach could result in a structure that would very quickly run out of processing capability and would not have the long term resources to take advantage of ongoing developments within the region. A lack of capacity could force both local and international investors to place their funds through foreign brokers in other emerging markets in the region, exchange control legislation permitting. Limited capacity would also act as a disincentive to the possible establishment of additional broking firms in Swaziland by both local and foreign financial institutions.

- *Position Swazi capital markets participants to take advantage of the post "big bang" markets in South Africa as well as facilitating their active role in the regional development activities of the sub-Saharan stock exchanges on an equal partner basis. The recommendations contained in this report suggest such a phased approach implementable over two to three years.*

**Benefits:** An accelerated local privatization program and the development of a South African modelled small business Venture Capital Market or Development Capital Market, to increase local stock exchange listings, trading volumes and market liquidity would provide lasting economic benefit to the country as a whole. The resulting increase in trading could, on an almost immediate basis, substantially increase the current Swazi stock market (SSE/SSL) income stream.

The possibility of funding other stock exchanges in the region, inclusive of the JSE, should be considered. Such funding, would greatly facilitate the controlled development of a truly regional capital markets federation. Logically, the JSE would act as the central exchange within such a federation but the other regional exchanges, if

adequately funded in a timely manner, would be able to develop in parallel and not just on a piecemeal basis. Joining in any future JSE electronic initiatives would prove easier and more cost effective if the other exchanges were developed in a coordinated manner.

**Limitations:** Trying to connect to a mix of procedures and systems which have been developed independently in each country will increase costs and reduce benefits.

Successful development of Swaziland capital markets will require the establishment of at least one more stockbroking firm also acting in a market making capacity. It is also recommended that a reorganized Swaziland Stockbrokers Limited (SSL) consider a strategic alliance with a JSE member broking firm. It is not beyond the realm of possibility that the reorganized SSL could, in the mid to long term, become a JSE corporate member firm just as many other foreign broking firms are scheduled to become along with South African financial institutions in the near future.

In order for the JSE to consider the SSL as a member, the SSL would have to meet all of the revised membership criteria, including capitalization, which will result as an integral part of the updated rules and directives following the forthcoming amendments to the Stock Exchanges Control Act 1947. It would be necessary for the SSE to have been formally established as a completely separate legal and operating entity and for internationally acceptable legislation to be in place governing the operations of the stock market overall. The SSE should be a member of the African Stock Exchanges Association.

## **5. Financing Formal Sector SMEs**

The principal source of current small business development funding in Swaziland appears to be the Swazi Growth Trust and its subsidiary, the Growth Trust Corporation, which has a relatively small E3 million loan portfolio placed in the market. The local Development Banks are not well regarded within the financial community and are not reported to be in good financial condition. The commercial banks do not concentrate on small business development. At the same time, they appear to be losing money in their retail segment due to relatively high operating costs compared to segment profitability.

The lack of financing mechanisms for small and medium size enterprise growth would appear to leave open a market niche for an Swaziland Stock Exchange capital raising vehicle, such as the proposed Development Capital Market. Local sources report that there would be no shortage of investors who would trade in such stocks, if available through the medium of an approved and controlled stock exchange entity operating within a framework of internationally accepted legislation.

Swaziland operates, from a capital market participants' viewpoint, along very similar lines to its counterparts in South Africa. Instruments traded include:

- . Equities;
- . Corporate debentures
- . Government bonds (commonly called "government stock");
- . A dual listing with the JSE - E.X. Lonrho Sugar Corporation;
- . A capital weighted index (the SSM).

Small and medium size enterprises (SMEs) have limited access to this market, as is currently the case in South Africa. Further liquidity would be generated by:

- . The establishment of a JSE style development capital market with reduced listings requirements specifically targeted towards small businesses that do not meet the current listings requirements for local flotation on the stock market.
- . An accelerated government led privatization program for entities, such as the Swaziland Posts and Telecommunications Corporation.
- . The introduction of a two tier corporate tax system in favor of public companies listed on the market. The granting of a tax break to newly listed companies for a fixed period of time, perhaps one to two years.

It should be noted with concern that the board of directors of SSL approved a dividend of E110,000 for the fiscal year ending June 30, 1994, a four-fold increase over the previous year. Given the SSL is in every sense a developing stage organization and has requested grant assistance from the GOS and international donors, this excessive dividend payment may not be received well. The donor community may feel that SSL could, in the future, finance training and promotion from its own resources.

## PART TWO

### III. PROMOTION OF AN EFFECTIVE STOCK EXCHANGE IN SWAZILAND

#### 1. Assessment of the Current SSL Staffing

At the time of this report, the Swaziland Stockbrokers Limited operation consisted of one full time staffer and one part time officer who, in actuality, appears to work almost full time on SSL related business. The workload is heavy for this small staff dealing with administrative work in relation to local stock market business, public relations and marketing oriented activities. In addition, a growing number of overseas visitors are coming to the SSL on request briefings and capital markets information. These activities are directed towards obtaining inward investment from overseas and from South Africa, as well as market to market liaison activities with other exchanges and market participants both internal and external to the sub-Saharan Africa region.

Swaziland Stockbrokers Limited permanent staffing level is rather low, even considering the limited market activity. Staff includes:

- One officially part time Managing Director, who also operates as a consultant to local financial institutions;
- One secretary/receptionist/office clerk;
- One temporary clerk/messenger;
- One full time clerk/computer operator.
- Two staffers on overseas study leave at Australian and British universities (Australian government and ODA financed).

During the course of this study, the full time clerk went to Washington, D.C. on a USAID sponsored conference and the temporary clerk resigned to join the local development bank. In spite of these limitations, it should be noted that, although the pace of work is slower than in a more developed environment, the staff appear to work quite hard and are very conscientious in their duties. The SSL staff's reputation within the local community is very high and the CEO, who has worked in the Swaziland financial sector for some years, appears to be well known and respected for his dedication and honesty.

## 2. Assessment of the Current SSL Premises

SSL occupies two small basically furnished offices separated by a secretarial position, which includes minimal waiting facilities. Each room has only one power point (plug socket) and one desk. The slightly larger office also contains a small round table which could accommodate four people for an impromptu but very public meeting. SSL board meetings are held elsewhere; the CDC office is the most popular venue.

The current Swaziland Stockbrokers Limited facilities do not facilitate the generation of overseas investment. A number of international financial institutions visit the SSL, such as J.P. Morgan and Chase Manhattan Bank, and make comparisons with other emerging markets. A move to larger, more upmarket premises will also assist greatly in implementing the proposed development plan while facilitating training programs.

The Swaziland Stock Exchange space planning for physically separate premises from the SSL should include: sufficient space and office facilities to initially accommodate the President and an administrative assistant; a surveillance/listings function and a technology-administration function plus a reasonably sized conference or boardroom and ancillary facilities as in the case of SSL above. A corporate standard, for instance using locally produced furnishings, should be agreed for both entities as an integral facet of the development of a common corporate image program.

The recommended square footage for a new stock exchange facility should be at least three times larger than present. This should include the appropriate number of offices (both private and general), together with a conference or boardroom which could be utilized for small seminars. Items of equipment, such as an overhead projector, flip charts and chalk boards should be included in the equipment budget. The new premises should include the following at a minimum:

- A reasonably equipped waiting cum secretarial area;
- A suitably equipped office for the Managing Director;
- A general office to take at least four staff plus equipment for back office and administration work;
- An office suitable for the compliance and research functions;
- A trading office suitable to facilitate electronic trading in due course;
- A conference or boardroom large enough to accommodate the existing board members plus 20% extra space for visitors, or seminar usage;

- A spare office suite for four people to allow for expansion and visitors such as consultants as well as acting as an in house training facility;
- A small technology and equipment room;
- Toilet/kitchen facilities integral to the SSL premises, (ideally).

### 3. Operations Support

As the Swaziland markets develop, the need will arise for more sophisticated banking arrangements than those presently utilized by SSL, including custodial services and electronic transfer and cash management facilities.

Consideration could be given to identifying a commercial bank, such as Meridien BIAO Bank Swaziland Limited, that could meet these future requirements. Meridien BIAO possesses modern management methodology and operations, utilizes state of the art technology (U.S. made in most cases) and has taken an aggressive stance in the market. Their twenty 23 country sub-Saharan and international network would also make them an ideal contender as a potential regional stock exchange federation bank. Other financial institutions should also be considered as and when a decision is required regarding the role of banks within the Swazi marketplace.

### 4. Hardware

As regards equipment, the situation is also rather basic. There are two old computers (P/C's) with 5.5 inch drives; one of which belongs to SSL and the other, upon which all of the back office accounting is processed, belongs the Managing Director. There is one dot matrix printer; one answerphone; one small fax machine and one telephone extension in each area.

It is strongly recommended that a plan be developed as soon as possible to upgrade the hardware and software systems at SSL. The current rather basic technology facilities available to the stock market operations (SSL) can not handle the anticipated increase in trading volume and diversification of financial instruments.

A suggested hardware upgrade could include an IBM (or, top class compatible) system of three to four networked Personal Computers (PCs) operating in a file server mode. These would be supported by at least three printers; one of which should be an office sized laser operating off the network (LAN). A small Uninterruptable Power Supply (UPS) is essential due to the local incidence of power failures.

The new hardware should be capable of being upgraded or migrated, as and when the need arises. It should also be able to cope with the processing of a five year volumes

forecast without having to replace the core network. This is particularly important should the SSE and SSL systems eventually be connected into the JSE's proposed electronic trading system which currently operates on Stratus (or, the "badge engineered" IBM system 88) hardware. SSE's technology needs will have to be evaluated also but should initially be less than SSL's. However, standard hardware and office software should be used by both organizations to facilitate ongoing compatibility and economies of scale.

A feasibility study as regards the JSE's implementing an electronic trading system has been conducted. The chosen system will be implemented for the equity market in the relatively near future to replace the current system of "chalk boards" and open outcry floor trading. Although the final decision has yet to be made, the current "favorite" for implementation is the Stratus based system originally developed by TCAM Systems of New York for the Vancouver stock exchange. This system was also recently purchased, redeveloped and considerably upgraded by ex London stock exchange personnel for Tradepoint Financial Services Network plc, the new automated equity exchange operating in London.

As JSE personnel and associates have performed various systems oriented review assignments and during the review process have worked closely with vendors such as TCAM (and their clients) and have established personal contacts at numerous exchanges, including Tradepoint, it is recommended that they should be approached should further information be required regarding this system.

## **5. Software**

All of the office systems have been built in house around Lotus 123 spreadsheets and the Multimate word processing package, supported to a great extent by manually oriented procedures. A separate software needs evaluation should be conducted with a view towards future replacement of the existing Lotus based system and Multimate word processing package. An on-line local connection to Reuters financial markets information system, which is an industry standard, should be integral to any system upgrade.

## **6. Communications Infrastructure**

Communications facilities in Mbabane are more than acceptable due to the fiber optic cable into the South Africa facilities. As South Africa also has an excellent Saponet network which facilitates, for example, X.25 transmission internationally, Mbabane has an adequate mode of international communications. The local ISDN, including data transmission is being implemented on a countrywide basis; except the topography from Mbabane to Matshapa (airport about 45 kms away) inhibits implementation. The local Meridien Bank has solved this problem by the interim

utilization of radio modems and microwave transmission into their Automated Teller Machine (ATM) network outside of Mbabane. Other high technology services are in process of implementation, including "smart card" vendor and purchaser systems.

#### **IV. TECHNICAL TRAINING PLAN**

Technical assistance will be required in various areas essential to creating the proper enabling environment for a stock exchange and capital markets. In order to hire and train personnel, legislation and regulations must be in place providing the foundation. Accordingly, observations regarding these framework issues are presented below.

##### **1. Legislation**

It is essential that an internationally acceptable financial sector framework of legislation be in place as soon as possible. This will assist in establishing investor confidence in the Swazi markets, as well as facilitating effective and efficient market oversight and control by the appropriate governmental and commercial bodies. Such a framework should assist in accelerating the development and growth potential of the local stock market, thus bringing it up to a regionally acceptable level of operations within a relatively short period of time, preferably during 1995.

The financial sector framework should take into consideration the content and timing of the amended Companies Act about to go before Parliament, as well as other securities legislation in operation within the region, such as the various laws, rules and directives governing the South African markets. The original Swaziland Companies Act was based upon the South African counterpart. The legal system prevailing in South Africa is based upon Roman-Dutch law and not upon English law which is the base of the legal systems of the United States and the United Kingdom. Therefore, changes in the Act and related legislation will most likely be based on South African law.

##### **2. Stock Market Framework - Legal Entities**

The current situation whereby the only legal entity operating and effectively controlling the local capital markets is the registered financial institution, Swaziland Stockbrokers Limited (SSL), should be addressed in the near term. Consideration should be given to forming a separate legal entity, such as The Swaziland Stock Exchange (SSE), registered under existing legislation to take over some of the various responsibilities, including new company listings, now performed by SSL.

From an international viewpoint, the present multiple functions performed by the

SLL would not be legally permitted. Under most countries' securities laws, the inherent potential for such abuses as "insider trading" and "market manipulation" would require separate legal entities split these market functions. A local consulting firm advised that the establishment of a separate legal entity could be accomplished within two weeks and would cost approximately E1500.00, i.e. \$420.

The timing for establishment of separate Swaziland Stock Exchange (SSE) is further impacted by the statutory local investment requirements of the new Insurance and Pensions Act. Under that Act, 15% of investment funds must be invested in Swaziland. As this requirement takes effect, the trading volume will increase significantly, thus increasing the need for market oversight and controls.

Both organizations would require separate premises in order to comply with commonly accepted international guidelines on compliance and market surveillance.

It should be noted that in the absence of other broking firms in Swaziland, members of the existing Board of Directors of SSL, which would then be re-classified as a member of the SSE, could elect an SSE Management Committee from among their current members, one of whom could then be elected Chairman of the SSE.

The foregoing recommendation would also facilitate the SSE's joining any possible Regional Exchange Federation, similar to the FIBV. The SSL, being a broking firm with a banking license, could not now join a federation or association of stock exchanges on a full member basis.

### **3. Technical Training**

There is a critical need for training programs to be developed for target audiences at all levels, both internal to and external to the stock market itself. Priority areas to be addressed as soon as possible would include:

- stock market personnel;
- government (e.g. Parliament, Ministry of Finance);
- educators and education facilities (e.g. schools etc.);
- commercial sector, including pension fund administrators;
- the general population.

### **4. Swaziland Stock Exchange Staff Training**

All staff recruited for the SSE in its proper legalized form will have to be trained in the functions they will be required to perform at the exchange. Training should include functions such as:

- listings;
- exchange administration;
- exchange systems and technology;
- and surveillance.

Training could be conducted in conjunction with another stock exchange within the region. Broking staff for SSL can best acquire their practical knowledge through secondment to an established broker with which SSL has a strategic alliance. In order for training to be meaningful within the context of the Swazi markets, all securities legislation should be in place, as should an officially sanctioned set of rules and directives for SSE's operations before training begins.

A draft action plan focusing upon the sequencing and timing of the objectives effecting these immediately identifiable training needs and priorities is attached in an Appendix. Personalized staff training programs, including specially tailored modern management studies, could be developed by local management, assisted when required by external consultants.

## 5. Site Orientation Visits

Direct knowledge of other regional stock exchanges operations is invaluable when developing legislation and operating procedures. Accordingly, selected senior personnel from the SSL board and the Ministry of Finance could conduct a series of visits, phased over the next one to three years, to:

- Regional stock exchanges in Johannesburg; Namibia; Botswana, Harare and possibly, Nairobi.
- The Vancouver stock exchange (due to the nature of the electronic system utilized - probably the one that will be implemented by the JSE). This visit should only be made if the JSE purchase and implement the VSE system.
- Institutions in London, (providing electronic trading is selected as the SSE's trading mechanism over the longer term).
- Tradepoint Financial Networks plc (a registered stock exchange utilizing their own locally developed and more up to date version of the Vancouver stock exchange electronic trading system).
- The OMLX - The small but efficient and effective London operation of a Swedish exchange which uses an electronic system on a Europe wide basis. Providing the JSE goes electronic trading and the proposed SSE also adopts this trading mechanism over the longer term, the OMLX is probably the best exchange that

could act as the ultimate "blue sky" model for any small well funded electronic exchange operating within a regional framework.

- Reuters - to review the latest Reuters systems applicable to capital markets, including their new equity markets products. It would also be logical to incorporate Reuters Johannesburg into any South African visit, with a U.K. visit only in the longer term.
- The Securities and Investment Board (SIB) - to review current securities legislation and oversight procedures.

## V. PUBLIC AWARENESS AND EDUCATION PLAN

Almost all of the market and product training and education concepts and materials which could be deemed necessary for the development of the Swaziland capital markets can be obtained through the Johannesburg Stock Exchange and easily modified for local utilization. Mr. Siniors Nkosi, JSE Communications Officer, who has been responsible for the development and implementation of almost all of the JSE material is the recommended point of contact. Specialized JSE sub-contractors, such as Progressive Systems, could be contacted through the JSE and their current product range reviewed for possible utilization in Swaziland.

The further possibility of modifying the JSE school pupil training games for Swaziland, as well as the television and video media could be investigated by SSL or SSE personnel in order to include in their own program what they deem appropriate to the development of their local marketplace.

A local program (modelled on the JSE material and possibly including a special seminar) could be developed and directed towards the Swaziland parliamentarians as an integral facet of the final SSE plan. See section II. 3. for details as to program activities which would be appropriate in Swaziland.

## APPENDIXES

1. Interview list
2. SSE/SSL Operations Plan
3. Swaziland Stock Market
  - 3.1 Listing of Securities: Requirements and directions for the guidance of companies
  - 3.2 Listing particulars: Requirements for an advertised pre-listing statement or prospectus. (Both sets of rules produced by SSL)
4. Swaziland Stock Exchange (SSE)
  - 4.1 Overview paper as at March 1994
5. Swaziland Stockbrokers Limited (SSL)
  - 5.1 Draft Corporate Strategy
6. Johannesburg Stock Exchange
  - 6.1 Changes in the South African Financial Environment
  - 6.2 Public Relations Department
    - 6.2.1 Press release dated 8th November, 1994 (proposed changes)
    - 6.2.2 Copies of public awareness/educational material (being mailed from the JSE)
  - 6.3 Research and Development
    - 6.3.1 Copy of the April, 1994 (500 page) report of the research sub-committee of the JSE entitled "Future structure of the JSE" (partially obsolete due to more recent developments)
7. Copies of Swaziland company prospecti
8. Copies of Swaziland company annual reports

9. Copy of IFC report by H. Cleland Associates to The Hon. Minister of Finance, Swaziland on "Necessary/ useful steps toward a more active market for securities in Swaziland"
10. Copy of JSE annual report as at 26th April, 1994
11. Copies of media clippings
12. Copies of current SSL personnel bio-data
13. Copy of current SSL balance sheet (annual accounts)

## Appendix 1 Interview list

### A. Johannesburg: 15 - 16 November, 1994

1. Mr. Ian J. Mitchell - Senior Consultant: Financial Risk, ABSA Bank - Management Training and Development (Ian is de facto Assistant General Manager of the division but was assigned the "Senior Consultant" title for exchange control purposes)
2. Ms. Madeleine de Balmain - Executive Secretary & P. A. to Roy Andersen, Executive President of the JSE
3. Ms. Heather Ferreira - Manager, Public relations (JSE) (Heather and Mr. Sinors Nkosi - Communications Officer have been directly responsible to Roy Andersen for developing and implementing all of the public awareness/ education programs for the JSE)
4. Ms. Leanne Parsons - Planning Analyst and assistant to Mr. Darrell K Till, Executive Consultant - Research & Development (JSE)
5. Mr. Ed Hern - Chairman, Ed Hern Rudolph Inc. (JSE)
6. Mr. R. A. (Tony) Norton - Director, Fergusson Bros. Hall Stewart & Co. Inc. (Tony was the Executive President of the JSE immediately prior to Roy Andersen)
7. Mr. Peter G. Redman - Managing Director, Mathison & Hollidge Inc. and member of the JSE Main Committee (Peter is a past Chairman of the JSE and was a member of the board of SAFEX, the South African Futures Exchange)

### B. Mbabane: 18 - 27 November, 1994

1. Mr. Jack Royer - Program Officer, USAID Swaziland
2. Mr. Andrew McGuire - Chief Executive Officer, Swaziland Stockbrokers Limited. (Mr. McGuire is in essence also Executive President of the Swaziland Stock Exchange)
3. SSL/SSE personnel
  - 3.1 Ms. Grace Ncongwane
  - 3.2 Mr. Welcome Maphalala
  - 3.3 Mr. Godfrey Magagula
4. Mr. Martin G. Dlamini - Deputy Governor of The Central Bank of Swaziland

5. Dr. Michael S. Masebula - Chairman, SSL (and other local businesses, inclusive Royal Swazi Insurance Company and Royal Swazi Airlines)
6. The Honourable Dr. John Sprott - U. S. Ambassador to The Kingdom of Swaziland
7. Mr. John J. H. Kivits - Managing Director, Standard Chartered Bank Swaziland Limited
8. Mr. Arthur H. Fandam - Partner, KPMG Aiken & Peat, Chartered Accountants (Swaziland)
9. Mr. Jeffrey L. Jackson - Consultant assigned to the Swazi Business Growth Trust and the Growth Trust Corporation, (Jeff was formerly assigned to the Ministry of Finance)
10. Mr. Roger L. Sheriff - Deputy Managing Director and Secretary, Barclays Bank of Swaziland Limited (most impressive and high tech oriented of all the Swaziland banks)
12. Mr. Geoffrey P. West - Chief Economic Planning Adviser, The Ministry of Economic Planning & Development
13. Ms. Valerie Dickson-Horton - USAID Mission Director, Swaziland
14. The Hon. Dr. John Sprott - U. S. Ambassador to The Kingdom of Swaziland (second meeting and draft report review, at his request)
15. Mr. Isaac Shabangu - The Hon. Minister of Finance for The Kingdom of Swaziland

**C. Johannesburg: 29th November, 1994**

1. Mr. Roy C. Andersen - Executive President, The Johannesburg Stock Exchange
2. Mr. Francois Tolken - Chairman, The Johannesburg Stock Exchange
3. Ms. Heather Ferreira - Manager, Public Relations, The Johannesburg Stock Exchange\* (second meeting to further review training/ public awareness products and material)
4. Mr. Sidney Frankel - Chairman, Frankel, Pollak Vinderine Inc., The Johannesburg Stock Exchange
5. Mr. John Wright - Executive Director, Meridien International Bank Limited, Sandton (Johannesburg)