Capital Market Master Plan
2014 - 2023

2nd Edition 30th April, 2016

CAPITAL MARKETS AUTHORITY

KENYA VISION 2030

CAPITAL
MARKETS AUTHORITY
Promoting the Integrity and Growth of the Capital Markets

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FOREWORD

The launch of the Capital Market Master Plan (the "Master Plan") represents a significant milestone in the history of Kenyan Capital Markets. It marks the first comprehensive strategic plan, formulated in collaboration with all stakeholders to chart the development of the capital market for the next ten years. This Master Plan was driven by broad consultation with internal and external stakeholders, including international benchmarking with jurisdictions that have instituted financial sector reform strategies, attained International Financial Centre (IFC) and/or Gateway status or developed diversified and sophisticated capital market products and services. The Master Plan forms a crucial guide in our journey to realize our vision to become ***"The Heart of African Capital Markets".*** With growing pressure on the traditional sources of government revenue as we implement programmes under the devolved government system, this Master Plan comes at a time when there is need for clear strategies to position the capital market to take up a central role in the next stage of development.

Kenya currently falls under the class of "frontier" economies with consistent economic performance. The economy has remained strong and resilient on the account of commitment by the Government to implementation of transformative economic policies and structural reforms. One of the five key areas under the country's 'Strategy for Economic Transformation' relates to *creation of a conducive business environment in order to encourage innovation, investment, growth and expansion of economic and employment opportunities.* The growth and stability of our financial system is expected to play a major role in promoting and facilitating investment and growth opportunities. Capital markets, being one of the main sub-sectors under the financial services will be pivotal in ensuring the growth and stability of our financial system.

The Financial Services Sector (FSS) is critical to achieving the Vision 2030 target of 10 per cent annual average economic growth and requires that the sector stimulates significant increase in investments and savings through mobilizing both domestic and international resources. The aspirations articulated for the FSS in the Vision is to **"Create a vibrant and globally competitive financial sector that will promote a high level of savings to finance Kenya's overall investment needs".** The second Vision 2030 Medium Term Plan 2013 – 2017 (MTP II) identifies the Capital Markets as key drivers of the FSS and lays out ambitious targets along the dimensions of Access, Stability, and Efficiency. In terms of **Access,** the plan targets to increase overall access to formal financial services to 90.0 percent by 2017 up from 66.7 percent in 2013. In terms of Stability the target is to significantly reduce the volatility in the stock exchange indices whereas under **Efficiency** the plan targets to boost Liquidity Ratios and the ratio of Bonds Turnover to Bond Market Capitalisation.

In order to achieve these targets the MTP II has identified two key flagship projects targeted to increase gross national savings from 16.2% of GDP to 27.7% of GDP. Similarly, investments as a percentage of GDP were projected to increase from 23.2% to 32.6% over the same period. Capital Markets as key drivers for long-term resource mobilization were to play a central role in raising savings and investments levels. For the economy to grow at the desired GDP rate, equity, and bond market capitalization were expected to increase from 50% and 16% to 90% and 30% of GDP respectively by 2012. The current figures of equity and bond market capitalization stand at 50 percent and 25 percent respectively; hence the MTP I targets were not achieved. There is therefore need to further deepen the capital markets as recognised in projections in the Master Plan of 70 percent and 40 percent, respectively, by 2023.

The vision articulated for the financial services sector in the Kenya Vision 2030 is to **"Create a vibrant and globally competitive financial sector that will promote high level of savings to finance Kenya's overall investment needs".** In order to achieve this vision, the second Medium Term Plan (MTPII) has identified two key flagship projects for the financial services sector namely: the establishment of the Nairobi International Financial Centre (NIFC) and the development and implementation of a Capital Market Master Plan. These projects are mutually reinforcing and each needs to be addressed to ensure a vibrant sector that effectively finances the country's investment needs for sustainable development. The Capital Market Master Plan is intended to support the development of Nairobi as an International Financial Centre in a number of important ways.

Improvements to legislation and regulation governing capital markets are likely to create an attractive institutional environment for users of the Kenyan market place and the International Financial Centre in particular; upgrading of financial market infrastructure will contribute towards creating an attractive proposition for would-be international entrants. Since financial service companies located in the NIFC are likely to draw upon domestic skills, initiatives to build capacity in Kenyan financial markets will create a deeper, more knowledgeable and diversified pool of capacity to support the NIFC. Targets contained in the Master Plan to achieve Morgan Stanley Capital International (MSCI) Emerging Market status and to improve Anti-Money Laundering (AML) and Combating the Financing of Terrorism (CFT) guidelines will also assist in attracting foreign firms to the NIFC by ensuring compliance to internationally accepted standards.

World over, the performance of the capital markets are an important barometer for measuring the economic health of a country. To date, notwithstanding the capital markets' active role in mobilizing funds and facilitating economic development, challenges to optimal utilization remain including: limited institutional investors, a narrow retail investor base, inadequately diversified financial products, uncompetitive transaction costs, low investor awareness and dominance by financial institutions as compared to the real sector companies at the securities exchange. These challenges must be addressed given greater demand will be placed on our capital markets in the coming years to achieve our national aspirations.

In the context of the heightened global competition it is timely that pragmatic measures are put in place through this comprehensive vision and road map for the development of the industry. The Master Plan will ensure that the capital market is well positioned to support national economic growth and to meet future challenges from regional competition and globalization as Kenya endeavours to be an International Financial Services hub.

I would like to sincerely thank the Capital Markets Authority, the Capital Markets Master Plan Steering Committee (CMMSC), and all other stakeholders who have provided their valuable support and input to the Master Plan. Ultimately, the success of this Master plan will be determined by the extent to which it will be successfully implemented. This calls for combined efforts and commitment of all concerned, particularly market participants and the relevant capital market institutions, to ensure that Kenya's capital markets emerge as a center of excellence and a gateway for regional and international capital flows.

Mr. Henry Rotich
Cabinet Secretary, The National Treasury

INTRODUCTORY REMARKS

In order to support the successful execution of the role of the capital markets in national economic growth, the Capital Markets Authority, in partnership with key stakeholders in the Kenyan capital markets, has developed this Capital Market Master Plan to set down the strategic direction for the Kenyan capital market, over the next 10 years.

This Master Plan envisages that by 2023, Kenya will be transformed into the choice market for domestic, regional and international issuers and investors looking to invest in and realize their investments in Kenya, within East Africa and across Middle Africa. The Kenyan capital markets will be the center of excellence for supporting the financing of the real sectors of the economy in which Kenya already has significant capacity and potential, including agriculture, infrastructure (including real estate), and technology, while also leveraging the strength of Kenya's broader financial sector to develop innovative products and services, including derivatives, asset management and Islamic finance.

This transformation will be achieved through the development of dynamic and liquid markets based on international standard financial market infrastructure and strong and independent supervision. This necessitates a legal and governance framework that inspires confidence and ensures the perception and realization of an open, competitive market place. The objectives set out in the Master Plan have therefore been formulated with a view to ensure the following key results:

- Build on recent market reforms to address regulatory and institutional constraints in order to strengthen market infrastructure, intermediation, oversight and governance standards;
- Stimulate innovation to broaden product and service offerings, deepen market participation and liquidity, and drive transformative economic development;
- Streamline and augment funding for developmental projects under Vision 2030, and provide alternative financing sources for the implementation of devolution;
- Establish the Kenyan capital markets as a centre of excellence and as a gateway for regional and international capital flows; and,
- Reinforce the development of Nairobi as an International Financial Centre and in the medium term, pursue the elevation of Kenya's ranking from Frontier Market to Emerging Market status, as classified by globally recognized Morgan Stanley Corporation International indices.

Over the years, Kenya's capital market has seen a significant amount of development and has taken on an increasingly visible role in the overall financial sector and financing of the economy. Much has been done to enhance market infrastructure and institutional arrangements, improve policy and regulatory framework, increase financial and investment literacy and expand capital markets products and services. This has resulted in substantial growth in the capital markets. Currently Kenya has the largest securities exchange in East and Central Africa; the Nairobi Securities Exchange (NSE), which has sixty-five out of the ninety-two listed companies in the East African region. The NSE is the fifth largest market in Africa (after South Africa, Nigeria, Egypt and Morocco) in terms of market capitalization at Kshs. 2.1 trillion. In the last two decades, the capital market has raised over Kshs. 2.4 trillion through bonds and equities issuances.

The growth experienced has been stimulated and complemented by a number of reform initiatives including: the implementation of Risk Based Supervision (RBS); modernization of market infrastructure with an Automated Trading and Settlement System (Equities since 2006 and Debt since 2009) and a robust Central Securities Depository; immobilization and subsequent dematerialization of listed securities; introduction of legal and regulatory frameworks in line with IOSCO principles and international best practices; introduction of a listing platform for Small and Medium Enterprises (SME) and Venture Companies through the Growth and Enterprise Market Segment (GEMS); introduction of Real Estate Investment Trust (REITs) and the Demutualization of the Nairobi Securities Exchange (NSE).

In spite of the foregoing initiatives and achievements, the Kenyan Capital Market still faces a number of challenges that must be addressed if it has to realize its full potential as identified in the Master Plan. These challenges include; inconsistent usage of the capital markets by domestic and regional entities for capital mobilization; weaknesses in the conduct of business by intermediaries which have contributed to retail investor apathy and constraints on international investment flows thereby affecting liquidity in the market; low financial and investment literacy and savings levels; limited innovation in the market; inadequate supply of appropriate products and insufficiently responsive structures to satisfy potential demand in the market; inadequate expertise for the structuring of complex capital market products; and concerns over the adequacy and competitiveness of key systemic infrastructure

Therefore three key pillars anchor the Master Plan, from which nine building blocks have been identified to form the basis for the Master Plan's main strategic initiatives and specific actions. The first three building blocks together form a pillar that focuses on the role of capital markets in supporting developmental and economic transformation in the country. This support is grounded in enhancing the knowledge of domestic users of capital markets, leveraging existing strengths and developing new specialist areas of expertise. The second group of the three building blocks constitutes another pillar that focuses on developing a solid core for the market; through promoting depth and liquidity in the market, creating international standard market infrastructure, and building capacity among market participants. The final three building blocks form the foundational pillar that focus on strengthening the regulatory and legal environment that supports the capital markets, including enhancing the capacity of the regulator and on creating an open and competitive environment that enables innovation to flourish in the market. It is envisioned that implementation of a detailed list of 107 strategic initiatives and specific actions identified within the nine building blocks will ensure that the benefits of capital markets will contribute to the desired domestic economic transformation.

On behalf of the Board and Management of the Authority, we wish to recognize the members of the Capital Markets Steering Committee who worked together tirelessly, selflessly and professionally in developing this Master Plan and the wider stakeholders who participated in the extensive consultations, which ensured that this remained an industry driven plan. The CMMSC members are:

Mr. Paul Kavuma	CEO, Catalyst Principal Partners (Chairman);
Mr. Amish Gupta	an Associate Director at Standard Investment Bank, representing Kenya Association of Stockbrokers and Investment Banks (KASIB);
Mr. Victor Nkiiri	General Manager, Securities at Fidelity Bank, representing Kenya Bankers Association (KBA);
Mr. James Muratha	Regional Managing Director, Stanbic Investment Management Services, representing the Fund Managers Association (FMA);
Ms. Fahima Zein	Head of Portfolio Management and Research, Genesis Kenya, representing the Fund Managers Association (FMA);
Ms. Anne Aliker	Head of Investment Banking (East Africa) for the Standard Bank Group;
Mr. Donald Ouma	Head of Market and Product Development, representing the Nairobi Securities Exchange (NSE);
Dr. Freshia Waweru-Mugo	Senior Lecturer, School of Management and Commerce, Strathmore University;
Mr. Gerald Nyaoma	Director, Financial Markets Department, Central Bank of Kenya;
Mr. Lazarus Keizi	Deputy Chief Economist in the Economic Affairs Department at the National Treasury;
Mr. Mutuma Marangu	Director, Green Resources AS;
Ms. Rose Mambo	Chief Executive Officer (CEO), Central Depository and Settlement Corporation (CDSC);
Professor Gituro Wainaina	Acting Director General of the Vision 2030 Delivery Secretariat, and a consulting economist, educator;
Ms. Wanjiku Mugane	MBS, an entrepreneur and renowned investment banker;
Mr. Ahmed Bashir	Founder and Managing Director of Takaful Insurance of Africa Ltd (TIA);
Mr. John Mwaka	Ag. CEO, SASRA; and
Mr. Paul Muthaura	Chief Executive, Capital Markets Authority.

The Authority would also like to acknowledge the invaluable input, support and guidance of the consultancy team who supported the work of the Master Plan Steering Committee who were drawn from Bourse Consult and Genesis Analytics: Stuart Turner, Mauro Mela, David Green, Hugh Simpson and Richard Ketley.

We look forward to the celebration of the full implementation of this Master Plan, which sets a bold aspiration of positioning Kenya as the Heart of African Capital Markets, which will have profound positive implications for the region and the continent, and a transformative impact from which future generations will derive significant social, economic and financial dividend. Let us move forward together with pride and fortitude in the execution of this ambitious Master Plan.

In line with our commitment to ensure transparent monitoring and evaluation of the implementation process of the Master Plan, the publication of this Second Edition as at the end of April 2016 presents a clear assessment of the strides made and focuses on areas requiring further attention and resource allocation as we progress on our journey to establish Nairobi as the Heart of African capital markets.

Mr. James Ndegwa
Chairman,
Capital Markets Authority

Mr. Paul M. Muthaura
Chief Executive
Capital Markets Authority

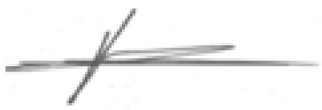
INTRODUCTORY REMARKS

In the development of the Master Plan, consideration was given to the uniqueness of Kenya's particular circumstance, environment and aspirations as detailed in Vision 2030 and as deemed necessary by the diversity of stakeholders in the capital markets. Critically, in tailoring solutions and in defining strategic imperatives, careful consideration was given to ensuring alignment with parallel, cross-cutting initiatives, including constitutional and regulatory reforms, as well as the development of Nairobi as an International Financial Centre. In establishing medium-term goals for Kenya's capital markets, the Capital Markets Master Plan Steering Committee took careful cognisance of the important role that the capital markets must play in the strengthening of an integrated financial system and in the development of the nation, while being conscious of wide-ranging regional implications and benefits.

The Master Plan addresses the particular characteristics of the Kenyan markets, recognizing the significant challenges and vast opportunities presented, with the scale of ambition being set for transformative and sustainable positive impact. Conceptualisation has been highly collaborative with constructive input from industry players, building upon the capital markets firm foundation. The adopted approach draws from global best practise, from which milestones are benchmarked, while prescribing a unique model that differs from traditional IFCs that are physically concentrated jurisdictional conclaves, carved out from the domestic economy within isolated legal, regulatory, and infrastructural frameworks. Instead, this Master Plan seeks to strengthen existing national frameworks and elevate the depth, reach, access, efficiency, liquidity, and sophistication of the capital markets to service the specific breadth of needs of the domestic economy as the priority, which will then be leveraged to offer innovative products and services across the region, for which Kenya has significant capability and potential. Uplifting of the capacity, governance, attractiveness and relevance of the capital markets, will stimulate dynamic demand and supply of public and private sector products and services, which will necessarily drive local, regional, and international capital flows.

This virtuous circle will require reinforcement of domestic skills, attracting talent from the Diaspora, and drawing of expertise from around the globe. Meanwhile the confidence and exposure of domestic retail and institutional investors will need to be enhanced through continuous educational programmes and capacity building, and the capabilities of market players and intermediaries will need to be constantly strengthened and monitored. Much needs to be done to create the conducive institutional environment to meet the ambitious expectations captured in the Master Plan, for which active support and collaboration will be required from all stakeholders.

On behalf of the Capital Markets Master Plan Steering Committee, I wish to sincerely thank and recognize the Board of Directors of the Capital Markets Authority for its firm guidance and its unwavering confidence. I also express heartfelt gratitude to the Steering Committee members for their commitment and dedication to this important process, and to the Management of the Capital Markets Authority for their professionalism and tireless devotion to the delivery of a world-class and inspirational product that we are assured will stand the test of time.



Mr. Paul Kavuma
Chairman, Capital Markets Master Plan Steering Committee

ACRONYMS AND ABBREVIATIONS

ADR	American Depositary Receipt
AIFMD	Alternative Investment Fund Managers Directive
AML	Anti-Money Laundering
BMA	Bond Market Association
CBK	Central Bank of Kenya
CCP	Central Counter Party
CDSC	Central Depository and Settlement Corporation Limited
CFT	Combating the Financing of Terrorism
CIS	Collective Investment Scheme
CMA	Capital Market Authority
COFEK	Consumer Federation of Kenya
CPSS	Committee on Payment and Settlement Systems
CSD	Central Securities Depository
DMA	Direct Market Access
DR	Depositary Receipt
DVP	Delivery Versus Payment
EAC	East African Community
ETF	Exchange-Traded Fund
EASRA	East Africa Securities Regulatory Authorities
ESAAMLG	Eastern and Southern Africa 'Anti-Money' Laundering Group
EU	European Union
FATF	Financial Action Task Force
FCB	First Community Bank
FRC	Financial Reporting Centre
GEMS	Growth Enterprise Market Segment
GFCI	Global Financial Centres Index
GoK	Government of Kenya
ICPAK	Institute of Certified Public Accountants of Kenya
ICPSK	Institute of Certified Public Secretaries of Kenya
ICSD	International Central Securities Depository
IFC	International Financial Centre
IFCI	Islamic Finance Country Index
IFIAR	International Forum of Independent Audit Regulators
IFRS	International Financial Reporting Standards
IFSB	Islamic Finance Standards Board
IMF	International Monetary Fund
INFE	International Network on Financial Education
IOSCO	International Organisation of Securities Commissions
IPO	Initial Public Offering
IRA	Insurance Regulatory Authority
ISA	International Standards on Auditing

ISC	Implementation Steering Committee
KASIB	Kenya Association of Stockbrokers and Investment Banks
KDR	Kenya Depositary Receipt
KRA	Kenya Revenue Authority
LSE	London Stock Exchange
MOU	Memorandum of Understanding
MSCI	Morgan Stanley Capital International
MTP	Medium Term Plan
NIFC	Nairobi International Financial Centre
NSE	Nairobi Securities Exchange
NSSF	National -Social Security Fund
OECD	Organisation for Economic Co-Operation and Development
OTC	Over-the-Counter
RBA	Retirement Benefits Authority
REIT	Real Estate Investment Trust
SASRA	SACCO Societies Regulatory Authority
SACCO	Savings and Credit Co-operative
SEC	Securities and Exchange Commission
SIDC	Securities Industry Development Corporation
SITI	Securities Industry Training Institute
SLA	Service Level Agreement
SLB	Securities Lending and Borrowing
STP	Straight-Through-Processing
SRO	Self-Regulatory Organisation
WRS	Warehouse Receipt System

EXECUTIVE SUMMARY

The Government of Kenya (GoK) is currently implementing a long-term strategy to transform Kenya into a middle-income, rapidly industrializing country by 2030, offering all its citizens a high quality of life. To achieve this aspiration, we need sustained economic growth at an annual rate of 10 percent over the next two decades.

Critical to achieving this high-level growth is availability of capital to fund the range of projects that form part of Vision 2030. The financial sector must therefore drive a significant increase in investment in Kenya by mobilising both domestic and international resources. Under the second medium term plan (MTP II); two key flagship projects for the financial services sector have been included namely: (i) the establishment of the Nairobi International Financial Centre (NIFC), and (ii) the development and implementation of a Capital Market Master Plan. These projects are mutually reinforcing and each needs to be addressed to ensure a vibrant sector that effectively finances the country's investment needs for sustainable development.

Status of Kenya's Capital Market

The Kenya Financial Stability Report (2012) and the Capital Markets Assessment undertaken in 2013 identified areas that need to be addressed for the country's capital market to realize its full potential. In both reports it was observed that there is a limited level of public awareness of capital markets in the country, which consequently led to a very low uptake of its products by the retail sector, as well as inconsistent usage of the capital markets by domestic and regional entities for capital mobilization.

While there is a growing number of institutions and funds considering Kenya as their next investment destination, there is insufficient supply of appropriate products and responsive structures to satisfy potential demand, both in the primary and secondary markets. The most pressing issue in the primary market for equities is inadequate supply, while from the demand side there are constraints on foreign room level in certain issues (especially where there are large non-traded blocks held by foreign strategic investors) caused by the foreign ownership limits and inadequacies in post-trade infrastructure that pose a greater problem in the future as the market develops.

In the fixed income markets, the most pressing issues relate to: the difficulty in raising infrastructure finance as a result of regulatory and institutional obstacles; shortage of well-prepared projects; as well as the lack of capital and expertise for risky, early-stage project development. Addressing these issues is particularly important, as the fixed income market will play a central role in funding the development of centres of excellence in infrastructure, real estate, oil and gas, metals and mining in Kenya.

Kenya has a thriving agricultural sector but commodity markets are undeveloped. There are sector specific organised markets for agricultural produce but most produce sold by farmers does not benefit from an efficient price discovery mechanism. A well regulated spot and derivatives market is therefore critical in realizing the full potential of the agricultural sector, necessary to accelerate the growth of a more value adding agro-based industry in Kenya.

The assessment also confirmed that legislation covering the capital market is widely regarded by the market as outdated and confusing. Instead of major reform of the legislation, Acts have been amended piecemeal to address certain issues. In addition, certain recent modifications appear to inadequately support some of the developments planned, such as commodity and financial futures markets.

A further challenge is the lack of sufficient communication across the industry. Many organizations are of the opinion that, the industry does not communicate with the capital markets regulator to stimulate more appropriate levels of market innovation and growth. There have been initiatives in the past to improve the channels of communication, but discussions have been inconsistent, with a greater focus on specific technical issues rather than on the larger structural and strategic challenges affecting multiple stakeholders.

In addition, education in the market was also found to be piecemeal and uncoordinated. All organizations surveyed as part of the market assessment agreed that financial and especially, investment literacy is at a low level in Kenya. It was confirmed that the various initiatives are undertaken from time to time on the part of individual companies, industry groupings, the Capital Market Authority (CMA) and other financial sector regulators are perceived as uncoordinated and piecemeal in the absence of a national strategy for consumer education and financial literacy.

Lastly, there are gaps in key systemic infrastructure, which if not expediently bridged, may undermine confidence in the Kenyan capital market. There are concerns about post-trade infrastructure and institutional capacity not being fully in line with international best practice. The practical concern in light of efforts to develop the country into an International Financial Centre is that the trading and settlement process is not as attractive to international investors in its present form as it should be. In addition, some very important initiatives, such as the creation of a single central securities depository (CSD) for Government paper, corporate debt and equities and full delivery-versus-payment (DVP) settlement in central bank money will not be able to take place unless a different approach is taken to solving the system constraints. It is however appreciated that there are significant reforms underway to address these challenges.

This Capital Market Master Plan seeks to chart the strategic positioning and future direction of the Kenyan capital market over the next 10 years. It seeks to provide market participants with strategic clarity on the vision and objectives of the capital market. It is also intended to ensure that the capital market is well positioned to play its part in supporting national growth needs and aspirations as envisioned under Vision 2030, while meeting relevant challenges such as a growing domestic marketplace, regionalization and increasing globalization of financial services.

Vision of the Capital Markets Master Plan: "The heart of African Capital Markets": The Capital Markets Master Plan envisions that the Kenyan capital markets will become sufficiently deep and dynamic to stimulate domestic development, while simultaneously providing a gateway to Middle Africa for regional and international capital flows. By 2023, it is expected that Kenya will have been transformed into the choice market for domestic, regional and international issuers and investors looking to invest in and realize their investments in Kenya, within East Africa and across Middle Africa. The market will be the centre of excellence for the real sectors of the economy in which Kenya already has significant capacity and potential including: agriculture, infrastructure (including real estate), and technology, while also leveraging the strength of Kenya's financial sector to develop innovative products and services, including derivatives, asset management and Islamic finance.

The country will have dynamic and liquid markets based on world class financial market infrastructure and subjected to strong and independent supervision. The capital markets will be supported by a legal and governance framework conducted in an open, competitive market place that inspires confidence.

Further, the capital markets will be fully integrated with the rest of the financial system, which will be the prime supplier of long term finance. Kenya will develop domestic talent and attract and retain it from the Kenyan diaspora, expatriates, and across the region. Its domestic retail and institutional users will be educated as to the benefits and risks of the capital markets in order to expand capacity, build up liquidity, and create an enabling environment for public and private sector entities to access public markets.

During the period of the Master Plan, the plan projects that for the Kenyan capital markets to qualify for rating by the Morgan Stanley Capital International (MSCI) Index as an emerging market. It is projected that the ratio of equity market capitalization to GDP will rise to 70 percent by 2030 while equity market capitalization will grow to USD 84 billion. The ratio of corporate bond market capitalization to GDP will rise to 40 percent from the current 2 percent while the percent of county financing through capital markets will increase to 30 percent. The percentage of infrastructure investment financed through capital markets will increase from the current 18 percent to 80 percent.

The Master Plan is anchored upon three key pillars namely:

- Support for Development and Economic transformation;
- The Infrastructure of the Markets; and
- The Legal and Regulatory Environment.

The above three pillars form the foundation of the transformation, from which nine core building blocks are derived as strategic imperatives of the Plan, with specific initiatives and action steps identified to ensure achievement of the envisaged outcomes. The five-fold rationale for developing a Capital Market Master Plan is to:

- Build on recent market reforms to address regulatory and institutional constraints to strengthen market infrastructure, intermediation, oversight and governance standards;
- Stimulate innovation to broaden product and service offerings, deepen market participation and liquidity, and drive transformative economic development;
- Streamline and augment funding for developmental projects under Vision 2030 as well as to provide alternative financing sources for devolution of services;
- Establish the Kenyan capital markets as a centre of excellence and gateway for regional and international capital flows; and
- Reinforce the development of Nairobi as an International Financial Centre.

Kenyan capital markets as a centre of excellence

One of the areas of focus will be regional and international activities and investment. During the plan period, Kenya will develop and build on centres of excellence in areas it has strengths. The country has well-established opportunities in agriculture, infrastructure, financial services and technology and real estate, and is developing strengths in sectors like oil and gas, metals and mining. It will aim to develop strengths in more sophisticated financial services, such as asset management, private equity/venture capital, private placements, and Islamic finance. These are important components of the Master Plan that will position Kenya as a centre of excellence for raising sophisticated funding. In particular, the country will build centres of excellence in the following areas:

- Commodities derivatives in agriculture, energy and minerals/metals;
- Construction and real estate development;
- Technology services and financial inclusion;
- Infrastructure finance; and
- Financial services that include, Islamic finance, asset management, and financial derivatives.

Pillar One: Support Developmental and Economic Transformation

The first pillar of the Master Plan focuses on the role of capital markets in supporting developmental and economic transformation in the country. The pillar moves progressively from its role in the domestic economy to its role in the regional and African context and then to the role in developing Kenya's place among international financial centres. The pillar has three building blocks namely; Domestic market accessibility and prosperity; Gateway for regional and international capital flows; and alignment with Nairobi International Financial Centre (NIFC).

The plan appreciates that well-developed and properly functioning financial markets have an important role to play in achieving Kenya's target of transforming itself into a newly industrialized, middle-income country, by generating wealth as well as safeguarding it. The objective of this pillar is to ensure that the benefits of capital markets contribute to the desired domestic economic transformation on three levels: domestically; within East Africa and Africa specifically; and internationally. The country will further endeavor to be positioned at the heart of financial services in Africa, within the East African Community (EAC) and beyond. To this end, two areas of work are identified under the Master Plan. This will be achieved through leveraging on the integrated EAC market and enabling the Kenyan capital markets finance the country's key strengths. A critical element in enabling Kenya to be a key international centre will be to expedient harmonization of financial market regulations in the EAC, wherever possible, in the form of identical regulation.

Finally, the pillar will aim at enabling Nairobi to join the ranks of other international financial centres. A strong domestic and regional financial centre will make Nairobi more attractive as a location for international financial firms, while access to international financial markets will enhance their ability to achieve domestic objectives.

A tangible objective of this programme will be to achieve MSCI Emerging Market status for Kenya by 2020 and for Nairobi to enter the Global Financial Centre Index (GFCI) ranking of financial centres published by the Z/Yen Group and gradually to move up the same table. The target for the latter is to achieve a ranking of 70 by 2020 (roughly equivalent to the current position of Mauritius) and 50 by 2023 (which would be higher than the current ranking of Johannesburg and Rio de Janeiro). Both ranking systems are based largely on qualitative assessments by people and organisations, and apply the key capital market assessment criteria.

For Kenya to become an International Financial Centre multiple conditions need to be met including: an attractive business environment with access to experienced and qualified staff; a legal and regulatory regime that gives confidence; a critical mass of financial and professional services firms present and a network of connections with other financial centres. To a large extent, this is the culmination of other building blocks in the Master Plan, which come together to create the conditions for Nairobi to develop its international status. However, there remain some further actions to complete the process, which will require close cooperation between CMA and NIFC to hasten the development of the centre. The proposed Steering Committee on the NIFC can play an important role as a focal point in coordinating the policy developments necessary to achieve this objective.

Pillar Two: The infrastructure of the Markets

Kenya's financial markets are at different stages of development. Whereas Kenya has a well-developed and liquid Government bond market, the equities market on the other hand is characterized by relatively few listings, which are skewed towards financial companies, and low liquidity. Commodity markets exist only in the rather undeveloped forms of the Mombasa Tea Auction and the Nairobi Coffee Exchange. Pillar two has three building blocks namely, Deeper, more liquid domestic markets; International standard market infrastructure; and Institutional and capacity building initiatives.

Nevertheless there is considerable international investor interest in Kenya, which has not been fully exploited due to shortage of assets, lack of liquidity and inadequate infrastructure. Therefore, Kenya needs to improve the actual operation and infrastructure (both physical and human resources) of its capital markets in order to:

- Increase product supply and trading activity of existing markets;
- Add new markets and products; and
- Bring infrastructure up to international best practice standards to improve the security and risk management of the markets and to attract more international players.

To develop Kenya's financial markets, the Master Plan has set ambitious targets for improvements in listings, liquidity and performance of new product areas. The three building blocks below contribute to achieving the objectives of growing and deepening existing markets and developing new markets. These targets are designed to reflect developments that can be shaped by the Capital Market Master Plan rather than by external factors. Specifically, the targets are:

- The ratio of equity market capitalisation to GDP to rise from 50% now to 70% by end-2023, putting Kenya slightly above the world average;
- The number of GEMS listings, which reflect the supply of future main board listed companies, to increase by 3-4 annually;
- The ratio of corporate bonds outstanding to GDP to reach 40% by end-2023; and
- The value of outstanding exchange-traded derivative contracts to reach USD 200 billion by end-2023 - an ambitious target, given that the market has not yet been launched, but is achievable by comparison with other markets.

The Pillar will ensure the accelerated development of the securities markets through sophistication of the securities trading arrangements as well as spot and derivatives markets. The areas key to the development of the country market infrastructure relates to the development of the depository and clearing infrastructure to ensure efficient and reliable post trade process meeting international standards. The post trade infrastructure is critical in attracting international investments.

With regards to the derivatives market (whether traded on an exchange or in the OTC market) a robust infrastructure to provide a secure and efficient platform to manage risks and ensure efficiency is a major prerequisite. The requirements are different from those of the cash securities markets. Whereas in securities markets the time between trading and settlement, when the two parties, are exposed to each other is typically measured in days, in derivative markets it may be measured in weeks or months. This therefore requires a robust and secure Central Counter Party (CCP) clearing house to offer novation services meeting international standards.

The final area of focus for the pillar is human capacity. The role of human capital is pivotal to the development of a world-class capital market in Kenya. Access to a deep pool of highly skilled and trained a human resource will enhance the capacity of the entire financial sector and is critical for the development of specific sub-sectors like the capital market.

This pool of finance professionals will also support the growth of an International Financial Centre based in Nairobi through providing ample supply of skilled capacity for the centre. Creating a deep pool of finance professionals in the country will have a virtuous effect in attracting companies to the International Financial Centre. Specifically, these companies will benefit from access to qualified and knowledgeable professionals in finance, law, accounting, audit and a range of other specialist skills necessary to establishing local and regional operations in the financial centre.

Lastly from a developmental perspective, as Kenya becomes a gateway for financial services into Middle Africa and as foreign investment into the country increases, there will be a growing need to ensure finance professionals are sufficiently competent and qualified so that the Kenyan capital market can compete effectively in an increasingly open environment.

Pillar Three: Legal and Regulatory Environment

For the capital markets to flourish as the Master Plan articulates, the regulatory and legal environments need to be strengthened and streamlined to accommodate the requirements placed upon them and the regulator itself needs to be fully equipped to perform its role. The arrangements for corporate governance and financial reporting need to be upgraded and rendered fully effective, and the environment needs to be innovative, open and competitive. This last pillar has the following building blocks; sound and responsive legal framework that inspire confidence; Improved corporate governance and financial reporting; and Innovative open and competitive environment.

As part of the consideration of the best form of the regulatory architecture, consideration should also be given to ensuring that the regulatory objectives are best suited to their purpose. This applies whether the regulatory framework is integrated or not. One of the issues which arises internationally is the extent to which promotional or developmental objectives for a market place should be directly reflected in the objectives of the regulator, in whichever sector, rather than be assigned to other agencies. Although a number of regulators internationally do have promotional or developmental as well as regulatory objectives, the international trend is against them. The current international approach rather aims at putting in place other approaches to trying to ensure a financial centre's competitiveness and capacity for innovation is not unwarrantedly impeded by regulation. Under this model, the promotional and developmental role is assigned to a separate agency without regulatory responsibilities. This also makes it clear that responsibility for innovation and development of products and markets must lie with market participants themselves. They are the ones who can best identify viable opportunities for new products, if need be, in collaboration with other market participants.

The reason for the debate about regulatory mandates at the international level is that the combination of developmental and regulatory objectives within a regulator's mandate may lead to conflicts and tensions which may undermine the effectiveness of rulemaking and fairness in individual regulatory decisions. An improper bias may be introduced in favour of particular providers of financial services against either users or other providers. And there has been adverse experience where developmental objectives have distracted the regulator from adequately protecting the consumer or market user.

The emerging international consensus is that a better way of achieving the intention of such a development or promotional objective is if lawmaking/rulemaking/decision remains focused, in the case of a securities regulator, on the core objectives of protecting investors, maintaining orderly markets and supporting financial stability but under the constraints of "better regulation" principles. This will of itself help to improve the attractiveness of markets and their international competitiveness as well as reducing the risk of conflict of objectives. Such principles would normally be included in the legislative and rule-making process.

Such principles might be:

- Identify the mischief. The intention is that without prior understanding of what the rule(s) were supposed to address, it is not possible to know what character of rule to adopt or how much detail the rule needs to provide.
- Identify the market. Detailed rules at the national (or EAC) level should focus on requirements which will open those markets to contestation, assuming that competition policy is not a better tool. Otherwise, changing a market structure without good reason will be a costly exercise without necessarily corresponding benefits for the customers in those markets.
- Choose the right policy tool. At one level this involves deciding which tool is best to address the mischief; whether an issue is best addressed by competition policy, by supervisory activity or by enforcement. At another, it means deciding whether there should be ever greater detail in rules about what precisely firms should do or whether the rule might incorporate a set of considerations or principles against which a firm's decision would be assessed by supervisors and overruled if determined to be excessively risky.
- Identify the right kind of rule. Is the best approach one addressed at content, process, outcome or behaviour? Content relates to a specific requirement which must be met, like a capital ratio. Process sets out a set of actions which must be followed over time. Outcome relates to what is achieved, perhaps at a certain level of generality. Behaviour specifies or prohibits the way in which an act must be undertaken. There could also be tests relating to how the rule is to be used; is it to be enforced and if so is it suitable for this purpose; is it just a means to an end rather than the outcome itself; what are the risks of the rule generating unwanted changes in behaviour; and so on.
- No rule should be more detailed than necessary. This is in part to avoid unrealistic implementation challenge, partly to avoid diversion to rule evasion rather than true risk mitigation.
- Innovation in connection with regulated activities should not be impeded where it does not conflict with the regulator's primary responsibilities.

With regards to promoting innovation, one of the ways in which innovation can be supported, irrespective of the sector, is by formalisation of a "no-action" approach to proposals for new products or approaches. The Authority will put in place "no action" arrangements whereby the market can come to the CMA and ask for assurance that some action may proceed without the law specifically allowing it. The CMA can then advise the firm or market that in its view the proposed new product or approach can proceed without breach of law provided it remains strictly within certain specified parameters.

This is similar to an approach used in the USA by the Securities and Exchange Commission (SEC). An individual or entity who is not certain whether a particular product, service, or action would constitute a violation of the US federal securities law may request a "no-action" letter from the SEC staff. Most no-action letters describe the request, analyse the particular facts and circumstances involved, discuss applicable laws and rules, and, if the staff grants the request for no action, concludes that the SEC staff would not recommend that the Commission take enforcement action against the market intermediary based on the facts and representations described in the individual's or entity's request. The SEC staff sometimes responds in the form of an interpretive letter to request for clarification of certain rules and regulations. The no-action relief is limited to the specific facts and circumstances set forth in the request. In addition, the SEC staff reserves the right to change the positions reflected in prior "no-action" letters.

The authority will review legal framework to make it more "Principles-Based" regulation. Principle based is at times used as shorthand for introducing rules which are sufficiently flexible to accommodate a range of circumstances. This is to enable quicker adjustment to changes in the market than can be met if rules have to be formally amended to meet all changes in circumstances. However, if the markets are to remain reliably protected, it is best if a flexible drafting of rules, which carries risks of its own, goes hand in hand with the formalization of a "no-action" approach as described above. It also has to be possible, for legislation and/or rules to be implemented in a timely manner to be able to address emerging risks or to accommodate emerging market developments.

Finally, the pillar envisages measures and actions that will improve corporate governance and financial reporting. A sound financial market is critically dependent on sound corporate governance and reliable and transparent financial reporting. Without this, a market is unlikely to develop or attract foreign interest.

Failures in corporate governance or the issuance of misleading financial reports can cause enduring reputational damage to any capital market which can be difficult to reverse rapidly. A number of measures will be put in place to bolster the existing arrangements and bring them to international level.

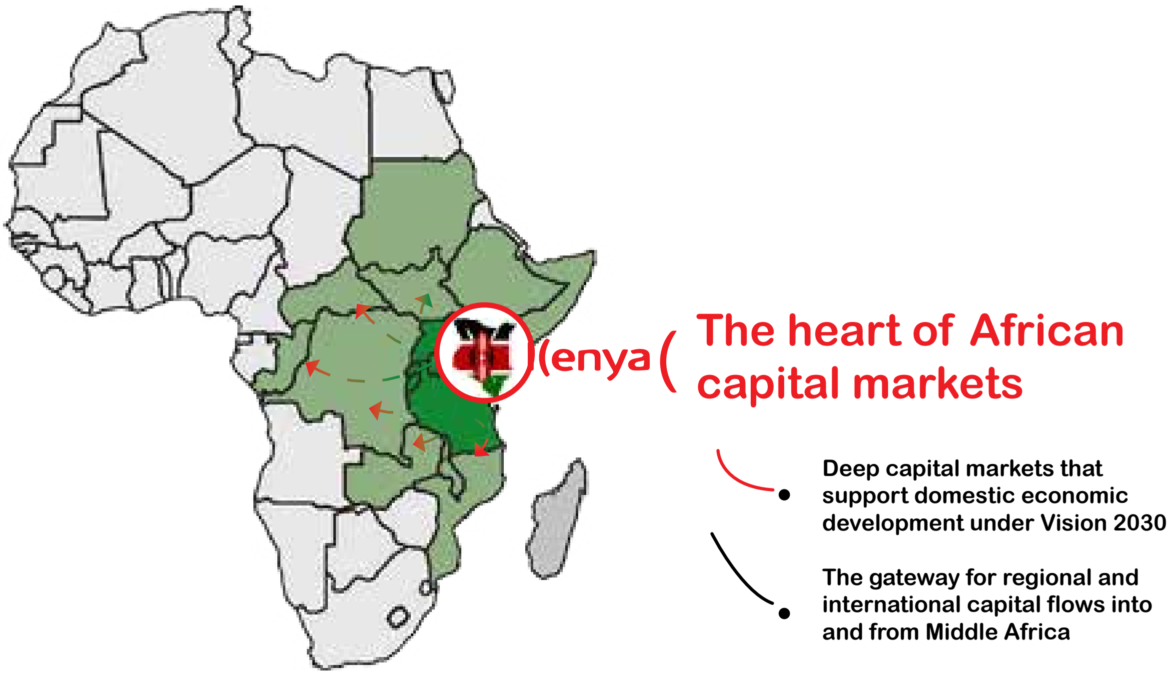
The Capital Market Master Plan (CMMP) seeks to provide market participants with strategic clarity as to the vision and objectives of the capital market. It is also intended to ensure that the capital market is well positioned to play its part in supporting national growth needs and aspirations as envisioned under Vision 2030, as well as meeting relevant challenges such as a growing domestic marketplace, regionalisation and increasing globalisation of financial services.

The CMMP has been prepared under the auspices of the Capital Market Authority by a Steering Committee representing a broad cross-section of market participants, financial sector regulators, industry associations, academia and other industry experts. The contribution of the Steering Committee has been to provide the direction for the Kenyan capital market over the next 10 years through a consultative process. This extensive process involving all capital market stakeholders has harnessed the creativity and the thought-leadership of the Kenyan capital market industry. This contribution has ensured that the industry is well positioned to support the implementation of the Capital Market Master Plan in the coming years and to support the positioning of Kenya as an international financial services hub.

THE VISION FOR KENYAN CAPITAL MARKETS

Kenya: The heart of African Capital Markets.

Kenya's capital markets will be deep and dynamic to stimulate domestic development while simultaneously providing a gateway to Middle Africa for regional and international capital flows.



By 2023, Kenya will be transformed into the choice market for domestic, regional and international issuers and investors looking to invest in and realize their investments in Kenya, within East Africa and across Middle Africa.

The capital markets will be the centre of excellence for real sectors of the economy in which Kenya already has significant capacity and potential, including agriculture, infrastructure (including real estate), and technology, while also leveraging the strength of Kenya's financial sector to develop innovative products and services, including derivatives, asset management and Islamic finance.

The country will have dynamic and liquid markets based on world-class financial market infrastructure, subject to strong and independent supervision. The capital markets will be supported by a legal and governance framework that inspires confidence and market activities will be conducted in an open, competitive market place.

The capital markets will be fully integrated with the rest of the financial system, in which they will be the prime supplier of long term finance. Kenya will develop domestic talent and attract and retain it from the Kenyan Diaspora, from expatriates and from across the region. Its domestic retail and institutional users will be educated as to the benefits and risks of the capital markets in order to expand capacity, build up liquidity, and create an enabling environment for public and private sector entities to access public markets.

Kenya will actively promote its attractiveness as an investment destination for financial services and as the preeminent capital markets gateway to East and Middle Africa, open to the world and fully interconnected with other international financial centres. Within the medium term, Kenya's ranking will be elevated from Frontier Market to Emerging Market status, as classified by globally recognized MSCI. This rating will unlock access to considerable additional capital flows and investment finance for the Kenyan market.

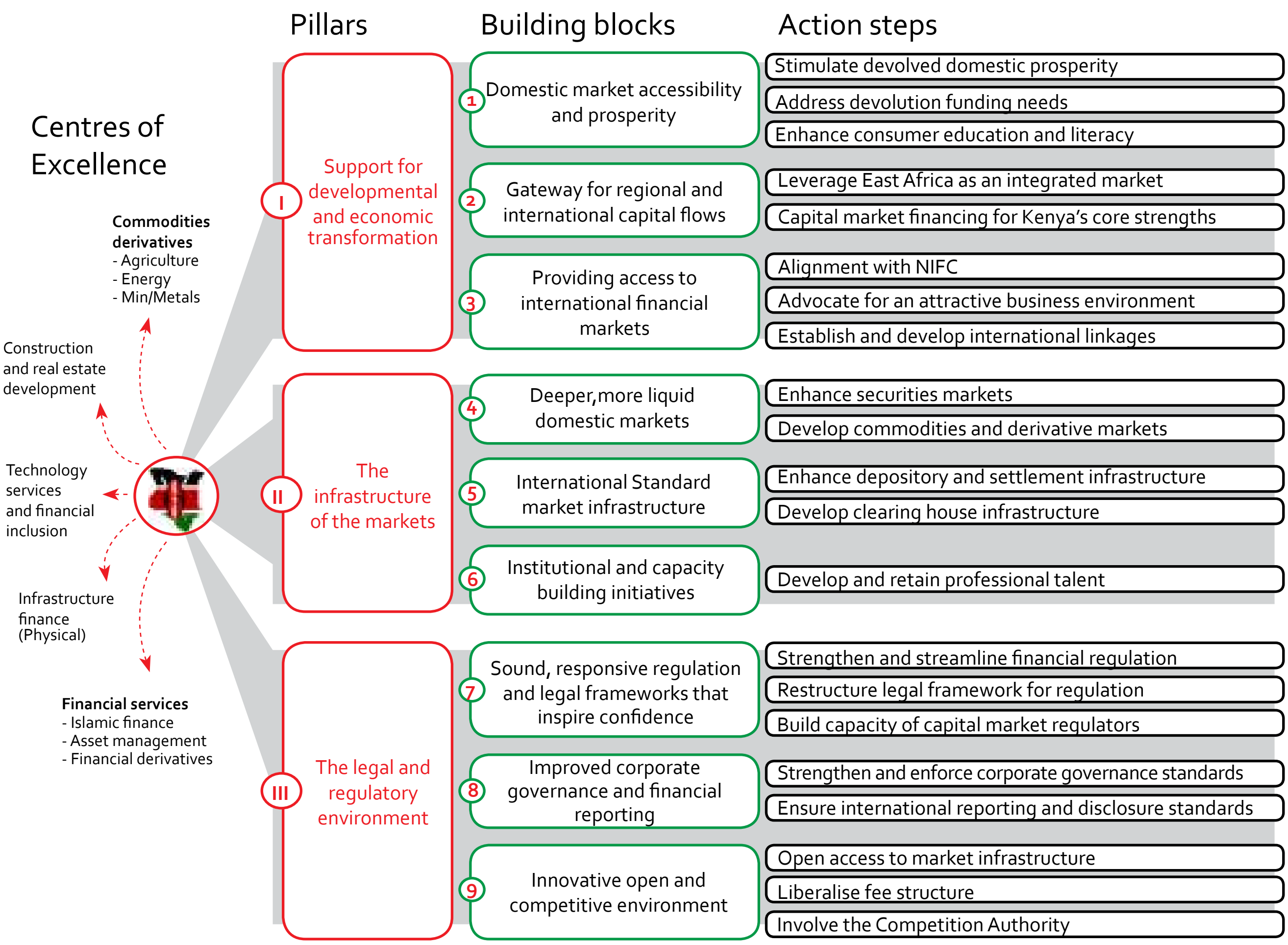
This transformation will see the capital markets benefit the continued strong growth of the Kenyan economy at both national and county level. It will support the achievement of Vision 2030 making it easier to attract finance for vital infrastructure projects, giving Kenyan businesses and entrepreneurs a wider range of options for longer term finance and for risk management, offering domestic and regional institutional investors greater breadth and diversity of investment products, giving Kenyan savers access to greater diversification in their investments, and creating employment opportunities in the market. There will also be benefits for the East African region as a whole in having easy access to a strong and diverse financial centre in Kenya.

The impact of this transformation will be continuously monitored and evaluated, guided by critical qualitative and quantitative measures on which performance will be benchmarked against the bold aspirations for the capital markets. Select quantitative indicators are captured in the table below, which reflect ambitious yet achievable targets.

Targets	Starting Point (Jan 2014)	Short Term (end 2016)	Medium Term (end 2020)	Long Term (end 2023)
MSCI Market Rating	Frontier	Emerging	Emerging	Emerging
Ratio of equity market capitalization to GDP Equity market capitalization implied by annual GDP growth of 10% from 2013	50% USD 25.02bn	53% USD 39.21bn	60% USD 67.60bn	70% USD 97.35bn
Number of GEMS listings	1	12	27	39
Ratio of corporate bond market capitalization to GDP Ratio of corporate bond market turnover to total bond market capitalization	2% 0.1%	4% 5%	15% 35%	40% 50%
Percent of county financing through capital markets	0	0	20%	30%
Cost and percentage of infrastructure investment financed through equity, bonds, private equity	USD 4.29 bn 18%	USD 5.51bn 60%	USD 10.87bn 60%	USD 12.41bn 80%
Exchange-traded financial derivatives: value of contracts outstanding	-	-	$ 50bn	$ 200bn
Assets under management in CIS by fund managers in Kenya	USD 0.42bn	USD 0.67bn	USD 1.90bn	USD 2.29bn
Target for Islamic finance (IFCI)	2.2	4	7	15
Ranking in GFCI	-	80	70	50

Note: Targets represent achievements as at end-of-period. Conversion at Ksh 100 to 1 USD

The Capital Markets Master Plan sets out the route to realize this aspiration and to ensure these critical success factors are met. The Master Plan is anchored on three key pillars that form the foundation of the transformation, from which nine core building blocks are derived as strategic imperatives of the Plan, with specific initiatives and action steps identified to ensure achievement of the envisaged outcomes:



A comprehensive and prioritized work plan will be developed on the basis of this Master Plan, with assignment of detailed responsibilities, deliverables and timelines to specific institutions for each initiative and action to which specific measurements and monitoring tools will be attached to facilitate achievement of expected results.

Overall coordinating, implementing and monitoring authority will be assumed by a Capital Market Master Plan Implementation Committee (CMMPIC) under the umbrella of the NIFC Steering Committee to be appointed by the Cabinet Secretary to the National Treasury, and chaired by the Capital Markets Authority. It is further recommended that an appropriate number of CMMPIC members be drawn from the CMMP Steering Committee for continuity, and that the constitution of the full CMMPIC continues to draw upon the expertise of industry stakeholders, as well as professional advisors, specialist resources and Working Groups as necessary. Full details are set out in the *Implementation Process and Roadmap* section below.

INTRODUCTION

The Government is currently implementing a long-term strategy to transform Kenya into a middle-income, rapidly industrialising country by 2030, offering all its citizens a high quality of life. To do so, the economy needs to sustain economic growth at an annual rate of 10 percent over the next 16 years.

Critical to achieving this high-level growth is the targeting of funding for the range of projects that form part of Vision 2030. This requires that the financial sector drives a significant increase in investment in Kenya by mobilising both domestic and international resources. The vision articulated for the financial services sector is to:

> *"Create a vibrant and globally competitive financial sector that will promote high level of savings to finance Kenya's overall investment needs."*

In order to achieve this vision, the first two of the projected five successive Medium Term Plans (MTPs) to implement the Vision 2030 have identified two key flagship projects for the financial services sector: (i) the establishment of the Nairobi International Financial Centre (NIFC), and (ii) the development and implementation of a Capital Market Master Plan. These projects are mutually reinforcing and each needs to be addressed to ensure a vibrant sector that effectively finances the country's investment needs for sustainable development.
As the key driver for long-term resource mobilisation, the capital market will play a central role in achieving the vision for the financial sector through:

- Intermediating long-term savings in the economy;
- Contributing to increasing the monetisation of the economy and promoting financial inclusion;
- Mobilising and allocating capital to fund the development of public and private sectors;
- Reducing dependency on the banking sector and facilitating access to long term capital;
- Offering mechanisms for risk management and mitigation;
- Providing platforms for the broadening of ownership of performing and strategic assets and community empowerment;
- Providing a framework for the sound governance of corporations;
- Contributing to financial sector economic activity and job creation; and
- Promoting overall balance and stability in the financial system.

The Starting Point

Kenya is fortunate that its "vibrant and rapidly expanding financial sector constitutes a major asset to support economic growth and reduce the vulnerabilities of low-income portions of the population".[1] International investor interest in Kenyan markets is high and the country is a world leader in fields such as mobile money transfers.

In spite of these strengths, the Financial Stability Report (2012) noted that public awareness of capital markets is limited and this has led to a very low uptake of its products by the retail sector as well as inconsistent usage of the capital markets by domestic and regional entities for capital mobilisation. Weaknesses in the conduct of business by intermediaries have contributed to retail investor apathy and constraints on international investment flows which may be affecting liquidity in the market. The low level of liquidity is also accentuated by low financial literacy and saving levels in general. The Financial Stability Report lastly noted that innovation in the market is limited. This is in part due to delays in enacting securities industries laws. It is also in part due to a perception among market players that the current regulatory framework is too stringent and insufficiently responsive resulting in an inconsistent and inadequate allocation of resources by market players to innovation and product development within the existing legal framework.

In preparation for the development of the Capital Market Master Plan a market assessment was carried out, which confirmed these challenges as well as identifying others that need to be addressed.

1 IMF (2013) Fifth Review Under the Three-Year Arrangement Under the Extended Credit Facility

There appears to be a growing number of institutions and funds that want to invest in Kenya but there is insufficient supply of appropriate products and responsive structures to satisfy potential demand. The most pressing issue in the primary market for equities is inadequate supply. In the context of secondary market liquidity, constraints on foreign room level in certain issues (especially where there are large non-traded blocks held by foreign strategic investors) caused by foreign ownership limits and inadequacies in post-trade infrastructure may pose a greater problem in the future as the market develops.

In the fixed income markets, the most pressing issue relates to the difficulty in raising infrastructure finance as a result of regulatory and institutional obstacles, shortage of well-prepared projects, as well as the lack of capital and expertise for risky, early-stage project development (described in more detail in the next section). Addressing these issues is particularly important, as the fixed income market will play a central role in funding the development of centres of excellence in infrastructure, real estate, oil and gas, metals and mining, for example.

Kenya has a thriving agricultural sector but commodity markets are under-developed. There are sector specific established organised markets for agricultural produce but most produce sold by farmers does not benefit from an efficient price discovery mechanism.

The assessment also confirmed that legislation applicable to covering the capital markets is widely regarded as outdated and confusing. Instead of major reform of the legislation, Acts have been amended piecemeal to solve certain issues. In addition, certain recent modifications appear to fail to adequately support some of the developments planned, such as commodity, derivatives, and financial futures markets.

A further issue that has been noted is the lack of sufficient communication across the industry. Many organisations surveyed as part of the market assessment pointed to the fact that, in their opinion, the industry does not communicate enough with the capital markets regulator to stimulate more appropriate levels of market innovation and growth. There have been initiatives in the past to improve the channels of communication but whatever discussion has taken place has been inconsistent, with a greater focus on specific technical issues rather than on the larger structural and strategic challenges affecting multiple stakeholders.

Education in the market was also found to be piecemeal and uncoordinated. All organisations surveyed as part of the market assessment agreed that financial and, especially, investment literacy is at a low level in Kenya. It was confirmed that various initiatives are undertaken from time to time on the part of individual companies, industry groupings, the Capital Market Authority (CMA) and other financial sector regulators. However, these are seen as uncoordinated and piecemeal in the absence of a national strategy for consumer education and financial literacy.

Lastly, confidence in key systemic infrastructure was noted as being very low. There are many concerns about post-trade infrastructure in particular, ranging from lack of trust in the competence of relevant organisations to specific issues about the systems not being able to support the market. The practical concern in light of efforts to develop the country into an international financial centre is that the trading and settlement process is not designed to support international investors. In addition, some very important initiatives, such as the creation of a single central securities depository (CSD) for Government paper, corporate debt and equities and full delivery-versus-payment (DVP) settlement in central bank money will not be able to take place unless a different approach is taken to solving the system constraints.

Recognising the critical role of the capital market in supporting national economic growth, CMA, in partnership with key stakeholders in the Kenyan capital markets, has developed this Capital Market Master Plan to provide the direction for the Kenyan capital market over the next 10 years.

The objective of involving all capital market participants in this process is to harness creativity and innovation in the industry and to enhance commitment to collective understanding that is incorporated into an industry plan that informs prioritisation and resource allocation at both the micro and macro levels in the sector.

The Capital Market Master Plan is intended to ensure that the capital market is well positioned to support accelerated national economic growth, to bring reality to the vision for the financial sector, to leverage future opportunities from regional integration and to ensure the competitiveness of the Kenyan markets in an increasingly globalised environment as Kenya endeavours to be a hub for international financial services and the heart of capital markets financing on the African continent.

Rationale for the Master Plan

The rationale for developing a Capital Market Master Plan at this time is fivefold, to:

- Build on recent market reforms to address regulatory and institutional constraints to strengthen market infrastructure, intermediation, oversight and governance standards;
- Stimulate innovation to broaden product and service offerings, deepen market participation and liquidity, and drive transformative economic development;
- Streamline and augment funding for developmental projects under Vision 2030, and to provide alternative financing sources for devolution of services;
- Establish the Kenyan capital markets as a centre of excellence and as a gateway for regional and international capital flows; and
- Reinforce the development of Nairobi as an International Financial Centre.

Each of these five areas is discussed in more detail below:

Build on recent market reforms

In recent years, CMA has been undertaking several reforms aimed at enhancing the capital markets' contribution to the Kenyan economy. These include automation of the bond market, introduction of infrastructure and savings bonds, introduction of securitisation and real estate investment products, review of the legal framework governing securities markets and demutualisation of the Nairobi Securities Exchange (NSE). These programs have been driven through the regulator's strategic planning process.

In parallel, the industry has also been engaged in other important programs to develop the market. These programs include, for example, the introduction of the Growth Enterprise Market Segment (GEMS) at the NSE, the introduction of Sharia-compliant capital market products and services, and the development of a hybrid bond market.

The purpose of the Capital Market Master Plan is to integrate these and other programs that are driven by the industry or by the regulator into a single, cohesive, and shared work program for the capital markets. In doing so, all developmental initiatives in the market are targeted to be aligned toward achieving a single vision for the growth and development of the Kenyan capital market.

Stimulate innovation

Kenya is already well regarded for having successfully established the first scalable mobile payment platform in the world. In large part the outcome of this innovation has been to triple financial inclusion in the country over a period of seven years to a point where two thirds of the population use some form of formal financial service; be it in payments, credit or insurance. The capital markets are an ideal vehicle to support the country's aptitude for innovation in technology services, particularly for nascent technology firms that need access to investment capital. In addition, the widespread uptake of such platforms provides a unique channel for greater retail participation in capital markets (for example through collective investment schemes). Efforts are already underway, for example, to provide investors with direct access to treasury bonds through mobile payment platforms.

Streamline and augment funding for projects under Vision 2030

While the capital market has played an important role in mobilising funds and facilitating economic development in the past, the development financing requirements of the economy as the country seeks to attain middle-income status indicate that even greater expectations will be placed on the capital markets in the coming years in order to achieve national aspirations.

These aspirations and development objectives, as spelled out in Vision 2030, indicate the need for appropriate capital market structures and mechanisms to support the economic, financial, social and commercial goals of the country. The Capital Market Master Plan is therefore designed to develop key features of the capital market such that long term domestic and international funding can be provided to support Vision 2030 projects. Improvements to financial market infrastructure, depth and liquidity of products in the market, as well as to the enabling legal and regulatory environment as targeted in the Master Plan are thus integral to the achievement of Vision 2030 targets.

Establish the Kenyan capital markets as a centre of excellence

To attract regional and international activity and investment, Kenya will develop and build on centres of excellence. The country already has well-established strengths in agriculture, infrastructure, financial services and technology and real estate, and is developing strengths in sectors like oil and gas, metals and mining. It aims to develop strengths in more sophisticated financial services, such as asset management, private equity/venture capital, private placements and Islamic finance. These are important components of the Master Plan that will position Kenya as a centre of excellence for raising sophisticated funding.

Support the establishment of Nairobi as an International Financial Centre

A key flagship project under Vision 2030 is the establishment of Nairobi as an International Financial Centre (NIFC). This centre will attract global financial services institutions through offering attractive legal, regulatory and institutional frameworks, world-class infrastructure, and favourable investment and tax incentives.

The CMMP is intended to support the development of Nairobi as an International Financial Centre in a number of important ways. Improvements to legislation and regulation governing capital markets through the Master Plan, for example, are likely to have an important impact in creating an attractive institutional environment for users of the Kenyan market place and the International Financial Centre in particular, while improvements to financial market infrastructure through the Master Plan could similarly contribute toward creating an attractive proposition for would-be international entrants.

Since financial service companies located in the NIFC are likely to draw upon domestic skills, efforts to build capacity in Kenya's financial markets as part of the Master Plan will create a deeper, more knowledgeable pool of employment for the benefit of the NIFC.

Targets contained in the Master Plan to achieve MSCI Emerging Market status and to improve Anti-Money Laundering (AML) and Combating the Financing of Terrorism (CFT) guidelines will also assist in attracting foreign firms to the NIFC by ensuring compliance to internationally accepted standards.

Lastly, as the Master Plan has been prepared with the benefit of analysis of international best practice, the study of other capital market master plans and efforts to establish international financial centres in other emerging centres, this Master Plan is consequently intended to be instrumental in informing efforts towards the establishment of Nairobi as an International Financial Centre.

FROM VISION TO PLAN

The Vision for the Kenyan capital markets was set out at the start of this document. The purpose of this Master Plan is to develop a programme of specific, achievable and sequenced actions that will realise that Vision over a ten-year period.

In preparing this Master Plan, the plans of six comparable markets were reviewed. These markets have all implemented capital market master plans or are striving to develop international financial centres of their own. The conclusions drawn from this analysis are as follows:

i. There is no one single recipe for developing capital markets. Each country needs to tailor its plan to its circumstances. This Master Plan therefore has been built to address the specific requirements of Kenya, rather than attempting to follow any generic template for development.
ii. The broad phasing of development is to start by building the domestic market and gradually establishing links and opening up internationally. As a recent report published by the City of London noted, "As a financial centre grows in a developing economy, it initially serves a largely domestic group of participants. As a country's economy grows and businesses develop increasingly sophisticated financing requirements, foreign investors become interested in investing in the country, while domestic firms stretch the domestic capacity to provide the capital they need to expand and begin to seek external sources of finance". This Master Plan therefore focuses on developing the domestic market before expanding international links.
iii. Capital market master plans are broadly developmental, while plans to develop international financial centres often imply the creation of a centre of excellence/expertise in a particular service or product. This Master Plan is broadly developmental at the same time as trying to establish specific expertise/excellence and trying to support the NIFC.

Core Components to Achieve the Vision

Nine key building blocks have been identified to form the basis for the Master Plan's main strategic initiatives and specific actions. These nine building blocks are grouped into three pillars which anchor this Master Plan.

As illustrated below, the first three building blocks focus on the role of capital markets in supporting developmental and economic transformation in the country. This support is grounded in enhancing the knowledge of domestic users of capital markets, leveraging existing strengths and developing new specialist areas of expertise.

The second three building blocks focus on developing a solid core for the market; through promoting depth and liquidity in the market, creating international standard market infrastructure, and building capacity among market participants.

The final three building blocks focus on strengthening the regulatory and legal environment that supports the capital markets, including enhancing the capacity of the regulator and on creating an open and competitive environment that enables innovation to flourish in the market.

I	II	III
Support for developmental and economic transformation	**The infrastructure of the markets**	**The legal and regulatory environment**
1. Domestic market accessibility and prosperity	4. Deeper, more liquid domestic markets	7. Sound, responsive regulation
2. Gateway for regional and international capital flows	5. International standard market infrastructure	8. Legal frameworks that inspire confidence
3. Alignment with NIFC	6. Qualified and educated workforce	9. Innovative, open and competitive environment

The following sections constitute the core of the Master Plan and identify actions to be taken by different actors toward the fulfillment of the Vision. A full list of actions is provided in the last section of this document together with an overall plan for implementation, under the leadership of an Implementation Committee.

THE CAPITAL MARKET MASTER PLAN

The Capital Market Master Plan is articulated in the sections that follow.

I. SUPPORT DEVELOPMENTAL AND ECONOMIC TRANSFORMATION

The first three building blocks of the Master Plan focus on the role of capital markets in supporting developmental and economic transformation in the country. They move progressively from their role in the domestic economy to their role in the regional and African context to their role in developing Kenya's place among international financial centres.

1. DOMESTIC MARKET ACCESSIBILITY AND PROSPERITY

Well-developed and properly functioning financial markets have an important role to play in achieving Kenya's target of transforming itself into a newly industrialised, middle-income country, both by generating wealth and by safeguarding it. The objective of this first pillar of the Master Plan is to ensure that the benefits of capital markets contribute to the desired domestic economic transformation on three levels: domestically; within East Africa and Africa specifically; and internationally.

1.1. Stimulate Devolved Domestic Prosperity

The ultimate objective of the Master Plan is to benefit the Kenyan economy - by making it easier to attract finance for vital infrastructure projects, by giving Kenyan businesses a wider range of options for longer term finance and for risk management, by giving Kenyan savers access to greater diversification in their investments and by creating employment opportunities. Over time, for instance, this will make it possible for greater returns to be available not just to direct investors, but also through increased participation in the retirement fund and insurance markets. At some point it could be possible for savings and credit co-operatives (SACCOs) to offer a range of investment services across the country and perhaps for investment services to be grafted onto mobile money transfer systems, as is being considered in the recent Treasury Mobile Direct Project.

There will also be complementary benefits for the East African region as a whole in having easy access to a strong and diverse financial centre in Nairobi. The practical steps described below are designed to deliver these objectives.

It will be important to ensure that the benefits reach the whole of the domestic economy in the context of implementation and strengthening of devolution and that the capital market does not drain resources or create financial imbalances. There also needs to be a focus on raising the level of financial literacy in the country so that the Master Plan strengthens financial access and inclusion ultimately contributing to empowerment. In order to do this, three fundamental steps are necessary which are described in the sections that follow.

Develop a national financial sector approach

For the capital markets to be able to play their own meaningful role in the development of the country, they need to be seen within the wider national context. A holistic approach needs to be developed covering the role of the entire financial sector and its relation to its users. Such a wider approach would serve to highlight what the challenges are across and between the different financial sector components. A cross-sectoral analysis is necessary because both suppliers and users of capital can and should shift over time between product sectors, and especially between the range of banking and capital market channels of finance. This will enable the expected demand for different capital markets products in the context of the Master Plan to be set in the wider financial and economic context.

A nation-wide approach needs to be based on a sound analysis of underlying financing needs. This analysis needs to assess over the period of the Master Plan what financing needs are likely to be across all categories of users of funds and by all categories of sources of investable funds in terms of instruments and providers. In other words, it would assess funding demand and supply gaps, particularly in relation to capital markets products. An important outcome would be the identification of where the largest gaps lie and what the obstacles are to bridging them.

In terms of users of funding it would look at different categories of user such as SMEs, mid-size corporates, multinational corporates, Counties, infrastructure funds, real estate developers, and so on. In terms of instruments it might look at term and revolving lending facilities, bonds, equities, asset-backed securities, structured finance, private placements, private equity, venture capital, and so on. The analysis would then assess the likely supply in relation to each category of user and instrument. This would look at institutional investors such as insurance or retirement funds, credit institutions, collective investment schemes, individual investors, and so on. Without such analysis, there is risk that effort may be diverted to development of product lines for which there is little demand, either in terms of users or suppliers of funds. In order to underpin the development of the Master Plan within the context of overall national financing needs, the action which follows from this (and the first action presented in this Master Plan) is:

- 1.1.1. **- CMA will identify and analyse the funding gap at the national and county level to inform on product development.**

1.2. Address Devolution Funding Needs

The changes to the overall structure of public sector financing and in particular the significantly enlarged role of the Counties, imply the need to develop new forms of funding to support accelerated empowerment of County Governments as well as County level corporates and to respond to County level demands as well as to fund projects with national significance. Such funding is most likely to come in the form of long and short term capital market financing, whether of general revenue needs or project specific (for example of infrastructure). Instruments could be developed in this area along the lines of the provincial or municipal bond markets elsewhere or through the emergence of commodity specific markets in core production areas supported by national derivatives exchanges. There is also a role for private equity and venture financing frameworks to increase the number of entities of a critical size and level of development that they would be able to access public markets. This would serve the dual function of providing additional sources of stable finance at County level and enlarging the range of Kenyan investment products at both the local and international level.
County Governments and market participants would need to work together in order to develop a reasonably homogeneous range of products which would be well-understood by potential investors. These may be based on specific assets or infrastructure investments or County-level corporations. This process should include engagement with the National Treasury on reform of public financial management laws to create more space for Counties to operate; the design by the industry of structured projects to respond to County project specific funding tools; and supporting the emergence of fund of fund structures to increase fund flows for County level venture capital and private equity. The target is that, by end-2023, County Governments should be able to meet 30% of their financing needs through the capital markets.

To achieve this outcome, the **action** is:

- 1.2.1. **- CMA to host forums on county financing needs strategies** in which the Counties and the market participants could develop ideas as to how a County bond market might be developed.

- 1.2.2. **- CMA to partner with relevant stakeholders to develop an adequate legal and regulatory framework** both at the national and county level to support financial sector growth, which will provide a platform for fiscal and financial stability at the devolved level.

1.3. Enhance Consumer Education and Literacy

Most financial literacy surveys conducted worldwide show that a majority of the population do not have sufficient knowledge to understand even the basic financial products and the risks associated with the products. Thus the majority of individuals may not adequately plan for their future and are likely to make ineffective decisions in managing their finances. The same is true in Kenya where a significant proportion of the population has a very limited understanding of financial products and services. This is particularly the case among the rural poor but also across the relatively more affluent peri-urban and urban mass market.

As a result, improving financial literacy and educating consumers around financial products and services has become an essential means toward greater economic, social and financial inclusion as well as an important complement to market conduct and prudential regulation. For capital markets in particular, investor education is important to promote greater retail participation in the market on a sound basis – in other words the best protection for investors is education.

In Kenya, financial literacy, consumer education and investor education are conducted on a sectoral basis across the financial services sector. In most cases, within each sub-sector, whether banking, pensions, insurance or capital markets, these are done separately by the regulator, industry associations, and among individual firms. External, mostly non-profit, donor-funded, organisations also provide financial literacy and education targeted at lower-income groups.

Though each of these initiatives is useful in its own right, a holistic and coordinated approach to financial education is needed to ensure consistent messaging and to educate consumers as to the benefits and risks of the full range of financial products on offer in market, including banking, insurance, retirement, capital market products as well as informal financial products.

At the same time, however, it is important to recognise that different strategies need to be applied to different groups of the population, owing to the heterogeneity of demand for financial services across the country, both demographically and geographically. By way of example, the content of financial education targeting the Kenyans in the rural areas will differ significantly from the financial education provided for the urban retail mass market.

This integrated but tailored approach makes it possible to develop in-depth education for each sector in sequence, rather than attempting to provide a shallow approach across the board.

This is in line with a broader international trend toward developing national strategies for financial education. This follows the adoption by the G-20 in 2012 of the Organisation for Economic Cooperation and Development and the International Network on Financial Education (OECD/INFE) High-Level Principles on National Strategies for Financial Education. These principles provide general guidance on the main desirable elements of efficient national strategies for financial education which should be applied taking into account countries' circumstances and context.

Of course, there is no one-size-fits-all model for the development of national strategies for financial education. In Australia, for example, the market conduct regulator, Australian Securities and Investment Commission (ASIC) coordinates a multi-agency strategy for national financial literacy. In Brazil, the implementation of a national strategy for financial education is driven by the Committee for the Regulation and Oversight of Financial, Capital, Insurance and Pension Funds and Capitalisation Markets (a committee that brings together all financial sector regulators – including the central bank). In the United Kingdom (UK), the web-based Money Advice Service has been developed, with its origin being a statutory obligation on the cross-sectoral Financial Services Authority to provide consumer education, in part motivated by a belief that a well-educated consumer is the front line of financial regulation. There are now efforts in the UK to make financial education a formal part of the national school curriculum. In Kenya, from a legislative point of view, the Consumer Protection Act exists to promote and advance the social and economic welfare of consumers in Kenya by, among other proposals, promoting consumer confidence, empowerment and the development of a culture of consumer responsibility, through individual and group education, vigilance, advocacy and activism.

Once a national policy is adopted, the general trend worldwide is to establish an independent, not-for-profit organisation to manage implementation of policy and to coordinate all stakeholders involved. In South Africa this body (the Financial Services Consumer Education Foundation) is funded by a 0.7 percent levy on net profit after tax for the entire financial services sector under the Financial Sector Charter. In Canada, by comparison, the Investor Education Fund is funded through fines and settlements imposed by the Ontario Securities Commission. Just like in the UK, both the Financial Services Consumer Education Foundation and the Ontario Securities Commission have web-based portals that offer impartial advice to consumers across the full spectrum of financial services products. In the UK the Money Advice Service is funded by a levy on all financial industry participants and managed by a board appointed by the financial regulators.

An illustration of what can be done in Kenya is demonstrated by the objectives of the Money Advice Service which are to:

- Enhance the understanding and knowledge of members of the public on financial matters (including the financial system); and,
- Enhance the ability of members of the public to manage their own financial affairs.
- Its statutory functions include, but are not limited to:
- Promoting awareness of the benefits of financial planning;
- Promoting awareness of the financial advantages and disadvantages with regard to the supply of particular kinds of goods or services;
- Promoting awareness of the benefits and risks associated with different kinds of financial dealing;
- Publishing educational materials or the carrying out of other educational activities; and,
- Providing information and advice to members of the public.

Against this context, specific actions to enhance consumer education and literacy in Kenya include:

- **1.3.1. - CMA to support the development of a national consumer financial education policy and strategy** in consultation with key ministries (National Treasury and Ministry of Education, for example) and a cross section of relevant stakeholders (including regulators, industry associations, academics, external organisations like the Financial Education Partnership for Kenya, and any others which may be relevant).

  This national consumer financial education strategy should define target groups using a risk-based approach to decide on which target groups to focus on (such as university students, retail investors, consumers (e.g. farmers) and mass market). Components of the strategy could include:

  - A framework (including a national committee and strategy) for collaboration and coordination of financial sector stakeholders around consumer financial education;
  - Recommending the allocation of funding for consumer financial education programmes and initiatives;
  - Key performance indicators, data and measurement of consumer financial education programmes to determine whether policy and programme goals are being achieved; and
  - Advising on the development of broad-based curricula and materials. The lower the age at which financial education commences (for example at primary school level), the more impactful the longer term outcomes will be. Balanced against this is the need to achieve rapid results, which points to targeting those just at the point of entering the labour force (i.e. secondary and tertiary students).

- **1.3.2. - CMA to continue implementing its own Investor Education and Public Awareness programme, subject to its own area of competence.**

2. GATEWAY FOR REGIONAL AND INTERNATIONAL CAPITAL FLOWS

The objective of the second building block of the Master Plan is to position Kenya at the heart of financial services industry in Africa, both within the East African Community (EAC) and more widely. To this end, two areas of work are identified under the Master Plan.

2.1. Leverage East Africa as an Integrated Market

A critical element in enabling Kenya to be a key international centre will be to press hard for harmonisation of financial market regulations in the EAC, wherever possible in the form of identical regulation.
Experience in Europe on this subject suggests that "harmonisation", meaning implementing in similar ways, offers limited gains in terms of efficiency to market participants, whereas identical implementation can greatly reduce management, compliance and information technology costs. Having understood this, most new directives in the European Union now have to be implemented in precisely identical ways.

Although a series of EAC Directives have been developed in order to set down agreed upon convergence of standards for the regional markets that are at substantially different levels of development, it seems that there has been very limited progress in their implementation at a national level in respective states. This will require enhanced engagement with other EAC Members to demonstrate the common interest and benefit in creating a functioning single EAC market. One way to re-energise this process might be to seek to gather consensus around a vision of what a single EAC market in financial services might ultimately look like. Such a vision could consist of the following:

The EAC market in financial services will be an innovative and competitive financial marketplace within which lenders and borrowers, issuers of securities and insurance policies, providers of pensions and of financial market services, will interact freely, on a non-discriminatory basis, with lenders, investors and policyholders, and pension plan providers. They will do this on the basis of common and proportionate prudential and conduct regulation and investor or customer protection, on a remote, cross border basis if they choose, and have access to all necessary market infrastructure, wherever located, without necessarily requiring a local presence. The market for corporate ownership will safeguard the interests of investors and operate within a framework of sound proportionate corporate governance and takeover arrangements, and be subject to high quality financial reporting and auditing standards.

If such a legal framework were to be achieved, there would be benefits across the EAC, with final users of financial services obtaining clear benefit wherever they were located while financial institutions would decide to locate in whichever locations proved competitively the most attractive to them.

Without such a legal framework it will be less likely that non-EAC firms would see much advantage in establishing in Kenya in order to access the region as a whole.

One way in which progress might be achieved over time in the purely capital market sphere is to proceed by stages; a process discussed when there was an assisted self-assessment of each of the East African capital markets for compliance with the International Organisation of Securities Commissions (IOSCO) Core Principles in 2010. As a general underlying matter it is important that the definition of the main market abuse offences and competency, certification and conduct standards be as consistent as possible so as to avoid very serious cross-border market distortion and abuse.

The first essential step would be to reach the position where each regulatory authority is able to accept that a prospectus approved in another EAC country could be distributed throughout the authority's own jurisdiction without separate approval.

Mutual recognition would also be the basis for allowing intermediaries to operate on an EAC-wide basis. An intermediate step would be to permit all brokers to access all exchanges but only provide services to investors in their own jurisdiction. The final step would be to allow intermediaries to trade on any exchange and to offer services anywhere in the EAC. To be able to achieve this, the East Africa Member States Securities Regulatory Authorities (EASRA) would need to be able to accept that an intermediary that received a license in another EAC country would be able to operate in their own jurisdiction on the basis of their home country license.

It would not be necessary to have all the provisions necessary to operate a single market substantively in place until all the other preparations for a single market are ready.

Equally, it would result in long delays to the regionalisation project if the process of legislative amendment were not to begin until all the other preparations were complete.

If importance is attached to the achievement of a single EAC capital market within the foreseeable future, as would be necessary if the Master Plan is to contribute maximum benefit for East Africa as a whole and if international participants are to be attracted, CMA and the National Treasury need to have a clear, prioritised action plan to carry forward within the EAC framework.

In the near term, however, the Kenyan authorities should not stand in the way of efforts by the market to be creative in encouraging investors to become comfortable with cross-border products. Actions to this effect include:

- 2.1.1. - **Support discussion on regional financial integration.** CMA should promote continued discussion within Kenya and within the EAC to arrive at a common view as to the ultimate destination for the East African single market in financial services and on the optimum phasing, including timing, of the steps necessary to achieve this goal for the capital markets.
- 2.1.2. - **Develop creative products that promote investor comfort in regional products.** As a precursor to a regional market, one of the ways of stimulating the market and getting investors comfortable with regional products is to encourage the market to be 'creative' in the short term. Strategies to develop Kenyan or East African Depositary Receipts should thus be considered by the Implementation Committee and by relevant market stakeholders (for an overview of Depositary Receipts see box 1 in section 4 below).
- 2.1.3. - **Support regional financial market infrastructure linkages.** A strategy should also be developed between EAC member-state regulators (EASRA) and member state infrastructure providers to drive the process toward establishing linkages in trading, settlement and clearing infrastructure between EAC member countries.

2.2. Capital Market Financing for Kenya's Core Strengths

To become the heart of African capital markets Kenya will develop expertise in a number of services. In doing so, Kenya will become a centre of excellence for capital markets and attract international investment into its domestic capital markets and into the region more broadly.

Kenya has already well-developed banking, insurance, and pension sectors. These more traditional financial services sectors are well suited to the needs of an emerging market. However, as the economy becomes more sophisticated, the demand for more advanced financial services among a wider range of users will outgrow traditional sources. In this environment users such as infrastructure funds, real estate developers, financial sponsors, high potential SMEs, including technology companies, and fast growing local mid-corporates will require access to more varied sources of finance and risk management. The availability of different categories of finance will make it possible for borrowers to progress through different types of funding, ultimately up to the main market, as their needs evolve over time. The development of expertise in asset management, private equity/venture capital, private placements, Islamic finance and financial derivatives are therefore important components of the Master Plan that will position Kenya as a centre of excellence for raising sophisticated funding.

Centres of excellence will be created across the following financial services:

Commodities spot and derivatives markets

Under Vision 2030 key sectors of the economy are being strengthened. Agriculture, for example, has been identified as one of the key drivers of the economy, in order to sustainably achieve average economic growth of 10 per cent, reduce poverty levels and boost food security. In addition, recent discoveries of oil, gas and other mineral resources are likely to sustain the creation of new industries over the next few years. Finally the country's potential for clean energy use in geothermal, hydroelectric, wind and solar power also supports the creation of a large energy sector that can support the growth of the broader region. As these sectors flourish, the capital markets will be well placed to offer spot markets and derivatives markets based on agriculture, energy and mineral/metal commodities.
The development of a Warehouse Receipt System for agricultural products will greatly benefit farmers as this will give the farmers an organised market for their produce. Such a market will monetise agriculture that is presently subsistence-based and will also enable farmers to hold their produce via a negotiable instrument rather than sell it immediately on harvest. The negotiable instrument can then be used as collateral for finance and is tradable. This will also provide the underpinning of, initially a spot commodities market and, later, a derivatives market, which will enable farmers and food producers to protect themselves against commodity price volatility.

There are actions in section 4.2 of this document to develop a Warehouse Receipt System and commodities spot and derivatives markets.

Infrastructure and construction finance

The capital markets play a key role in providing long term funding for large infrastructure projects such as the development of transportation networks, extractive industries, technological connectivity and utilities infrastructure – projects which all form part of the Vision 2030 developmental agenda. The National Treasury has published a National Priority List of 47 public private partnership infrastructure projects. These have a requirement for private sector funding of at least $27 billion over the next ten years, indicating an infrastructure funding gap of $2-3 billion per year over this period. The size of the required investments for large infrastructure projects makes the capital markets an ideal channel for mobilising international financing for these projects. The target is that the share of infrastructure investment financed through the private capital markets, by means of listed equity, private equity or bond issues, should rise to 25 percent by 2023. (This is separate from private sector financing provided internally by private sector partners.)

The infrastructure bonds so far issued in Kenya do not have income streams associated with the underlying asset and cash flows for the bonds and are paid directly out of Government tax revenues. Some of the barriers to realizing the infrastructure needs include; shortage of well-prepared projects, regulatory and institutional obstacles as well as the lack of capital and expertise for risky, early-stage project development. The regulatory and institutional obstacles relate to the lack of public-private partnership legal frameworks to ensure the delivery of efficient and cost effective infrastructure. This is because private sector participation ought to be governed by specific regulations or long term concession contracts. Institutional arrangements are also needed to ensure the sustainability of private sector participation. We now have a Public-Private Partnership (PPP) framework in place which is expected to spur activity in the infrastructure finance capital raising sphere going forward.

The real estate and construction sector has already grown considerably during the first Medium Term Plan period as a result of higher infrastructure spending and housing construction. As this infrastructure spending continues and as the demand for housing, office space, retail services and tourism facilities increase, the sector will become a key user of long-term capital market products. Through supporting the development and use of innovative products such as Real Estate Investment Trusts (REITs) and encouraging greater institutional participation in the sector, the Master Plan can play a key part in developing a vibrant construction and real estate sector.

As the capital markets develop expertise in supporting these domestic projects, Kenya will be able to support similar projects within the East African region and across Middle Africa. This will further enhance the opportunity for Kenya to hold itself out as a regional centre for the export of construction-related services, such as architecture, engineering, project management, planning, and other services. Such clusters of related financial and non-financial businesses are characteristic of centres such as London or Singapore.
To support this outcome the following actions should be taken:

- 2.2.1. - **Review obstacles to raising finance for infrastructure projects.** A review should be conducted to inform what challenges exist to raising finance for infrastructure projects through the capital markets. The outcome of this review should be to identify challenges at the level of supply, demand, legal and regulatory environment and at the level of financial market infrastructure that are preventing infrastructure providers from accessing capital markets efficiently.

- 2.2.2. - **Assist potential infrastructure issuers in coming to market.** A framework needs to be developed such that potential infrastructure issuers (whether public or private) can be identified and guided through the process of obtaining finance from the capital markets. This framework should also facilitate the process of obtaining regulatory approval so that efficient access to capital market funding is not seen as a barrier to infrastructure providers.

Financial services

As mentioned earlier, Kenya has a well developed banking, insurance and pension fund financial services sub-sectors that cater to the needs of retail and institutional clients across the country. In comparison, other financial services sub-sectors are less developed. The independent asset management sector and the market for Islamic finance in particular are not well developed. The development of these sub-sectors, however, is fundamental in the context of deepening Kenya's capital markets and creating a wider range of innovative products for domestic investors and for foreign investors interested in investing in Kenya.

Asset management

The asset management sector is an important component of capital markets. The sector includes the management of funds by institutions, such as pension funds and insurance companies, and the independent management of funds for retail investors, which can be distributed as collective investment schemes (or unit trusts). The latter are particularly important, as they provide an opportunity for small investors to have access to professionally managed, diversified portfolios of assets. As institutions directing the investment decisions for investors, asset management companies are important buy-side institutions.

The opportunity for private sector pension schemes to opt out of the NSSF, provided they meet certain criteria, emphasises the importance of a thriving and cost-efficient asset management sector to manage pension fund assets. The development of a strong asset management sector is therefore critical to facilitate access to the capital markets by investors whether they are retail, wholesale or international investors. Development of specialist products, such as REITs, can also support the contribution of the capital markets to infrastructure investment in the economy.

The development of a centre for asset management services based in Kenya hinges on creating a two-way flow; of international investment coming into Kenya; but also of outward investment to enable Kenyan savers to diversify their holdings. As Kenya develops its role as a regional financial hub, there is potentially a virtuous circle in which financial and related services firms create the base of knowledge and expertise necessary for an asset management industry and the growth in assets under management in turn attracts additional firms and supports the development of the financial centre. As the financial centre develops, it will increase its attraction as the centre for fund management groups to headquarter their regional offices.

The target is that assets in collective investment schemes under management in Kenya should increase from USD 360 million in January 2014 to USD1.2 billion in 2020, rising to USD2 billion in 2023.

To support the creation of this market the following actions should be taken:

- **2.2.3. - Implement actions contained in the World Bank/IFC report on mutual funds.**[2] Drawing upon the recommendations made in the World Bank, IFC, IOSCO, and CMA Case Study on Kenya's Mutual Fund Industry Report (2013). Drawing upon the recommendations in the report, these actions include;

    - Take a policy decision on CISs to be enabled under the capital markets legal framework and define the legal and regulatory frameworks that will be needed to widen the range of funds made available and the needs they can address, including attracting diaspora savings;
    - Merge the two existing trade associations to maximise impact, focus attention and minimise cost;
    - Revise the Securities and Investments Bill and underlying regulatory frameworks to strengthen investor protection and make provision for the agreed range of CIS's to be enabled to improve choice;
    - Review tax rules to improve provision of corporate CISs to provide greater certainty and enhance confidence;
    - Develop Government policy on regulation of financial advice;
    - Develop a comprehensive and fair trade association information and data section on CISs on the CMA website; and
    - Draft legislative and regulatory frameworks for regulation of financial advice.

2 World Bank and IFC (2013) *Case Studies for a Study on Key Impediments to the Growth of Mutual Fund Industries in Developing Countries (Kenya)*

- 2.2.4. - **Examine the tax structure of collective investment scheme products.** A review should be conducted of the tax arrangements and implications for investors associated with purchasing collective investment scheme (CIS) products as provided by asset management companies. The purpose of this review is to identify potential tax levers that may incentivise greater uptake of CIS products by investors, including international investors. In addition, the review should identify and propose ways of addressing potential tax issues that prevent the development of a facilitative environment for CIS products, including closed-ended investment companies (also referred to in 2.2.3). Such a review, for instance, has already been conducted by CMA in relation to REITs - the outcome of which has been to draw attention to necessary amendments to the Income Tax Act to effectively address the taxation of REITs in line with stated policy. To ensure the recommendations made in this review are implemented, therefore, part of this action should be to follow up on the status of the taxation framework for REITs.

Islamic finance

The market for Islamic financial services is still nascent in Kenya. However, given the country's geographical position, sizeable Muslim population, and infrastructure funding needs, there is great potential to develop a centre of excellence in Islamic financial products in the country and for the region. The development of additional capital market Sharia-compliant products and services in particular is important to support infrastructure project funding as envisioned under the Vision 2030 strategy and hence is a priority under the Master Plan.

In terms of the broader Islamic financial services market, CBK has to date licensed two Islamic banks - Gulf African Bank and First Community Bank (FCB), while various other banks are offering Sharia-compliant services and products through "Islamic Windows". Similarly, FCB has been authorised to act as an Islamic insurance (Takaful) broker for general Takaful products. In addition, Takaful Insurance of Africa, the first fully Sharia-compliant insurance company in Kenya, was launched in January 2011. In 2014, the launch of the first Re-Takaful Insurance (Islamic re-insurance) is expected as the Kenya Reinsurance Corporation ventures into Sharia-compliant business. The local reinsurer already has presence in West Africa and Middle East markets and hence has the potential to provide a regional platform for this product.

In the capital markets, CMA has also licensed FCB Capital, which offers Islamic asset management services. In addition, Genghis Capital has been approved to operate an Islamic CIS. CMA has also introduced new regulations relating to REITs and these regulations provide for the creation of Sharia-compliant REITs. These developments have enabled the formerly unbanked Kenyans and specifically the Muslim communities in the country to have access to financial services adding to the wealth creation in the economy.

However, to develop a centre of excellence in Islamic financial products underpinned by a formal framework, a concerted program of regulatory reform and recognition as well as broader capacity building will have to be undertaken so that Islamic financial services become a sector in their own right capable of attracting international business. To achieve this outcome, the following actions should be taken:

- 2.2.5. -**Create a regulatory framework for Islamic capital markets.** In the short term, include provisions in the current framework for conventional capital markets covering Islamic finance (under jurisdiction of the CMA) and focusing on corporate governance, disclosures, a Policyholder Compensation Fund, and responsible pricing (borrowing from guidelines adopted in other Islamic jurisdictions).

  This would also include developing capacity within financial sector regulators (Institute of Certified Public Accountants of Kenya and the Kenya Revenue Authority) to regulate Islamic capital markets.

- 2.2.6. - **Develop a separate policy, legislative and regulatory framework for Islamic products and services** (that cover Islamic financial institutions, financial regulators, Islamic groups, and the Ministry of Finance) that runs parallel to the conventional Act. This is a long term project, but this framework should provide the legal basis for the Islamic finance sector by giving explicit recognition for Islamic financial services in all relevant financial sector legislation (i.e. in the Acts governing CMA, CBK, SASRA, Retirement Benefits Authority, Insurance Regulatory Authority as well as the Kenya Revenue Authority Act to address taxation issues). As the policymaker for the financial sector, the National Treasury should take the lead on this initiative as part of a concrete financial sector strategy to acknowledge that Kenya will become a hub for Islamic finance services. This will include:

- Put in place an Islamic standard-setting body. Develop (and give legal recognition to) a single national Sharia advisory board or council - to provide guidance on product authenticity through screening and qualification for the entire Islamic finance industry. This body would set rules, guidelines and policies for all subsectors of the Islamic finance industry. The Sharia board will be able to review the investment framework for Islamic finance in terms of permissible products and other requirements governing investment by Islamic finance providers.
- Create an Association of Islamic Financial Institutions to act as a champion for the entire industry (with membership from banks, insurance providers, fund managers and SACCOs that provide Islamic financial products and services). This new Association needs to be recognised in regulation.
- Work with ICPAK and the relevant international authorities to secure recognition within IFRS of accounting standards provided by the Accounting and Auditing Organisation of Islamic Financial Institutions (AAOIFI) and within ISAs of auditing standards set by the Islamic Finance Services Board (IFSB) for Islamic financial services.

- 2.2.7. - **Leverage existing relationships to develop Islamic finance expertise.** CMA should leverage existing relationships with regulators and with financial market infrastructure providers in other countries to develop Kenya's Islamic finance markets. To this end, CMA should draw upon the existing Memorandum of Understanding (MOU) with regulators in Malaysia to receive long term resident support to develop knowledge and rules for the Islamic finance market. It could also look to explore its working relationships with the London Stock Exchange and UK regulatory authorities on how to promote and develop Kenya's Islamic finance markets.

- 2.2.8. - **Identify and make policy proposals to facilitate development of Islamic finance in the annual Memorandum of Policy Proposals to the National Treasury and implement programmes through industry coordination and relevant partnerships.**

3. PROVIDING ACCESS TO INTERNATIONAL FINANCIAL MARKETS

3.1. Alignment with NIFC

The objective of the third building block of the Master Plan is to enable Nairobi to join the ranks of other international financial centres. This builds on and strengthens the domestic and African objectives; a strong domestic and regional financial centre makes Nairobi more attractive as a location for international financial firms, while access to international financial markets enhances their ability to achieve domestic objectives.

A tangible objective of this programme will be to achieve MSCI Emerging Market status for Kenya by 2020 and for Nairobi to enter the Global Financial Centre Index (GFCI) ranking of financial centres published by the Z/Yen Group and to move up the same table. The target for the latter is to achieve a ranking of 70 by 2020 (roughly equivalent to the current position of Mauritius) and 50 by 2023 (which would be higher than the current ranking of Johannesburg and Rio de Janeiro). Both ranking systems are based largely on qualitative assessments by people and organisations and the key capital market assessment criteria are detailed in the *Implementation process and Roadmap section below.*

For Kenya to become an International Financial Centre multiple conditions need to be met. These include: an attractive business environment with access to experienced and qualified staff, a legal and regulatory regime that gives confidence; a critical mass of financial and professional services firms present and a network of connections with other financial centres. To a large extent this is the culmination of other building blocks in the Master Plan, which come together to create the conditions for Nairobi to develop its international status. However, further actions are required to complete the process.

This will require close cooperation between CMA and NIFC so that CMA can best support the development of the centre. The newly-formed Steering Committee on the NIFC can play an important role as a focal point in coordinating the policy developments necessary to achieve this objective. Two key actions emerge:

- 3.1.1. - **Implementation Committee, together with other relevant authorities, should establish a process for monitoring progress in international rankings,** with the objective of achieving MSCI Emerging Market status and being included in the GFCI ranking.

- 3.1.2.- **CMA to be represented on the Steering Committee of the NIFC.** In order to assist in the promotion and monitoring of the many conditions necessary to create a financial centre of international status, it would be desirable, in view of the central importance of the capital markets, if CMA was represented directly in the Steering Committee of the NIFC.

3.2. Advocate for an Attractive Business Environment

There is intense competition among developing markets to attract international financial institutions, which must meet numerous compliance requirements in their own jurisdictions and which will look for attractive business conditions abroad.

In this context it is necessary to align domestic requirements with international standards so that would-be entrants into the country can operate in a similar way as they do in their home market. To this end two key areas need to be strengthened:

International home country regulatory requirements

International firms must comply with a number of conditions set by their home country regimes, which include anti-money laundering and combating the financing of terrorism (AML/CFT) rules internationally and, in Europe, the requirements of the Alternative Investment Fund Managers Directive (AIFMD). Kenya needs to put the necessary measures in place to enable foreign firms to comply with these requirements in areas where it currently falls short, since otherwise these firms will simply direct their operations to countries where compliance is easier, particularly given the very heavy penalties now being levied on international firms for breach of compliance. Actions proposed to strengthen market infrastructure (section 5 below) will help with AIFMD compliance. The following action is relevant here:

- 3.2.1.- **Kenya to take action to raise its AML/CFA rating.** CMA needs to contribute to the steps Kenya needs to take materially to upgrade its current poor rating by implementing the Action Plan set out by the Financial Action Task Force (FATF). The latest FATF assessment in October 2013 notes that:

Kenya has taken steps towards improving its AML/CFT regime, including by parliamentary approval of the Finance Bill, which amends the FT offence; however, this is still awaiting Presidential assent. Despite Kenya's high-level political commitment to work with the FATF and ESAAMLG to address its strategic AML/CFT deficiencies, Kenya has not made sufficient progress in implementing its action plan within the agreed timelines, and certain strategic AML/CFT deficiencies remain. Kenya should continue to work on implementing its action plan to address these deficiencies, including by: (1) adequately criminalising terrorist financing; (2) ensuring a fully operational and effectively functioning Financial Intelligence Unit; (3) establishing and implementing an adequate legal framework for the identification and freezing of terrorist assets; and (4) implementing an adequate and effective AML/CFT supervisory programme for all financial sectors. The FATF encourages Kenya to address its remaining deficiencies and continue the process of implementing its action plan.

Tax regime

Tax plays an important role in the relative attractiveness of an international financial centre, including its role as a centre for capital market business. The tax arrangements need to be both competitive for the users of the markets and acceptable for their home country tax authorities, especially when there is heightened international emphasis on reduction of inappropriate tax avoidance. Pertinent actions that will require CMA to work with the relevant authorities are to:

- **3.2.2. - Extend Kenya's network of Double Taxation Agreements while managing risks of investment practices such as transfer pricing.**

- **3.2.3. - Ensure Kenya adopts OECD standards wherever possible.** For example covering the Treaty Relief and Compliance Enhancement (TRACE) for cross-border portfolio income tax relief.

- **3.2.4. - Ensure standards for information exchange on taxes are in line with requirements of the OECD Global Forum on Transparency and Exchange of Information for Tax Purposes.** This will minimise risk of blacklisting by important investor countries with the aim of moving to "Full Compliance under Phase 2".

- **3.2.5. - Ensure personal and corporate tax are attractive to internationally mobile employers and employees.**

- **3.2.6. - Review the adequacy of the corporate and personal tax framework for financial services** against international practice and in the context of creating and promoting an International Financial Centre.

3.3. Establish and Develop International Linkages

Financial centres around the world form a network of connected services linking borrowers and lenders, risk takers and risk mitigators from different countries and different continents. Much of this network consists of business relationships between firms that work together and the branch networks of international firms, but these depend on a foundation of legal and regulatory agreements and technical interfaces that make it possible for business to flow between centres.

If Kenya's ambitions are realised it will become part of this network. To a large extent this will be the result of steps taken as part of the Master Plan to create modern and open financial markets in Kenya which will attract international business. Work should be undertaken on developing the key structural links with other market places including to:

- **3.3.1. -Putting in place Regulatory MOUs to allow for the exchange of confidential information.**

  The following actions to link markets, which are described in later sections, are also relevant to creating international linkages:

  - Remote access to infrastructure (for example driving Direct Market Access to the Nairobi Securities Exchange) – see section 4.1.
  - Use of Depositary Receipts (DRs) to open markets in both directions (inward and outward) - see the box and actions in section 4.1.
  - Development of Euroclear and Clearstream links - see section 5.1.
  - Infrastructure linkages with other EAC markets and post-trade infrastructure - see section 2.1.

II. THE INFRASTRUCTURE OF THE MARKETS

Kenya's financial markets are at different stages of development. Kenya has a well-developed and liquid government bond market (the size of which is dependent on government financing needs). The equities market is characterised by relatively few listings, which are skewed towards financial companies, and low liquidity. Commodity markets exist only in the underdeveloped form of the Mombasa Tea Auction and the Nairobi Coffee Exchange.

Nevertheless there is considerable international investor interest in Kenya, which is not currently met due to shortage of assets, lack of liquidity and inadequate infrastructure. Therefore, Kenya needs to improve the actual operation and infrastructure (both physical and human resources) of its capital markets in order to:

- Increase product supply and trading activity of existing markets;
- Add new markets and products; and
- Upgrade infrastructure to international standards to improve the security and risk management of the markets and to attract more international players.

To develop Kenya's financial markets, this Master Plan has ambitious targets for improvements in listings, liquidity and performance of new product areas and these three building blocks below each contribute to achieving the objectives of growing and deepening existing markets as well as developing new markets. These targets are designed to reflect developments that can be shaped by the Capital Market Master Plan rather than by external factors. Specifically, the targets are:

- The ratio of equity market capitalisation to GDP to rise from 50% now to 70% by end-2023, putting Kenya slightly above the world average;
- The number of GEMS listings, which reflect the supply of future main board listed companies, to increase by 3-4 per year;
- The ratio of value of corporate bonds outstanding to GDP to reach 40% by end-2023; and
- The value of outstanding exchange-traded derivative contracts to reach $200bn by end-2023 - an ambitious target, given that the market has not yet been launched, but is achievable when compared with other markets.

4. DEEPER, MORE LIQUID DOMESTIC MARKETS

The actions recommended under this building block provide short-term to medium-term improvements that can strengthen the existing markets and develop new ones.

4.1. Enhance Securities Markets

There are many short and medium term enhancements that can be made to the existing securities markets to enhance their liquidity.

More sophisticated securities trading arrangements

One way in which liquidity in markets can be improved is by introducing market makers. Market makers are firms, who meet necessarily stringent capital and operational requirements, who are obligated to provide a two way price in certain securities in order to ensure that there is always a certain amount of liquidity in these stocks. This means that investors always have the opportunity to buy or sell. This can greatly improve liquidity. It is, therefore, recommended that a Market Making arrangement be implemented at the NSE by making arrangements for certain member firms which meet the requisite criteria to provide continuous two way prices for individual stocks. Market makers will guarantee to provide a two-way price with a maximum spread, for a certain volume for a certain period each day.

- **4.1.1. - Introduce arrangements for market making in the equities market**

- **4.1.2. - Introduce market-making arrangements for the Government bond market.**

Market makers in the bond market could be the same members as primary dealers.

For market making to operate effectively, market makers will need the ability to sell short in order to meet their obligations (that is . to sell stock to buyers which they do not currently have). This shortfall is covered before settlement from later purchases or from stock borrowing

- **4.1.3. - Develop regulations to allow for short selling.**

  Stock lending and borrowing. In order for market makers to do their job they will need the ability to borrow stock from time to time to meet their obligations. Therefore, a Securities Lending and Borrowing (SLB) arrangement needs to be put in place. Such a service can also be used by other market participants to meet unexpected delivery shortfalls or short selling operations. With the introduction of stock lending, investors will be able to allocate all or part of their holdings at the Central Depository and Settlement Corporation (CDSC) to a lending pool (if so allowed by their investment guidelines). Market participants (not restricted to market makers) will then be able to borrow stock from this pool for a fee paid to the holders. The borrowed stock can be used to meet delivery obligations resulting from short selling.

- **4.1.4. - CMA to provide explicit recognition for SLB in the legal and regulatory framework**

- **4.1.5. - Regulators to change investment guidelines to permit SLB**

- **4.1.6. - CDSC to put in place necessary technical arrangements to allow for SLB**

  Pre-funding: The requirement for pre-funding is a barrier to international investors. Currently, an investor wishing to trade has to provide access to its account to a broker so that the broker can ensure there is the required stock in the account before placing the order.

  Instead, changes should be made to remove this requirement and replace it with a requirement for all investors to ensure delivery of stock for settlement. If they do not, sanctions can be put in place (such as fines or suspension of brokers whose clients fail to settle on time). The introduction of SLB (as mentioned above) will reduce the risk of settlement failure if an investor unexpectedly finds himself short of stock.

  This change will make it safer and easier for international firms and will bring Kenya in-line with international practice.

- **4.1.7. - CMA to remove its requirement for pre-funding**

  Direct Market Access (DMA). DMA is an arrangement whereby investors (domestic or foreign) can access the technical trading infrastructure of the exchange directly. This arrangement allows for speedier trading. The broker remains responsible for ensuring, as for any client, that Know Your Customer (KYC) standards are met and trades are still undertaken in the name of a local broker and he is still liable, for the performance of such trades but orders can be placed without his direct intervention. There is currently no technical barrier to such a change but rules at the NSE need to be modified to allow for it.

- **4.1.8. - NSE to change rules to allow for DMA.**

  Block trading. The trading of large blocks of shares is often undertaken at a price different from that currently available in the market. Exposing such large orders to the market can impact that price. Therefore, a facility should be provided so that large blocks of stock can be traded directly between brokers and then reported after the fact to the exchange. Rules will need to be put in place to determine what size of transaction constitutes a block trade, what deviation from market prices is allowed and to ensure that such trades are reported to the market (and the prices distributed) within a reasonable time frame (which may depend on the size of the block traded). Such rules are needed in order to prevent liquidity moving to a dark pool of trading that is not seen by other investors.

- **4.1.9.- CMA to introduce rules to allow for block trading.**

Hybrid bond market: There are now rules and regulations in place to allow for trading of bonds between Authorised Securities Dealers. This trading can be enhanced by the introduction of a dedicated bond trading platform and this should be chosen and introduced as soon as possible.

- **4.1.10. - Implement trading platform for the hybrid bond market.**

Primary dealer arrangement for Government bond market: The primary issuance of bonds by the Government is a manual and inefficient procedure. This, and liquidity in the secondary market could be improved by introducing the concept of primary dealers – firms that are obligated to carry out market-making activities in Government securities and take actively take part in primary market auctions.

- **4.1.11. - Implement primary dealer arrangement for Government bonds.**

Local Depositary Receipts (DRs) for international companies: Box 1 below describes the concept of DRs and suggests several ways in which they can contribute to this Master Plan. One of these is for the NSE to list DRs of attractive foreign companies to provide additional investment opportunities for local investors which could, in turn, improve the attraction of the NSE to investors as it gives them a wider range of stocks to invest in. The companies could be those which already have an involvement in the Kenyan economy (and which already have brand recognition) and major regional companies.

The creation of DRs is carried out by investment banks which create DRs from a holding of the underlying stocks.

If current listing criteria are broad enough to cover the listing of DRs, a 'no action' approval by CMA on the listing may be appropriate. If they are not, actions need to be taken to make the necessary changes.

- **4.1.12. - NSE to promote listing of international DRs.**

Margin trading. Trading on margin (whereby people invest using borrowed money) is a feature of many international markets and has a positive effect on liquidity. Rules and regulations have to be put in place so that the loan has adequate security (usually using collateral of other shares already owned). CMA already has a policy framework which it needs to implement.

- **4.1.13.- CMA to issue regulations allowing for margin trading.**

Development of the stock exchange

Demutualisation and listing of NSE. The delays to full demutualisation have been negative for the reputation of the NSE. Experience has shown that once an exchange is fully demutualised and is no longer under the specific influence of a narrow group of owners it becomes much more responsive and dynamic. This process should be accompanied by NSE being listed on its own main board. At the same time, the NSE should undertake a programme of education and public relations to ensure the investment community knows that it is now a new and improved organisation in order to remove any previous negative perceptions.

- **4.1.14. - NSE to complete the demutualisation and listing process.**

Re-branding of NSE: The opportunity for demutualisation and listing of the NSE allows for a break with the past. Serious consideration should be made by NSE to use the opportunity, as has happened on several occasions overseas, to re-brand itself. This should be further reinforced by separating the regulatory and commercial aspects of its business to address potential conflict. This should be inspired by efforts undertaken by Exchanges such as New York, Mauritius, and Moscow.

- **4.1.15. - NSE to implement a re-branding strategy**

NSE to set its own fees: Centrally determined fees do not give an organisation the ability to manage its business most effectively. Once the NSE has fully demutualised it should be given the authority to set its own fees so that it can obtain and allocate the resources it needs and can rapidly respond to market developments and opportunities. However, it is important that the fee structure is completely transparent so that participants (both existing and those contemplating to join) know exactly the complete cost structure of participation.

In addition, as the recent study into Fees and Commissions found[3], the critical consideration first and foremost must be to build volumes and fees should be set at appropriate levels to achieve this objective, as efficiency improvements are passed through to users.

- **4.1.16. - National Treasury to grant NSE freedom on fee structure subject to competition and consumer protection controls**

In the absence of competition to the NSE there could be a concern that the NSE would raise fees unfairly. To prevent this, there clearly needs to be a strong Competition Authority to intervene in the event of complaints about unreasonable fees (see action 9.3 below). In addition, this freedom can only be given where there is the potential for effective competition. Therefore, it is important that new suppliers of exchange and clearing infrastructure be permitted to operate in Kenya (assuming they meet the necessary criteria). CMA should ensure that the approval process for such new infrastructures is straightforward and efficient. This should include an SLA for the process.

- **4.1.17. - CMA to ensure approval process for new infrastructures is straightforward and efficient.**

Free and non-discriminatory access to infrastructure. Markets will not develop if artificial restrictions are put in place on who can participate in them. Access should be given to all firms who meet reasonable participation requirements (and which have to apply both to existing members and potential members (such as liquid capital, operational expertise, and risk management arrangements). Such barriers include unreasonable costs for new participants. This point is further developed in section 9 of the Master Plan.

- **4.1.18. - NSE to remove any artificial barriers to membership for new participants.**

Greater depth in the domestic securities market

The next group of recommendations mostly refer to the equities markets. As mentioned above, the bond market is already deep and liquid. Both markets, however, need to function actively. While debt is well aligned to funding infrastructure in public markets, private sector wealth creation largely comes through public equity markets.

Number of listed companies: As mentioned above, Kenya has relatively few listed companies. Any unnecessary barriers to companies listing need to be removed so that more companies come to market. There is a perception that the process of listing is expensive and challenging to eligible companies often do not understand the benefits of listing as compared to alternative sources of finance.

The benefits of listing need to be made more explicit to companies and the process of becoming a listed company needs to be clearly outlined and made less onerous.

- **4.1.19. - Industry (CMA, NSE and KASIB) to promote the benefits of listing.**
- **4.1.20. - CMA to publicise the streamlined listing application procedure.**
- **4.1.21. - Solicitor General to streamline company registration and compliance procedures.**

3 CMA (2013) *CMA Study on Capital Market Fees, Commissions and Levies*

- **4.1.22. -Review law on foreign ownership capping framework to make it more flexible and responsive to National Policy objectives**

There are legitimate national policy objectives in having foreign ownership limits in Kenyan equities, but it is recommended that a review be done to the entire capping framework to give opportunity to other methods aimed at maximizing the benefits of the foreign ownership ceilings. National policy objectives ensure participation of specific categories of investors in capital market issuances, including promoting local ownership, and protection of strategically important or sensitive companies and sectors.

The reason for suggesting this change is that the blanket 75 percent ceiling currently has an impact on liquidity of certain stocks and this is likely to be exacerbated as foreign investors continue to increase their investment in the Kenyan market. Besides this direct impact, there is a negative perception of such restrictions (e.g. foreign ownerships limits and the practical impact of them make up two of the 18 criteria of the MSCI assessment of openness of markets to foreign investment). As Kenya aspires to qualify for the MSCI ranking as well as have Nairobi as an International Financial Centre, the review of the foreign ownership framework is a necessary condition.

The review would look at various other solutions, such as allocating particular percentages of stock at Initial Public Offerings (IPO) of Government owned shares to Kenyan or East African residents. To protect strategically important companies, specific foreign ownership limits or minimum Government holdings could be imposed for particular sectors of national significance

Global Depositary Receipts and Notes for equity and debt issues. (See the box below for a general description of Depositary Receipts). Stocks which may be attractive to foreign investors could be packaged in Sponsored Depositary Receipt form, denominated in a major international currency (USD or GBP) and listed on foreign exchanges to make them more accessible to international investors. This could improve knowledge and understanding of Kenyan products. Liquidity in such products developed overseas would later move back to Kenya as the market developments outlined in the Master Plan are implemented.

- **4.1.23. - Consider GDRs and GDNs for both equity and debt issues to make them accessible to international investors**

Kenya Depositary Receipts (KDRs) as a potential alternative to creating CSD linkages. This arrangement would require a bank to package up listed company shares from other exchanges in the region in the form of a DRs, which could be called Kenyan Depositary Receipts (KDRs). These receipts could then be listed and traded on the NSE, without having to make complex arrangements for moving stock between regional CSDs (as the whole East African Depositary Receipt (EADR) issue would be held at CDSC).

- **4.1.24. - Create KDRs as a potential alternative to creating CSD linkages.**

The promotion of incorporation of early stage companies via the GEMS market. As mentioned above, globally, private wealth creation comes largely from financial assets. Equity listings provide a way for original owners to both obtain risk financing and to realise value from building a business. They also allow for investors to benefit in the growth of the company. It is, therefore, important that entrepreneurs have a clear path from startup, through initial angel and venture capital funding and through to listing on the main board of the NSE. The introduction of GEMS means that companies can be engaged with much earlier in their development and provided with another route for obtaining necessary risk capital.

NSE and its members should actively promote GEMS as the first listing destination for these younger companies. They should engage with companies very early in their development and assist these companies to structure themselves in ways that ease their path onto GEMS (e.g. ensuring an understanding of the importance of corporate governance and accounting standards). These GEMS listed companies will be encouraged to eventually migrate onto the main board as they mature and evolve into national and regional champions of scale.

- 4.1.25. - **NSE to more actively promote benefits of GEMS listing**

Box 1: Depositary Receipts

Depositary Receipts (DRs) are a means for investors to hold and trade foreign securities as if they were local securities. A DR is an instrument issued in one country representing an interest in an underlying security issued in another country. The underlying securities are held by a Depositary Bank, which is responsible for creating and issuing the DRs and for passing through any entitlements, such as dividends, to the holders of the DRs. The Depositary Bank either creates or cancels DRs as securities are moved into or out of this form.

If DRs are used simply as a mechanism for holding foreign securities, then the issuer need not be involved in setting up the DR programme. These are termed Unsponsored DRs and currently exist in the US Markets only (though there are multiple other markets currently looking at introducing the product). If the intention is to list the DRs for trading on a local exchange and/or use DRs to raise Capital internationally, then the Issuer needs to be involved as it is the Issuer that would effect the listing and create any potential prospectus (in the event of an International Capital Raising).

The best established DR market is for American Depositary Receipts (ADRs). These are widely used by US investors as a means of holding international shares in their domestic custody account without the cost and complexity of having to establish custody arrangements in multiple countries. ADRs are commonly used for holding shares, even when the trading takes place on the home market. The most common form of DR is the Level I ADR, which is an Over-The-Counter (OTC) traded DR. The Company is frequently involved but as there is no listing, there is no cost to the Company for this product, either financial or regulatory. Companies that have a Level I ADR include names as diverse as MTN, Shoprite, Heineken, SAB Miller, Burberry and Lafarge.

DRs have also been used by developing markets as a means both of raising capital and familiarising international investors with local companies. This typically takes the form of a Global Depositary Receipt (GDR) programme. Companies that have used GDRs in Africa to raise capital include a number of Nigerian banks (GT Bank, Access Bank, UBA, Diamond Bank and First Bank) and a number of Egyptian issuers, including Orascom Telecom, Orascom Construction and Telekom Egypt.

There are several ways in which DRs could contribute to the Capital Markets Master Plan:

- Develop GDR programmes for leading Kenyan companies, with secondary listings on an international exchange, most likely the London Stock Exchange. These would raise the international profile of these companies. Although, in the short term some trading liquidity could be diverted from the local to the international market, experience suggests that in the longer term the net result is an increase in liquidity in the domestic market, which is seen as the natural home for liquidity. This is the route that has been taken by many (over 33) primarily emerging market companies, most notably, in terms of number of DRs, India, Russia, Egypt and Taiwan.
- Develop GDR programmes for major domestic debt issues. Although DRs have traditionally been issued on equities, DRs on debt have recently been launched and are commonly referred to as GDNs. As with equities, these would make Kenyan debt issues more easily accessible to a range of international investors. The structure would be somewhat similar to the Eurobond, with the critical difference being that the debt would be denominated in local currency (as with equity DRs) removing currency risk from the Issuer. An international tranche could be considered from a local debt issue.
- Develop Kenyan Depositary Receipt (KDR) programmes for international companies that have an involvement in the Kenyan economy, together with a secondary listing on the NSE. These would bring additional trading instruments to the local market and give Kenyan savers opportunities for international diversification within the local market.
- Develop KDR programmes for companies from EAC countries. Launching KDRs for companies from neighbouring countries could provide a short-cut to developing a regional market, ahead of the implementation of the full technical solution linking regional stock exchanges

4.2. Develop SPOT AND Derivatives Markets

Kenya's financial markets have reached the level of sophistication from which it can move to the next stage with the introduction of derivative markets (both financial and commodity derivatives).

A financial derivatives market will be able to support some of the actions presented above (e.g.: helping primary dealers in the bond market better able to manage their risks), aid wider risk management for the whole economy and improve portfolio returns for institutional investors. This could be achieved by products such as foreign exchange, interest rate and equity based derivatives.

Kenya can develop active agricultural and minerals derivative products but, first, Kenya needs to improve the spot markets for agricultural products which would improve prices for farmers and improve food security. Within the lifetime of this Master Plan there may also be opportunities to create markets (both spot and derivative) in the products of mining and in power.

The actions are as follows:

Develop a financial derivatives market. The most obvious opportunity is for the market to trade and clear interest rate, foreign exchange and equity based derivatives (futures and options). However, such a market and its supporting clearing infrastructure needs to be built and operated to be compliant with the most recent international recommendations and best practice and regulated by a regulator that has the necessary legal underpinnings, rules, and regulations to effectively regulate such a market. The regulator will also need to have in place the necessary staff with appropriate skills to effectively monitor such a market and clearing arrangements:

- 4.2.1. - **CMA to improve rules and regulations relating to financial derivatives markets.** Work has already begun in this area but pending regulations must be benchmarked to international best practice.

- 4.2.2. - **CMA to ensure all exchange traded derivatives markets and their clearing arrangements come under its effective remit.**

- 4.2.3. - **CMA to assess and where appropriate license a suitable provider of a financial futures market which seeks to start operating and up-skill as necessary to provide effective supervision.**

- 4.2.4. – **CMA to work with the National Treasury to develop a supportive tax framework for the development of the derivatives market**

- 4.2.5.- **CMA and industry to educate traders and investors on derivatives trading.**
  Identify products where Kenya has the opportunity to be an international price formation centre (as palm oil is in Malaysia). Coffee and tea, where Kenya is a globally important producer are obvious candidates.

- 4.2.6. - **Undertake study of where Kenya has such an opportunity to be the international price formation centre (e.g. Coffee could be a candidate).**
  Warehouse receipt system (WRS) and spot commodities exchange for agricultural products and metals. The commodities markets in Kenya presently consist of the Mombasa Tea Auction and the Nairobi Coffee Exchange. These markets, however, operate as private clubs and information on the market prices achieved do not reach farmers on account of the opaque marketing systems that characterise both markets. There is clearly a need for more open, efficient and adequately regulated commodities markets covering a wider range of products.

  The development of a WRS, combined with an organised market in which to trade them can provide huge benefits, including mobilising credit for agriculture, smoothing market prices, improving food security, and improving the market power of small producers.

The required infrastructure (warehousing and market place) can be provided by Government, donors, private initiatives or a combination of these. Most important at this stage is to provide a facilitating environment.

These spot markets, which would provide accurate price signals, are also essential for the development of associated commodity derivative markets (see below), which add important opportunities to producers and consumers to hedge their exposure to often volatile prices.

- 4.2.7. - **Promote WRS schemes across the country.** This is a continuation of the work that the Ministry of Agriculture has already begun.

  Trading of warehouse receipts, which are financial instruments, needs quality regulation, just like any other market. The CMA is best placed to become this regulator due to the skills it has and its experience in regulating other markets.

- 4.2.8. - **CMA to be appointed regulator for spot commodity markets.**

- 4.2.9. - **Provide necessary rules and regulations to allow for the development of spot commodity exchanges.**
  Trading of electricity when market is liberalized: This is a longer term objective dependent on there being multiple suppliers of electricity in the country (which is, in itself, an objective of the Ministry of Energy). Once there are multiple electricity suppliers, an open spot market can result in a better price discovery mechanism and more attractive pricing. However, such markets need to be adequately regulated to ensure that there is real competition between suppliers and the cheapest priced electricity is provided to consumers.

- 4.2.10. - **Develop pool or spot market arrangements for power.**

- 4.2.11. - **Determine regulations for spot power trading arrangements.**
  Commodity derivatives exchange for the above. As the spot markets mentioned above (and others) develop and become liquid, a demand may arise to trade derivatives on certain of these products. Producers, shippers and end users of some or all of these commodities will want to use these products to hedge and speculators will be attracted and can offer the necessary risk transfer.

  A derivatives market can only develop successfully if there is real end-user demand for its products for hedging purposes. Many derivative markets fail as they are set up to appeal more to speculators and there is no local trading in the underlying physical products. The success of the South African maize futures contracts is testament to this. South Africa is a major producer of maize and the derivative products are used by farmers, trading houses and end users. Its success could not have come about without there being a real underlying physical market supported by a robust WRS. Therefore, care should be taken to only issue licenses for new commodity derivative exchanges that have a clear rationale for their existence, based on real world demand for the products they propose to offer.

  Section 5 below includes actions to create the necessary regulatory environment for any commodity derivative exchanges that may develop.

5. INTERNATIONAL STANDARD FINANCIAL MARKET INFRASTRUCTURE

5.1. Enhance Depository and Settlement Infrastructure

A central securities depository (CSD) is a key part of the financial market infrastructure, as it:

- Provides a secure central record of the ownership of securities;
- Enables the owners of securities to enjoy the benefits of ownership, such as voting and income rights (may be undertaken in conjunction with company registrars); and
- Provides the means for the secure transfer of ownership of securities either against or free of payment.

Important qualities of the CSD are that it should be:

- Secure - meaning that the owners of securities have confidence in it; and
- Efficient - meaning that it does not add unnecessary costs to the ownership and trading of securities and that it also enables other institutions to realise efficiencies.

In addition, and as Kenya is aiming to attract international investors to its markets, it is important that the CSD makes it possible for international participants to participate and should be operated to international best practice standards.

At present there are two CSDs in Kenya: the CBK acts as the CSD for Government Bonds and a private sector company, CDSC, acts as the CSD for equities and corporate bonds. CDSC has recently completed the process of dematerialising securities held in its system. However, international investors have commented critically on requirements in both CSDs that do not fit comfortably with international practice, mainly relating to the need to pre-position securities or funds, pre-notify purchases or obtain prior approval for transfers. The market assessment report identified a number of concerns about the ability of CDSC to support the ambitions of the market, given its current systems. CDSC is in the process of modernising its systems, even though its financial resources are tight. Its fee structure is set by the CMA and it is unlikely to have access to additional capital from its shareholders.

Proposals

Arguments can be made for maintaining separate CSDs, as it is now, or for integrating them. The arguments for separate CSDs focuses on the different needs of the Government bond and equities & corporate bond markets, which may be better met by separate entities, and the cost and disruption of change. The arguments for integration focus on the greater economies of scale in a single organisation and the opportunities for efficiencies for users in maintaining only a single interface and a single pool of liquidity. A single CSD would simplify linkages with CSDs in other EAC markets. Although both models can be found around the world, the recent trend, particularly in Europe, has been to integrate CSDs to create a single institution per country.

Weighing these considerations, the objective envisioned for the full implementation of the Master Plan is to **work towards a single integrated CSD in Kenya covering the full spectrum of securities -** Government bonds, corporate bonds, equities and potentially other instruments that may be introduced in future, such as short-term money market instruments. This should be achieved by transferring Government securities into CDSC. However, integration should be conditional on both CSDs being strengthened to enhance user confidence, which in this context would include the National Treasury as issuer and CBK as manager of Government debt.

The CMMP therefore puts forward a series of steps to strengthen CDSC, which would culminate in the transfer of Government securities to achieve the goal of a single integrated CSD.

Restructure CDSC shareholders and sources of finance

CDSC needs to consider incorporating additional shareholders with a shared vision, who will be not only a source investment funds but also strategic direction. Different models can be found around the world, but the two most common are ownership by a stock exchange and ownership by users.

Ownership by a stock exchange can achieve a close link between trading and post-trading strategies and the exchange can be a source of investment, technical support and strategic direction. The disadvantage of this structure is that it may divert attention and resources from activities that may be important overall, but are not critical to the exchange. Ownership by one exchange is also likely to be an obstacle to the CSD developing services for other competing trading platforms, either locally or across the region. The alternative shareholding structure that is commonly found is ownership by a group of shareholders that reflects usage of the CSD. Provided that ownership is well balanced and that governance reflects ownership, this structure could ensure that the CSD serves the needs of the market overall. The risk is that, if there are deep divisions between market users, these may impact decision-making at the CSD.

On balance, the user ownership structure appears better suited to the Kenyan context, given the objective of integrating the settlement of Government securities in CDSC, the opportunities for regional linkages and the long term objective of keeping open the possibility of competition among trading facilities.

Currently, the shareholders of CDSC consist of:

- 50% - Capital Markets Challenge Fund (a consortium of nine companies: banks, insurance companies and others)
- 20% - Nairobi Stock Exchange
- 18% - AKS Nominees (representing a group of stockbroking firms)
- 7% - CMA Investment Compensation Fund
- 2.5% each - Uganda and Dar es Salaam stock exchanges.

Some significant users of CDSC are not current shareholders, while on the other hand there is an apparent conflict in CMA indirectly having a shareholding in an entity it is responsible for supervising. Corporate governance is likely to be improved if all the brokers and custodian banks that act as depository agents were to become direct shareholders, rather than being represented indirectly through other companies. The NSE and other regional stock exchanges should be able to retain their shareholdings if they wish.

It should be possible for the CBK and company registrars to become shareholders if they wish, reflecting their interest in the operation of the system. Current shareholders which are not market users, such as the CMA Investor Compensation Fund, should be bought out.

Following the restructuring of shareholders, board composition should be restructured to reflect usage, ensuring that the main groups of users - brokers, custodians, registrars and the CBK - are represented, alongside a number of independent non-executive directors representing the public interest.
Actions are:

- **5.1.1. - CDSC to consider expanding existing scope of shareholders to include key users of its facilities.**

- **5.1.2. - CDSC Board composition should be restructured to reflect usage and public interest.**
  Restructuring should be an opportunity to raise capital to fund projects to modernise systems, but should also provide an opportunity to change the way in which CDSC funds its activities. With a board of directors answerable to a shareholder base that reflects usage of the system, it should be possible for the board to take responsibility for setting the fee structure for CDSC. Modernising and maintaining its systems will be in the interests of its shareholders, who are also its users and have an incentive to pay for these investments. The board would be best placed to determine whether investments should be paid for by retaining profits to create an investment reserve or by making occasional calls for additional capital.

  As a result, at this point, the requirement for the CDSC fee structure to be approved by regulators should be removed at this point. Its schedule of fees should then be standardised and publicly available. Although there is unlikely to be competitive pressure on CDSC, as its business is in practice a "natural monopoly" (see section 9.3), the user governance and threat of referral to the Competition Authority will act as deterrents against abuse of this fee-setting power.

The action is for:

- **5.1.3. - CDSC to set its own financial policy subject to appropriate competition and consumer protection controls.**

Modernisation of services

CDSC should strive to operate to best international standards, which means **providing full delivery versus payment (DVP) settlement in real time in central bank money.**

Full DVP means that the transfer of securities and the payment are made simultaneously and that, once made, there is no possibility for either the transfer or the payment to be unwound in any circumstances. Real-time settlement means that it can take place within a very short time - usually a few minutes - at any time during the day. This is essential for time-critical intraday activities, such as central bank liquidity operations or inter-bank collateral movements.

Finally, the requirement for payment in central bank money means that the movement of cash between participants in the CSD takes place across the books of the CBK, so that the seller of securities is not exposed to credit risk on a commercial bank for the cash it receives. In the current arrangements, the buyer makes payment to a commercial bank that acts as settlement bank for CDSC, which holds the cash until it is disbursed to the seller.

This creates a risk, albeit only temporary, that the settlement bank could fail while it is holding the settlement proceeds, leaving buyers or sellers exposed to losses. This risk can be removed if the payments pass through accounts at the CBK. This is desirable in its own right as a risk-reduction measure, as well as being a necessary precondition for integrating Government bond settlement. However, it requires a sophisticated link to be in place between CDSC and the CBK to synchronise the movement of securities and the movement of cash.

Moving to full DVP settlement in central bank money will reduce some of the risks inherent in the current structure that uses commercial banks as settlement banks. This presents an opportunity to **review CDSC's approach to risk management.** CDSC should conduct an overall **review of its risk exposures and risk mitigation measures** to ensure that all potential risks are covered with resources that are proportionate to the size of risk In the longer run, **introduction of central counterparty clearing** should be considered for cash securities transactions as the most effective means of eliminating counterparty credit risk between trade and settlement (see the following section).

In common with many CSDs in developing markets, CDSC, CBK and NSE should seek to ensure good performance by having various requirements "hard-wired" into their systems. Examples include the requirement that securities must be present in an account before a sell order may be placed, to ensure that the seller will be able to settle on the due date, and that free-of-payment transfers, with no change of beneficial owner, require advance approval. While these requirements may seem necessary for unsophisticated investors, they are an obstacle for more sophisticated international investors who are accustomed to managing their positions in different ways to ensure settlement.

In order to be open to international investors, therefore, CDSC should move from imposing pre-settlement operational requirements to concentrate on monitoring desired outcomes with subsequent disciplinary action if necessary. For example, CDSC should remove the requirement to pre-fund accounts in order to ensure settlement on the due date. It should instead achieve self-regulatory organisation (SRO) status in order to monitor the settlement performance of participating firms and if necessary take disciplinary action against firms that persistently fail to settle on time. This would leave more flexibility for firms in how they meet the target without lowering standards. Individual firms would still be free to require clients to pre-fund accounts with securities or cash before trading, but this would be a decision based on the relationship between the firm and its clients.

Another area of difficulty for international investors is **flexibility in the types of account structure available.** It should be possible to operate omnibus accounts, segregated accounts (in the name of the intermediary) or managed accounts (in the name of the end-investor but managed by the intermediary) according to the risk profile of the end-investor. Although CDSC is able to operate omnibus accounts, they may cause difficulties at the trading level when different underlying investors in the same omnibus account are buying and selling at the same time.

CDSC should modernise its systems to enable straight-through-processing using international standard messages (ISO15022 or later). This reduces costs and errors, enables faster processing and increases the market's openness to international participants; and develops a central corporate actions service, providing both registrars and investors with a single gateway for the distribution of income and making elections on optional corporate actions.

Finally, CDSC should set itself the objective of full compliance with the CPSS-IOSCO Principles for Financial Market Infrastructures and undertake regular monitoring to ensure this is achieved and maintained.

At the conclusion of this programme of change, we believe it should be possible to integrate the settlement of Government bonds with other corporate securities in the CDSC.

CDSC also needs to support the initiatives set out in section 4.1.

Depositories often support stock borrowing and lending in a variety of ways:

- As it is the central holder of securities accounts, it can locate the holders of securities that need to be borrowed and who are potentially willing to lend them. In some markets, depositories provide automated services to match borrowers and lenders, for which they charge a fee.
- Depositories can support stock lending by providing services which may include some or all of recording open loans, revaluing stock on loan, passing collateral, automatically returning borrowed securities when they are no longer needed and ensuring that benefits, such as dividends, are passed from the borrower to the lender.

If there is demand from international or regional companies to issue local depositary receipts ("KDRs"), they will be issued into CDSC for holding and settlement.

Actions are:

- 5.1.4. - **CDSC to modernise its systems** to provide full real-time DVP in central bank money and straight-through-processing (STP) using international message standards.

- 5.1.5. - **CDSC to review its risk management approach.**

- 5.1.6. - **CDSC to achieve SRO status and move to an outcome-based approach** to ensure good settlement performance.

- 5.1.7.- **CDSC to achieve full compliance with the CPSS-IOSCO Principles for Financial Market Infrastructures.**

- 5.1.8. - **Integrate Government bond and corporate securities in CDSC,** once the previous steps have been completed.

- 5.1.9. - **CDSC to develop services to support the introduction of Stock Lending.**

- 5.1.10. - **CDSC to ensure that there are no barriers to local DRs being issued.**

Longer-term developments

Looking further ahead, the post-trade infrastructure for securities markets will need to continue to evolve in line with the development of the trading market.

There is already a plan to link EAC stock exchanges for trading and CSDs for settlement.

- 5.1.11. - **CDSC to develop links with other EAC depositories** in order to support regional trading initiatives.

As trading volumes develop, it will be necessary to review whether a Central Counterparty (CCP) should be introduced to support the cash securities markets. The advantages of a CCP are that:

- It manages counterparty risk between trade and settlement in a way that responds quickly to changes in the risk positions of participants;
- By netting transactions, it can reduce the operational risk of having to manage large numbers of transactions and in particular can make a market resilient to sudden peaks in volumes; and,
- If the CCP is able to borrow stock, it can reduce the incidence of fails.

Therefore, in the longer term:

- 5.1.12. - **A central counterparty for cash securities should be considered.**
Many investors in fixed income markets expect to hold their assets in one of the two International CSDs - Euroclear or Clearstream (known as "ICSDs"). Making Kenyan fixed income securities "Euroclearable", therefore, is another contribution to their international accessibility (see Box 2 below for discussion of what this term means).

The two ICSDs set more demanding standards than global custodians for the markets they will connect to. The initial driver is investor demand, as they seek to provide the services their customers need. However, they also need to be assured that they will be able to provide services to the standards they expect. The ICSDs therefore expect to be able to connect through a local custodian using international message standards; to be able to use an omnibus account, so that they can make transfers between their own participants, and to make same-day transfers into or out of the local CSD; have access to local currency liquidity and to be able to convert the local currency outside the country. As a result, they each connect to around 50 markets. South Africa is currently the only market in Africa where Euroclear and Clearstream offer settlement.

The main preconditions for the ICSDs to offer Kenyan domestic bonds in their systems are for CDSC to complete the programme of modernisation set out above and for international investor demand to rise to a level that justifies the investment. Although, the ICSDs generally connect to markets using a local custodian, Malaysia is unusual among emerging markets in that its CSD has a direct bilateral connection with Euroclear. In the long run, Kenya should also aim for a direct bilateral relationship with one of the ICSDs, in which the ICSD opens an account with CDSC and CDSC opens an account in the in the ICSD. Achieving this, however, will require CDSC to be able to open an account for an entity established outside Kenya and provide the full range of services normally provided by a custodian bank, as well as having the capacity to open and manage an account outside Kenya.

- 5.1.13. - **CDSC should aim to build bilateral connections with Euroclear and Clearstream.**

Box 2: What does "Euroclearable" mean?

Individual securities or markets are sometimes described as "Euroclearable", often with the implication that this carries some kind of "seal of approval". However, other than the general meaning of "capable of being settled in Euroclear", the term does not have a precise definition and in practice may be used to mean different things. The following are some of the ways in which the term may be used.

- Eurobonds are issued directly into the two ICSDs and can only be held and settled in the two ICSDs or in other CSDs that have a link to one of the ICSDs. They are by definition "Euroclearable". This will be the case for any eurobonds issued by Kenya.
- The ICSDs also develop links to domestic markets where there is demand from their clients and where they can operate in line with their normal procedures. Not all markets meet these criteria: Euroclear has links to 45 markets and Clearstream has links to 52.

However, the services available in the ICSDs for securities issued in domestic markets vary by market or in some cases by type of security.

- In some cases (for example, Brazil) it is possible to hold securities in the ICSDs and make deliveries to and from the domestic market, but not between accounts in the ICSD, as the ICSD cannot operate an omnibus account. Not everyone regards such markets as fully "Euroclearable".
- In other cases, (like in Mexico) it is possible to make deliveries to and from accounts in the domestic market and between accounts in the same ICSD, but not across the "Bridge" between Euroclear and Clearstream. These markets would generally be considered "Euroclearable".
- Finally, the fullest form of acceptance is when it is possible to make deliveries to and from the domestic markets and between accounts in the same ICSD and across the bridge to the other ICSD. An example is South Africa.

This package of changes - restructuring of ownership, financial autonomy, modernisation of services, moving to outcome-based monitoring and a new regulatory framework - should create the conditions necessary for integrating Government bonds into CDSC. They can also position CDSC as the CSD in Sub-Saharan Africa most open to international participation after South Africa. Combined with regional linkages (see section 3), it would be well-placed to act as a regional entry point for international investors. While some of the objectives, such as supporting competing trading platforms or facilitating intra-day collateral movements, may seem far removed from the current operation of the market, these are likely to become requirements within the ten-year horizon of the Master Plan and should be incorporated from the outset.

5.2. Develop Clearing House Infrastructure

Derivatives markets - whether traded on an exchange or in the OTC market - require robust infrastructure to provide a secure and efficient platform to manage risks and ensure efficiency. The requirements are different from those of the cash securities markets: whereas in securities markets the time between trading and settlement, when the two parties, are exposed to each other is typically measured in days, in derivative markets it may be measured in weeks or months. The key is a CCP clearing house.

Requirements for a CCP

CCPs exist to reduce the various risks that exist in the markets they serve:

- Risk of post-trade disagreement on the terms of a trade (particularly for OTC trades);
- Counterparty risk - that one party to a trade defaults and the trade can only be replaced at a less favourable price;
- Operational risk of having to manage a large number of trades;
- Risk of loss in the default process, if the administrator/liquidator of the defaulter challenges the right of the CCP to offset positions or to use collateral to close out positions;

- Risk of delivery failure when a contract goes to physical delivery; and,
- Risk to clients' assets when an intermediary defaults.

To address these risks, a CCP needs:

- A legal framework that makes it possible for the bilateral contract between buyer and seller to be replaced by two contracts, one between buyer and CCP and one between CCP and seller, a process known as 'novation';
- A legal framework that ensures that the default arrangements of the CCP cannot be challenged by an administrator/liquidator;
- A legal framework that makes it possible to segregate and protect client assets;
- The expertise to develop and maintain a risk model, which needs to take into account not just the probability of price movements in a single contract but also the correlation between movements in the prices of related assets as well as the level of risk that the CCP is prepared to accept;
- The technical infrastructure for receiving, if necessary matching, and netting trades;
- The technical systems for applying the CCP's risk model to firms' portfolios to calculate the collateral required;
- The availability of assets it is prepared to accept as collateral (cash, securities, bank guarantees and, in some cases, precious metals) and price data in order to value them;
- The technical infrastructure and institutional relationships (with payment banks, custodians, depositories, etc.) for collecting, holding and valuing the collateral held; and
- Additional financial resources in the form of capital and/or a guarantee fund against the risk that the collateral posted by a defaulting member is insufficient.

Implementing a robust CCP needs to bring together the establishment of an appropriately staffed and funded institution with the legal infrastructure (see section 7 and 8) and staff development (see section 6) described elsewhere in the Plan. If the legal framework is deficient, then there is a risk that operations carried out by the CCP, for example in netting transactions or managing a default, could be legally challenged by one of its counterparties. If the counterparty was able to "cherry pick" which transactions were netted or closed out, this would undermine the basis on which the CCP had been managing risks and probably leave it with inadequate resources. Another risk is that confidence in the concept of using derivatives cleared through a CCP could be undermined, if some end-users of the market suffered serious losses as a result of reckless behaviour or inexperience. This should be addressed by educating potential users of the market (see action 4.2.4).
In this context the relevant action is to:

- **5.2.1. - Assess the adequacy of the legislative and regulatory framework to support derivatives clearing** as part of the programme outlined in 5.2 and maintain it under regular review.

  Establishment of a CCP

  Banks in Kenya already offer OTC financial derivatives to their business clients to help them manage interest rate or foreign exchange exposures, but the size of the market is not known. A first step will be to undertake a survey of OTC derivative activity in Kenya to understand its size and what products are most frequently traded. The methodology should follow that of the regular Bank for International Settlement surveys of OTC derivatives, so that the Kenyan data could in due course be added to the same survey. When the market reaches a certain critical mass, there are advantages in bringing it into an OTC clearing house, as this helps to standardise contracts as well as putting in place mechanisms for managing and collateralising counterparty credit risk.

  Different models exist for the ownership of CCPs around the world. Most often CCPs for exchange-traded commodity or financial derivatives are owned by or closely associated with the exchanges that define and trade those derivatives. CCPs clearing cash securities, securities derivatives or OTC contracts of various kinds are more likely to be independent of any individual exchange.

  It is difficult at this stage - when derivative exchanges and clearing houses do not yet exist in Kenya - to anticipate what will be the preferred market structure.

If the priority for Kenya is to develop an exchange trading commodity derivatives, then it is most likely that the exchange will develop and own a CCP as part of its market development. However, it is important that the CCP should be a separate legal entity from the exchange to insulate it from contagion of risks from the exchange. It is also desirable that the governance of the CCP is given a degree of independence to ensure that the commercial objectives of the exchange do not over-ride the risk-driven judgments required of a CCP. There should also be a requirement that the CCP should provide access to clearing for trades not originating on its parent exchange in order to support the development of a broad-based market. This would be consistent with the objective of an innovative, open and competitive market (see section 9).

However, if competing markets develop or there is a need for clearing trades transacted in OTC markets, then it would be important to consider alternative structures, such as an independent CCP that can clear trades from multiple trading platforms as well as the OTC market or separate specialist CCPs for different markets. Each model has its pros and cons. A single CCP clearing multiple asset classes can offer efficiencies to clearing firms that are active across all the asset classes, as they need only one connection and can concentrate their collateral in a single CCP. However, there may be a greater risk of contagion between different assets and it can be difficult to accommodate other firms that are active in only a small number of asset classes. On the other hand, although separate CSDs offer the advantage of each specialising in its own field, it results in duplication of infrastructure and requires clearing firms to split collateral across different entities.

The relevant Implementation Working Group formed under the Implementation Committee for this action should monitor the development of the market and make recommendations in the light of experience. The actions relevant for this Group are:

- 5.2.2. - **Survey the size of the existing OTC derivatives market in Kenya.**
- 5.2.3. - **Establish a CCP for commodity derivative products** (agricultural, energy, power, metals) alongside the development of a commodity market.
- 5.2.4. - **Review the derivatives market structure** to determine the most appropriate structure for CCPs.
- 5.2.5. -**Introduce a CCP for financial derivatives,** when there is sufficient activity in the OTC market to justify it, either based on the commodities CCP or as a separate institution, depending on the recommendation of the review.
- 5.2.6. - **All CCPs should carry out regular reviews to ensure compliance with CPSS-IOSCO principles.**

6. INSTITUTIONAL AND CAPACITY BUILDING INITIATIVES

The role of human capital is pivotal to the development of a world-class capital market in Kenya. Access to a deep pool of highly skilled and trained human resources will enhance the capacity of the entire financial sector and is critical for the development of specific sub-sectors like capital markets.

This pool of finance professionals will also support the growth of an international financial centre based in Nairobi through providing ample supply of skilled capacity for the centre. Creating a deep pool of finance professionals in the country will have a virtuous effect in attracting companies to the international financial centre. Specifically, these companies will benefit from having access to qualified and knowledgeable professionals in finance, economics, law, accounting, audit and a range of other specialist skills necessary to establishing local and regional operations in the financial centre.
Lastly from a development perspective, as Kenya becomes a gateway for financial services into Middle Africa and as foreign investment into the country increases, there will be a growing need to ensure finance professionals are sufficiently competent and qualified so that the Kenyan capital market can compete effectively in an increasingly open environment.

In view of these needs, it is important for all relevant stakeholders within the capital market to increase their efforts in training, development, certification, and to generally upgrade the skills of their staff so as to provide the necessary human capital to support the growth of the market and the creation of an international financial centre. The Master Plan will play a role in supporting these efforts and in developing talent and improving the level of professional certification in the capital market.

6.1. Develop and Retain Professional Talent

For the financial sector to operate in line with international standards and for the capital markets to accommodate the expected growth and international interest that is envisioned under this Master Plan, there needs to be a deep pool of qualified and trained staff in the market, which will also support the work of the regulators.

The theoretical underpinnings of the financial services sector already form part of finance curricula at universities across the country. In Kenya, as in most emerging markets, it is far less common for undergraduate and postgraduate law curricula to include courses relevant to the financial services sector and to capital markets in particular. What this means in practice is that there is a scarcity of homegrown legal practitioners skilled in the operation of capital markets at the level of financial products or market infrastructure as well as the requisite primary and secondary legislative frameworks for the operation of the market. Since these skills will become increasingly important as Kenya seeks to develop its financial markets, the CMA will approach universities based across the country and recommend that law curricula be expanded to include courses relevant to financial services and to capital market products, infrastructure and law in particular. The relevant action to develop these skills is therefore to:

- 6.1.1. - **Include education on financial services in university law courses**.

  In terms of broader professional capacity building, there have been attempts to provide a single capital markets certification for the country and for the East African region more broadly. These efforts were driven by the Securities Industry Training Institute (SITI), an organisation established in 2009 with support from the IFC to manage and deliver a wide range of training programs on capital markets and investments, corporate finance, asset management, entrepreneurship, corporate governance, and related fields of study.

  Though this organisation has been successful in training over 1,200 market participants across East Africa as at end of 2012, the certification process for participants who have attended the training proved problematic in the absence of recognition from domestic regulators and from relevant examination bodies of the training curriculum. The institution also struggled to be sustainable and to generate revenue from the provision of its training services.

  Efforts are currently underway to realise the potential of SITI by implementing a five-year Strategic Plan for the organisation. The hope had been that this strategic plan would put in place mechanisms that ensure the financial sustainability of the institution as well as achieve recognition from the market as to the examination and certification process. At the same time, there are other training and examination bodies that operate internationally that could be considered as providers of services in Kenya. In addition, consideration will be given by the CMA to examining the options for establishing a licensing framework for capital market participants that is supported by stakeholders in the market. The resulting action is thus for the CMA to:

- 6.1.2. - **Assess options for training, examination and certification.**

III. THE LEGAL AND REGULATORY ENVIRONMENT

For the capital markets to flourish as the Master Plan envisages, the legal and regulatory environment need to be strengthened and streamlined so as to accommodate the requirements placed upon it.

The regulator itself also requires to be fully equipped to perform its role. The arrangements for corporate governance and financial reporting need to be upgraded and rendered fully effective, and the environment needs to be innovative, open and competitive. This section of the Master Plan sets out actions to achieve these outcomes.

7. SOUND, RESPONSIVE, LEGAL, AND REGULATORY FRAMEWORK THAT INSPIRE CONFIDENCE

7.1. Strengthen and Streamline Financial Regulation

Coherence in regulation: the case for integration

Financial regulators internationally have three main overarching objectives built on the fundamental tenets underlying the international Core Principles set by the international financial regulatory standard setters. These include; the promotion of stability, the protection of investors, depositors or policyholders, and the preservation of orderly markets. These principles, and especially the promotion of stability, rightly apply across all the different sectoral disciplines of financial regulation because of the seamless linkages between all parts of the financial system.

The capital markets form an integrated whole together with the banking system, the insurance companies, the retirement funds and other financial intermediaries; most financial institutions hold capital market instruments of one form or another, and the capital markets are in turn reliant on the smooth functioning of the other parts of the financial system, and especially the banking and payments systems. Most financial institutions are therefore subject to one or more of the regulatory disciplines. The logic of the interdependence of different categories of financial business and hence of the need for integration of their respective regulatory arrangements has already been accepted by the Presidential Task Force on Parastatal Reforms.

Integrated financial regulation

In very many countries, the logic of the interdependencies between the sectoral branches of regulation has led to the formal integration of both regulatory bodies and the related legislation. Most successful international financial centres globally have already adopted a form of integrated regulation in which different categories of business are grouped together under the same regulator.

International financial market players considering participation in the Kenyan market place will likely expect to see a similar kind of integrated approach to financial regulation across all financial market products because of the coherence in regulatory approach that brings and its relative efficiency in dealing with the regulated community. Very many financial centres have chosen full integration of securities, banking and insurance, especially when they have been particularly concerned about attracting international interest. These include; Singapore, Switzerland, Ireland, Gulf countries, and Luxembourg.

The main alternative model, which has been named Twin Peaks, separates prudential and conduct of business regulation across the board, so that many firms will have two supervisors, one for prudential requirements and a different one to regulate their conduct.

While Twin Peaks can and has been successful in some countries such as Australia and has advantages in terms of providing focus for an organisation, it can have disadvantages for those firms which are subject two separate regulators because it institutionalises rather than internalises a potential conflict between the demands of consumer protection and financial stability. In the Netherlands, which runs a strict Twin Peaks regime, conflicts between the regulators in handling fitness and probity issues led to considerable market concern.

While in the United Kingdom, which has recently adopted a mix of Twin Peaks and sectoral regulation, which depends on the size of firm, tensions are already building up. An example can be found in the form of the pressure of the prudential regulator for increased capital in insurance companies because of the consequences of lower investment returns relative to likely payouts and of the conduct regulator to reimburse policyholders on a substantial scale. Separation of functions removes the mechanism to resolve these conflicting requirements.

Very few fully integrated regulators have chosen to split up, while the limited trend towards forms of Twin Peaks in Europe is partly driven by non-regulatory considerations or is in countries where capital market activities are very modest with little international interest. In the context of the development of the Master Plan it is arguable that, over the medium term, the full potential development of the capital markets is likely to be served best by full integration of all the regulatory disciplines and not by the less common Twin Peaks model.

There is also an issue internationally about whether there should be a separate legal and regulatory regime for international firms or for international business. Few countries have eventually chosen to have an international centre carved out separately in legal and regulatory terms from the domestic market. There are those that have not been particularly successful, for example, the Gulf states.

The international centres tend to have been created where there is no interest in developing a domestic market or where the domestic market arrangements are judged to be sufficiently inadequate beyond repair or reform. The label "IFC" tends rather to relate to carved out tax, property, or marketing benefits, but is often limited to such advantages. For instance, the Dublin International Financial Services Centre operates under identical legal and regulatory arrangements to the domestic market. Indeed, it has to in order to retain access to the EU Single Market, which is critical for foreign non-EU participants. Similar issues could arise in relation to the position of Kenya within a more developed EAC single market in financial services. There is, therefore a weak case for putting in place a separate regulatory or legal regime of international business in Kenya because the international business which the country hopes to attract will expect to have full access to the domestic market on the same basis as domestic players. Indeed one of the main purposes in making Kenya more attractive internationally is to bring external capital into the domestic market. It is unlikely that there will be much international interest otherwise.

There is also a discussion internationally as to whether a fully integrated regulator should be inside or outside the central bank. Internationally there is support for both kind of models. Japan, Germany, Luxembourg and other countries have placed the wholly integrated regulator outside the central bank while Singapore and Ireland have it inside. It is difficult to claim that one model is clearly superior to another. Factors which are often taken into account, particularly in emerging markets, are the capacity of the integrated regulator to be sufficiently independent of political pressure and to finance itself adequately. Both these factors will be issues in the eyes of foreign market participants when looking at the strength of the supervisory regime.

The approach currently advocated in Kenya, leaving banking supervision separate within the CBK, but integrating both the prudential and conduct of business supervision of all the other regulators in the Financial Services Council, is unusual internationally and does not correspond with either the standard fully integrated or the Twin Peaks model. While the integration steps proposed are welcome in themselves and can be progressed in the near term, they may not be sufficient to address the issues which the Presidential Task Force on Parastatal Reforms identified or deliver the full range of benefits which integration is intended to achieve. They afford neither the rewards of full integration nor the benefits of focus derived from dividing up prudential and conduct of business supervision. Instead they offer a rather eclectic mix of both disciplines. The proposed new arrangements may also be difficult to explain to prospective international participants in the Kenyan markets.

It would be sensible to keep the regulatory integration plans under close review in order to ensure the optimal outcome if the Kenyan markets are to achieve their full potential.

The full integration of all financial regulators would be consistent with the role of the capital markets within a fully integrated financial system; all the different sectors need to play an interrelated yet balanced role in order to deliver maximum transformational benefits for the economy as a whole. Failure to adopt a holistic approach could jeopardise the success of maximising the role of the Kenyan capital markets in an international context.

Regulation exists for a purpose. The structure that is ultimately created must be underpinned by objectives. The international sets of standards established under the auspices of the Financial Stability Board set underlying objectives which, as noted above, are common across the main regulatory disciplines of banking, securities and insurance with customer protection and systemic stability as core objectives for all, and, for securities regulators, ensuring that markets are fair, efficient and transparent. The fact that these objectives are common, simply reflects that financial markets exist as a seamless whole, each interrelated with the real economy in their different but overlapping ways. The capital markets form a key element in this seamless structure which must be regulated and supervised in a coherent and consistent manner across the board.

- **7.1.1. - CMA to support progression to full integrated financial regulation** as this will maximise the benefits of the Capital Markets Master Plan, both for the transformation of the domestic economy and for the attraction of international business. Whether this should be inside or outside the central bank should be determined by the extent to which this would assist the integrated regulator to be fully independent and satisfactorily resourced.

Critical success factors for an integrated regulator: what international investors will expect

As noted above, foreign participants in Kenyan markets will look critically at the coherence of the regulatory arrangements and are likely to prefer a fully integrated regulator. However, they will require that the integrated regulator functions to maximum effect. The following are generally regarded as critical success factors for putting in place integrated regulation:

- Secure a governance structure, which ensures that the regulator will not operate in a biased fashion with undue concentration on a particular areas according to the interests/experience of the top management. This can be a risk because international experience suggests that individuals can have a natural tendency to prioritise those areas they are most familiar with, such as focusing on stability at the expense of consumer protection or vice versa.
- Put in place a strong board with cross-sectoral experience, which will oversee a process of allocating resources across the whole organisation in relation to a risk-based assessment without institutional bias. The chair of the board will need to be strong and independent in order to ensure that this happens.

The chief executive officer of the integrated regulator will need to exercise considerable delegation to their immediate deputies because of the range of disciplines which need to be covered and quite often will need to be chosen for their administrative rather than sectoral technical skills.

- Secure an independent funding base for the new regulator. Excessive reliance on Government funding or budgetary control will create concerns about risk of political influence.
- Create new legislation integrating the different existing sectoral legislation; otherwise many of the benefits of integration will be missed. The legislation must treat all sectors consistently with approaches to all prudential and conduct risks.
- Create a structure that provides a one stop shopping for those firms who are active in multiple disciplines
- Relationship managers need to be appointed to coordinate all regulatory interface with a regulated firm.
- Create a unified licensing process so that all relevant information is available to those making licensing decisions and the regulated firms or other market participants are treated consistently.
- Work to create a unified culture of regulation with an appropriate balance between flexibility and proximity to the regulated, and firm and consistent regulation. The regulator needs to play both doctor and policeman and ensure that there is no inconsistency between the requirements placed on a firm for prudential and for conduct of business purposes.
- Create an integrated enforcement function to ensure enforcement actions are progressed with maximum effectiveness, including ensuring that all legal requirements for due process are met.
- Ensure information flows right across the organisation to the people who need to have it in a form which is accessible. Where the integrated regulator is outside the central bank, ensure that there are good two way flows for information about economic developments to reach interested regulators and that supervisory information reaches those responsible for financial stability.
- Put in place adequate liaison arrangements with Government and especially the National Treasury to ensure that Government is aware of potential risks to financial stability and especially to potential calls on the public purse. At the same time ensure that there is clearly understood independence for the regulator to make independent decisions in relation to individual firms and markets without inappropriate political involvement.
- Create a unitary information base for all regulatory information, both statistical and other, so that it is both consistent and readily accessible to those who need to access it.

- Create new human resource policies which can be consistently applied across all staff regardless of their organisation of origin. Although inappropriately generous employment terms should be eliminated as part of this process, this will often involve bringing employment terms up to the level of the most generous.

At this stage in the process of establishing an integrated financial services regulator the above are to be considered principles and not recommendations. However, irrespective of the degree of formal integration, the extent to which these principles are applied through informal arrangements, the more efficiently the markets are likely to operate and the more attractive they will be to both users and participants.

- 7.1.2. - **As steps towards integrated regulation progress CMA will seek to ensure that the outcomes are optimal from the point of view of achievement of the goals of the Master Plan.**

Maintaining financial stability

Whatever arrangements for supervision, and regulation, whether wholly sectoral or integrated in some form, sound connection is required between all the different regulatory disciplines and the macroeconomic and monetary policy decision makers, wherever they are located. For this reason the arrangements for reviewing financial stability matters need to be kept under review, irrespective of any regulatory reorganisation. Although there are existing arrangements for dialogue between all the regulators, these will need to be intensified as a more integrated financial sector develops in line with the Vision 2030 agenda and the conclusions of the Presidential Task Force, as well as the increase in international participation planned for in the NIFC context.

- 7.1.3. - **CMA will play its proper role in ensuring that the arrangements for maintaining financial stability in Kenya as a whole function well at all times.**

Better regulation as the best means to promote market development

As part of the consideration of the best form of the regulatory architecture, consideration should also be given to ensuring that the regulatory objectives are best suited to their purpose. This applies whether the regulatory framework is integrated or not. One of the issues which arises internationally is the extent to which promotional or developmental objectives for a market place should be directly reflected in the objectives of the regulator, in whichever sector, rather than be assigned to other agencies. Although a number of regulators internationally do have promotional or developmental as well as regulatory objectives, the international trend is against them. The current international approach rather aims at putting in place other approaches to trying to ensure a financial centre's competitiveness and capacity for innovation is not unwarrantedly impeded by regulation. Under this model, the promotional and developmental role is assigned to a separate agency without regulatory responsibilities. This also makes it clear that responsibility for innovation and for development of products and markets must lie with market participants themselves. They are the ones who can best identify viable opportunities for new products, if need be in collaboration with other market participants.

The reason for the debate about regulatory mandates at the international level is that the combination of developmental and regulatory objectives within a regulator's mandate may lead to conflicts and tensions which may undermine the effectiveness of rulemaking and fairness in individual regulatory decisions. An improper bias may be introduced in favour of particular providers of financial services against either users or other providers. There has been adverse experience where developmental objectives have distracted the regulator from adequately protecting the consumer or market user.

The emerging international consensus is that a better way of achieving the intention of such a development or promotional objective is if lawmaking/rulemaking/decision remains focused, in the case of a securities regulator, on the core objectives of protecting investors, maintaining orderly markets and supporting financial stability but under the constraints of "better regulation" principles. This will in itself help to improve the attractiveness of markets and their international competitiveness as well as reducing the risk of conflicts of objectives. Such principles would normally be included in the legislative and rulemaking process.

Such principles might be:

- Identify the mischief. The intention is that without prior understanding of what the rule(s) were supposed to address, it is not possible to know what character of a rule to adopt or how much detail the rule needs to provide.
- Identify the market. Detailed rules at the national (or EAC) level should focus on requirements which will open those markets to contestation, assuming that competition policy is not a better tool. Otherwise, changing a market structure without good reason will be a costly exercise without necessarily corresponding benefits for the customers in those markets.
- Choose the right policy tool. At one level this involves deciding which tool is best to address the mischief; whether an issue is best addressed by competition policy, by supervisory activity or by enforcement. At another, it means deciding whether there should be even greater detail in rules about what precisely firms should do or whether the rule might incorporate a set of considerations or principles against which a firm's decision would be assessed by supervisors and overruled if determined to be excessively risky.
- Identify the right kind of rule. Is the best approach one addressed at content, process, outcome or behaviour? Content relates to a specific requirement which must be met, like a capital ratio. Process sets out a set of actions which must be followed over time. Outcome relates to what is achieved, perhaps at a certain level of generality. Behaviour specifies or prohibits the way in which an act must be undertaken. There could also be tests relating to how the rule is to be used; is it to be enforced and if so is it suitable for this purpose; is it just a means to an end rather than the outcome itself; what are the risks of the rule generating unwanted changes in behaviour; and so on.
- No rule should be more detailed than necessary. This is in part to avoid unrealistic implementation challenge, partly to avoid diversion to rule evasion rather than true risk mitigation.
- Innovation in connection with regulated activities should not be impeded where it does not conflict with the regulator's primary responsibilities.

And the **action** is:

- **7.1.4. - CMA to assess whether the intent of its development objective would be better met by its replacement by a set of legislative and regulatory principles, which would ensure that the regulatory burden was the minimum appropriate.**

No-Action arrangements

One of the ways in which innovation can be supported, irrespective of the sector, is by formalisation of a "no-action" approach to proposals for new products or approaches. The case has been advanced for CMA to put in place "no action" arrangements whereby the market can come to the CMA and ask for assurance that some action may proceed without the law specifically allowing it. The CMA can then advise the firm or market that in its view the proposed new product or approach can proceed without breach of law provided it remains strictly within certain specified parameters.

This is similar to an approach used in the USA by the Securities and Exchange Commission (SEC). An individual or entity who is not certain whether a particular product, service, or action would constitute a violation of the US federal securities law may request a "no-action" letter from the SEC. Most no-action letters describe the request, analyse the particular facts and circumstances involved, discuss applicable laws and rules, and, if the staff grants the request for no action, concludes that the SEC staff would not recommend that the Commission take enforcement action against the applicant based on the facts and representations described in the individual's or entity's request. The SEC staff sometimes responds in the form of an interpretive letter to requests for clarifications of certain rules and regulations. The no-action relief is limited to the requester and the specific facts and circumstances set forth in the request. In addition, the SEC staff reserves the right to change the positions reflected in prior "no-action" letters.

For CMA to be able to follow this approach safely, it needs to be clear that CMA has the formal legal right to give such "no-action" opinions in specified circumstances with a clear understanding as to what such opinions signify. For the CMA to give such opinions without legal backing would give rise to the risk that the CMA might incur liability to market users in the event of detriment being suffered and that market users might be misled as to the degree of regulatory protection they enjoy. The CMA needs to be able to act swiftly in the event that the conditions have been breached, either to undertake enforcement actions or to introduce new rules if it becomes clear that the new activity warrants this. The action is:

- **7.1.5. - CMA will examine the case for amending the law formally to put in place "no-action" arrangements.**

Principles-based legislation

The case has been put by market participants for more "Principles-Based" regulation. This term is used in a number of different situations internationally. On one hand, it is used as shorthand for introducing rules which are sufficiently flexible to accommodate a range of circumstances. This is to enable swifter adjustment to changes in the market than can be met if rules have to be formally amended to meet all changes in circumstances. However, if the markets are to remain protected, it is best if a flexible drafting of rules, which carries risks of its own, goes hand in hand with the formalisation of a "no-action" approach as described above. It also has to be possible for legislation and/or rules to be implemented in a timely manner to address emerging risks and accommodate emerging market developments.

On the other hand, it is used as a way of describing a system of principles, which specify expected behaviour or outcomes, without detailed rules being specified as to how the regulatory outcomes are to be achieved. This can be a basis for the regulator to take enforcement action on its own judgement. In either case, the approach gives greater discretion to the regulator to decide what is permitted behaviour and what is not.

To illustrate the kind of principles which might be involved in such an approach, there follows below the 11 Principles of Business used in the UK:

1. Integrity - A firm must conduct its business with integrity.
2. Skill, care and diligence - A firm must conduct its business with due skill, care and diligence.
3. Management and control - A firm must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems.
4. Financial prudence - A firm must maintain adequate financial resources.
5. Market conduct - A firm must observe proper standards of market conduct.
6. Customers' interests - A firm must pay due regard to the interests of its customers and treat them fairly.
7. Communication with clients - A firm must pay due regard to the information needs of its clients and communicate information to them in a way which is clear, fair and not misleading.
8. Conflict of interest - A firm must manage conflicts of interest fairly, both between itself and its customers and between a customer and another client.
9. Customer relationships of trust - A firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgment.
10. Clients' assets - A firm must arrange adequate protection for clients' assets when it is responsible for them.
11. Relations with regulators - A firm must deal with its regulators in an open and cooperative way and must disclose to the Financial Conduct Authority anything relating to the firm of which the regulator would reasonably expect notice.

Under an approach such as this, enforcement action can be taken on the basis of both rules and principles. This means that enforcement action can be taken solely on the basis of a breach of Principle, even if no particular rule has been breached. For such approaches to work, market participants need to understand that they will be potentially subject to strict standards than are specified in rules. The regulator has to be sufficiently skilled, in the absence of clear rules, to be able to make a judgment determining what is acceptable and what is not. In addition, there should be clarity on the enforcement processes and applicable mechanisms that communicate the finality of decisions taken by the regulator. The relevant action in Kenya is:

- **7.1.6. - CMA will examine the case for some form of principles-based regulation.**

7.2. Restructure Legal Framework for Regulation

This section deals with the detail of the legal framework rather than the overall regulatory approach.

As integrated regulation is put into place it needs to be accompanied by a new, composite financial services law that is consistent across all sectors. Without this, and if the existing sectoral legislation is kept in place, the benefits of integration will be much reduced and the transformation of domestic markets and the attraction of international business will be less successful than it would otherwise be. The process of integrating legislation that is consistent across all sectors will provide the opportunity to update and streamline features of existing sectoral legislation.

- **7.2.1. - As Kenya moves over time to more comprehensive integrated financial regulation, CMA will support a parallel move to an integrated legal framework.**

Reviewing the adequacy of current legislation for financial markets

Irrespective of progress towards integrated regulation, a comprehensive review should be undertaken of existing and proposed capital markets legislation (Securities and Investments Bill; Capital Markets Authority Bill) against international standards, to accommodate new products and envisaged market infrastructures, and to strengthen the autonomy of CMA's regulatory approach vis- a-vis the National Treasury. This review should include the provision of a quality legal basis for derivatives markets.

Following CMA's self-assessment against the IOSCO Core Principles in 2010 an action plan was prepared to upgrade Kenyan legislative and regulatory arrangements to implement the standards in full. This work as well as work on assessment against CPSS-IOSCO Principles, including eight new principles on a regional basis, will be pursued to its conclusion. This is an essential part of enhancing the attractiveness of the Kenyan market to foreign participants and may result in a need for legislative change.

CMA will jointly with other interested parties carry out a fundamental review of the capital markets legislation, including ensuring that it meets the IOSCO Core Principles in full. It will be desirable in this review to ensure that there is clarity and accessibility of the statutes to ensure that all key infrastructure providers are governed by the same standards. As an outcome of this review the recently-amended CDSC Act should be incorporated into the newly updated securities and investment legislation.

- **7.2.2. - CMA will conduct a fundamental review of capital market legislation.**

Improving the quality of the consultation process

Before any new legislation, rules, guidelines or procedures are issued to the market the National Treasury or CMA, as the case may be, should issue, in exceptional circumstances, white papers on which there is proper public consultation, which ensures that all the relevant considerations are taken into account. This process is likely to be more efficient if these are preceded by green papers when time permits. A full cycle of consultation will involve: (1) the publication of research which sets out the background which supports either a change in policy or a new one; (2) publication of a draft of the proposed new policy itself together with a cost benefit analysis, and proposed implementation framework; (3) a specified consultation period; (4) publication of the input received during the consultation noting what/how feedback was incorporated and/or addressed in the final proposal; and (5) issue of the final legislation, rules, guideline or procedures.

- **7.2.3. - CMA will maintain consultation processes in line with international good practice.**

Improving the legislative process

The new emphasis on stakeholder participation in the legislative process has at the same time opened up political risks to the sound functioning of the process, including where parliamentarians may be under pressure from conflicted persons. Parliament needs to give due attention to the issues raised in the public consultation process.

It is also important to ensure that conflicted interests and contentious issues are identified and properly taken account of. The parliamentary process should be capable of tipping the balance against the authorities in their proper pursuit of the public interest.

In improving the Parliamentary process, especially in respect to law-making, CMA should be given the opportunity by respective House Committees to provide institutional support including offering appropriate clarifications when so required while championing that the final process needs to take into account public interest.

- 7.2.4. - **National Treasury and CMA will explore with National Assembly the scope for further improvement of process to ensure that capital markets legislation is properly considered with due account taken of public interest arguments.**

Streamline processes for creation of secondary legislation

Existing procedures for the generation of secondary legislation need to be reviewed in the light of the inefficiencies likely to have been introduced by the implementation of the Statutory Instruments Act. Since enactment of the new Constitution, new regulations have required Parliamentary approval. This slows down, perhaps materially, the ability of regulators to respond swiftly to detailed changes in markets.

The Statutory Instruments Act is out of line with international practice in requiring subsidiary legislation in the form of rules and guidelines for financial services to be specifically agreed by Parliament instead of being created under delegated powers. This is likely to have the consequence that subsidiary legislation may become out of line with evolving regulatory needs and affect the efficiency and international competitiveness of the Kenyan market place. It is vital for the smooth functioning of capital markets that rules and regulations can be adjusted swiftly in the light of evolving circumstances. It is imperative that this capacity is in place if there is to be any use made of the "no action" approach discussed above; it would be unsafe to allow new product developments to go ahead unless there was the capacity to make rules immediately if unforeseen circumstances arose. In this regard, amendments should be made to the Statutory Instruments Act to enable subsidiary rules and guidelines to be made by the National Treasury and/or CMA through delegated authority of Parliament.

- 7.2.5. - **CMA will explore with National Treasury the case for exempting subsidiary financial services legislation from the requirements of the Statutory Instruments Act.**

Keeping law up to date

As the law evolves, its always important to ensure it is up to date. Lawyers who practice in financial markets will most often be best placed to identify when law is getting behind market practice or else has gaps of other kinds. One option to obtain the best advice could be to establish a financial law committee or a review panel of leading financial market lawyers to act as a think tank for early identification of potential legislative gaps or challenges that could affect the functioning of financial markets including ancillary legislation, and propose legal and regulatory reforms. This legislation in question may extend beyond financial regulation and encompass, for example, commercial, contract, property or trust law. Such a panel would mitigate against the risk of new legislation failing to meet its purpose and ensure that existing legislation is up to date at all times. Such a panel would be chaired by an experienced lawyer. CMA would provide the secretariat, but the views of the panel would be independent and indeed would extend beyond the direct responsibilities of CMA. The panel's scope could cover other branches of financial regulation by agreement with the other regulators. The mandate of the comparable organisation in the UK is as follows:

The role of the [UK] Financial Markets Law Committee is to identify issues of legal uncertainty, or misunderstanding, present and future, in the framework of the wholesale financial markets which might give rise to material risks, and to consider how such issues should be addressed. The Committee will also act as a bridge to the judiciary to help UK courts remain up-to-date with developments in financial markets practice.

- **7.2.6. - CMA will establish a financial law review panel under its auspices.**

Integrated Financial Services Sector Tribunal

The development of sound legislation needs to go hand in glove with the development of the capacity of the court system to deal effectively with the complexity of financial services cases. It is important to ensure that judges have sufficient knowledge of the financial system, its regulatory structure, and current market practice. The financial law panel if established, would contribute immensely to keeping the Judiciary informed of new financial market issues through periodical engagement.

In some countries special courts or tribunals have been established in order to hear financial services cases. If Kenya is to be a centre of financial services, then it is likely that it will benefit from being a centre of expertise in terms of capacity to hear regulatory cases. For especially complex cases it would be possible to bring in external judges. Given that cases may involve more than one branch of financial regulation, it may be necessary for a specialized Tribunal to be established on a cross-sectoral basis,.

- **7.2.7. - CMA will support the development of financial expertise in the courts and support the establishment of an integrated Financial Services Sector Tribunal.**

7.3. Build Capacity of Capital Market Regulators

In line with the conclusions of the Presidential Parastatal Task Force, it will be necessary to ensure that the CMA board has the right skill sets through adequate, more competitive appointment and board evaluation processes. The CMA board has an important role in both providing guidance to the executive and presenting the CMA's external face to the Government, to the public and to the markets. To do this effectively, in addition to the skills brought by the ex-officio members, it needs to have among its non-ex officio members a broad range of key skills including technical market expertise, accounting, corporate governance and legal skills, and the availability and energy to apply them to the sound internal running of CMA and to its external presentation. At the same time it needs autonomy to not only be independent of both political and commercial pressures but also to be seen to be so, to avoid any perception that board members are representative of capital markets industry interests. This will be particularly important, especially to potential foreign entrants to the Kenyan market, who would be concerned if they thought that board members were serving local sectoral interests rather than the broader public interest. Similar consideration will apply when the Financial Services Council is appointed.

The board should undertake an initial review of the skill sets required, which should be kept updated as market requirements change. This should be used when new appointments are made in order to assess the skill sets required. Open advertising of appointments could increase the base from which appointments are made. A nominating committee of the board could make recommendations to the Cabinet Secretary who would expect to attach considerable weight to them. The board should undertake periodic external evaluation of its performance.

- **7.3.1. - CMA will seek to ensure that the appointment process for board members is in line with emerging best practice and the board will review the skill sets it requires.**

In order to meet the demands set by the Master Plan, CMA will continually enhance staff capacity through appropriate recruiting, performance assessment and training arrangements. The staffing of CMA needs to be responsive to the very particular skills required of a capital markets regulator and in particular to changes in requirements for technical skills. These may be different from those required of other parastatal bodies. This may require exemption from Government human resourcing guidelines. The CMA needs to have sufficient flexibility in its staffing to ensure that it meets the legitimate expectations of its stakeholders.

A particular challenge is the need to manage resources in anticipation of requirements, including those deriving from the Master Plan and from market developments, which may or may not eventually transpire. In this regard, CMA will need to ensure that it maintains centres of technical excellence capable of responding to market requirements as needed. It will need to be possible to employ staff with market experience on an appropriate basis, perhaps through secondments, as well as recruit internationally. It should give consideration to staff exchange programmes in order to develop hands-on experience amongst its own staff and to learn from the experience of staff from other national and international regulators.

CMA is currently undertaking a project which will propose a new establishment, identifying optimal numbers for each directorate, and will design a suitable pay structure to ensure both internal and external equity as well as link pay to performance through clear job classifications and a recommended remuneration structure for each grade. It will provide a competency framework for all positions and a grading structure for all positions in line with a revised organisation structure. It will also provide for career progression guidelines for all established positions to meet the functional and organisational needs of the CMA. There will be a detailed implementation and change management road map.

- 7.3.2. - **CMA will act on the conclusions of its current job evaluation and reorganisation project for its human resource requirements and will ensure over time that its staffing needs, remuneration arrangements and organisational structure continue to match evolving requirements.**

There are also questions as to whether CMA has adequate financial resources to perform the role expected of it. CMA needs to undertake a review of its budget against its statutory responsibilities and new roles required under the Master Plan and against investor, including international expectations. It should review alternative funding models, including reducing reliance on fees generated by attracting business, both because of their variability and because of the risk of perverse incentives. If alternative funding methods are required, CMA should seek to agree these with the National Treasury and with stakeholders.

- 7.3.3. - **CMA will seek to ensure its budgets and funding match resourcing needs over time and build in sufficient flexibility to meet stakeholder expectations including those arising from the Master Plan.**

There are said to be concerns that CMA's external communication effort is inadequate, leading to potential uncertainty and sometimes misunderstanding on the part of market participants. In particular, it is felt sometimes to have a slow response time in relation to supervisory matters. CMA will publish targets for response times, though it needs to be recognised by the market that requests for supervisory response need to be fully documented before CMA can begin to respond.

In terms of more general communication strategy, much well-considered thinking inside CMA is not always made publicly available. CMA will review its overall communication strategy and the range of communication tools at its disposal, including the consultation processes in relation to draft legislation or rulemaking (which is considered further below). It will consider what information needs to be available to the market, and to the public, at what stage and through what medium. It will also consider making more of its internal research available to demonstrate its forward thinking and to stimulate wider and earlier public discussion of critical market issues. Enhanced communication will lead to smoother working relationships with market participants and Parliament, better policy outcomes, a better informed public and an enhanced CMA reputation for thought leadership. A well-informed market place led by a regulator with a reputation for forward thinking will enhance the international attractiveness of Kenya's capital markets.

- 7.3.4. - **CMA will ensure its external communications and outreach demonstrate careful thought leadership and that it maintains reasonable response times.**

In order to ensure that its thinking is up to date with thinking internationally CMA will need to establish and maintain its links with important sources of ideas and advice. This can be done by informal relations with the CMA's peers internationally such as through IOSCO or with individual foreign regulators (e.g.: Kuala Lumpur or London for Islamic finance), through technical assistance from the official (e.g.: IMF, World Bank, IFC) and private sectors (e.g.: CityUK), and through appointment of external consultants on a targeted basis.

- 7.3.5. - **CMA will ensure adequate access to external expert advice.**

8. IMPROVE CORPORATE GOVERNANCE AND FINANCIAL REPORTING

A sound financial market is critically dependent on sound corporate governance, reliable, and transparent financial reporting. Without this a market is unlikely to develop or attract foreign interest. Failures in corporate governance or the issuance of misleading financial reports can cause enduring reputational damage to any capital market, which can be a challenge to reverse. A number of measures are necessary to bolster the existing arrangements and bring them to international level.

8.1. Strengthen and Enforce Corporate Governance Standards

In order to strengthen and enforce corporate governance standards in the capital markets, CMA will strive to create a single basic corporate governance code for all companies, with sectoral financial services requirements, for example, banks or intermediaries as additional add-ons. In any case it is important to accelerate work on converting corporate governance guidelines for issuers into a Code. In doing this, an opportunity is provided to consider incorporating recent enhancements from other jurisdictions; for instance, in relation to board training and evaluation requirements.

In furtherance of this objective CMA appointed a nine-member Capital Markets Corporate Governance Steering Committee in December 2012 as part of its overall effort to strengthen the corporate governance framework of the capital markets

The work of the Committee has involved extensive local and international benchmarking through the support of World Bank and International Finance Corporation corporate governance experts as well as local corporate governance experts.

The Committee reviewed various domestic and international corporate governance frameworks including; the Guidelines On Corporate Governance Practices by Public Listed Companies In Kenya; the Capital Markets (Securities) (Public Offers, Listing And Disclosures) Regulations (2002); Central Bank of Kenya Guideline on Corporate Governance (2012), Insurance Regulatory Authority Corporate Governance Guidelines (2011); the State Corporations Act and the draft (2012) Companies Bill of Kenya. International practice reviewed included the UK Code of Corporate Governance (2012); the updated Malaysian Code of Corporate Governance (2012); the King III report (2009); the Brazilian Corporate Governance Code (IBGC 2010); and the Australian Stock Exchange (ASX) Code (2010).

The work of the Committee was broken into two distinct phases; the first being the development of a Corporate Governance Blueprint giving concrete recommendations to strengthen the laws, regulations and institutions that impact corporate governance in Kenya. While corporate governance principles may apply to many different types of companies, the Blueprint focuses on those companies participating in the capital markets, including issuers (listed companies) and capital market intermediaries. The Blueprint details the business case for corporate governance and set out recommendations in respect of:

- Board Operations and Control
- Shareholder Rights
- Stakeholder Relations
- Ethics and Social Responsibility
- Transparency and Disclosure
- Regulation and Enforcement

The Blueprint incorporates the action plans, key steps and time frames with respect to the various recommendations. The Blueprint will be exposed for public consultation in coming months and thereafter will inform the second phase covering the drafting of the resultant Kenyan Code for Corporate Governance as well as the regulatory and statutory frameworks and amendments necessary to support the regulation and enforcement of the Code which are expected to be exposed for Industry consultation in the second quarter of 2014. The Code is also expected to set out the framework and principles for skills and knowledge development of directors through continuous education in addition to programs for advocacy and sensitization of investors and key stakeholders. Because of the resistance likely to be faced in relation to enforcement of the Code (see next section), consideration should be given to the Code being formally endorsed by the National Treasury to indicate the political importance attached to the progress, which is essential in this area.

CMA could consider whether the Code should make it compulsory for companies to issue an externally- audited governance report (in the same way as a financial audit is necessary) to make sure they are compliant with key standards and requirements. Such external governance audits could be conducted by Certified Public Secretaries.

More generally, the importance of good corporate governance needs to be more widely understood and should be promoted by CMA, including through the Listing arrangements, and Institute of Certified Public Secretaries of Kenya (ICPSK). This will be particularly important if there is to be a shift from family to more widely held companies. Lack of preparation for formal corporate governance requirements has been identified as a potential obstacle to an increase in the number of listed companies.

This may go beyond simple ignorance of corporate governance requirements to lack of understanding of the business case for good governance. There can be unresolved conflicts of interest between board members, improper board appointment processes, lack of segregation of the role of Chairman and CEO, and lack of independence of directors. The gap between what exists and what is required may require an unexpected degree of restructuring, including the appointment of new independent directors, as well as heightened transparency, both financial and in relation to business activities, any of which may be regarded as a threat to a family company's business model if the advantages are not properly understood. The action is:

- **8.1.1. - CMA will continue to pursue its existing work programme on corporate governance covering both the corporate governance code itself and education in good corporate governance.**

  A good corporate governance code is not sufficient in itself without mechanisms for ensuring that it is adhered to. The standard approach is to require companies to comply with the code or explain where and why they have not. There needs to be a review in Kenya as to whether such an approach, which tends to focus simply on enforcement in relation to lack of disclosure, is sufficient to deliver sufficiently high standards of governance. It seems likely that enforcement processes need to be enhanced to address issues of non-compliance with key requirements.

  CMA's powers will need to be set out in relation to the setting of a maximum time limit for disclosures of non-compliance and the taking of remedial measures, and the penalties for breach. CMA should consider establishing a process for confirming the independence status of directors which does not rely solely on a statement from the issuer and there should be sanctions for directors whose status changes without prior approval by CMA. The CMA should consider establishing a process for reviewing the role of directors through a periodic review of board operations. CMA should consider an explicit formulation of the CMA's powers in relation to board charters and to disputes between directors or between directors and shareholders.

  A complementary approach could be to build on the existing activities of ICPSK to intensify self-auditing of adherence to corporate governance requirements. The proposals for a regular corporate governance health check by companies leading to the generation of a regular Governance Index will provide a way of measuring improvements in the quality of corporate governance.

  In particular, it would be beneficial to build on the ICPSK project to seek to influence County Governments to embrace sound corporate governance principles. Sound governance at County level will be critical if the Counties are to come to the public markets, particularly if there is international involvement. The joint work between ICPSK and the Ethics and Anti-Corruption Commission to ensure governance, ethics and integrity are integrated at a County level should be encouraged.

A further approach is to consider whether a shareholder code designed to help in enforcing comply or explain, as is used in some other jurisdictions, is relevant to Kenya. This is normally most efficacious where there are active institutional shareholders. Another option is to consider promoting an enhanced role for shareholder associations in engagement with company boards. The development of a national publicly-listed shareholders association could assist in this. For such shareholder associations to be effective the members and their representatives will need to have adequate understanding of the issues so that capacity building in this area will be an element in the overall education programme.

There is also a need to consider the appropriate role for minority shareholders, balancing the rights and obligations of both majority and minority shareholders.

Concerns have been expressed that such a balance is not always achieved, although international experience suggests this is in its nature often a challenging issue.

- **8.1.2. - CMA will undertake a review of the different ways in which good corporate governance can be achieved in practice and will act on its findings.**

- **8.1.3 - NSE to develop a corporate governance social responsibility and sustainability index**

8.2. Ensure Adherence to International Reporting and Disclosure Standards

Accounting

Financial markets are wholly dependent on sound and reliable financial reporting. There needs to be confidence that financial reports reflect the true and fair view of a company's affairs in line with the International Financial Reporting Standards (IFRS). A coordinated effort is needed by issuers, auditors and investors to ensure that this is always an absolute priority. Markets internationally also expect that sound financial reporting will be policed by a regulator. There appears to be some ambiguity as to the responsibility for the official oversight of and then enforcement of financial reporting requirements which is not normally left solely to the auditors. Internationally, whichever agency is explicitly responsible for the enforcement of accounting standards, often the securities regulator, will usually have the legal means either directly or indirectly to require restatement of accounts so that markets are not misled. It is important to ensure adequate resources are available within CMA to perform this role and that proper powers and mechanisms are in place for requiring restatement of accounts when necessary.

- **8.2.1. - CMA in partnership with ICPAK will review the arrangements for the enforcement of the sound financial reporting of listed companies, including the legal basis and the adequacy of resourcing.**

Audit

For financial reporting to be reliable, audits need to be conducted in line with the relevant auditing standards, which should be International Standards on Auditing, and the performance of the auditors needs to be subject to external review. Existing inspection arrangements by ICPAK, while welcome, do not conform with international best practice which now requires independent oversight of public interest entities, including listed companies and financial institutions.

Government efforts should be renewed to agree a satisfactory Financial Reporting and Oversight Bill. New legislation is important to establish legal authority for independent auditor oversight responsibilities and for the related disciplinary arrangements. The need is to establish an independent auditor oversight body for Public Interest Entities along the lines established in nearly all other international financial centres (including in Africa: Egypt, Mauritius and South Africa) and adhering to the Core Principles of the International Forum of Independent Audit Regulators (IFIAR). In order to maintain international confidence in Kenyan auditor oversight arrangements, membership of IFIAR, which is subject to strict criteria, should be secured for Kenya. The IFIAR Core Principles provide stringent requirements for independence which also entail satisfactory resourcing.

The various parties with an interest in audit, including the accounting institutes and investors as well as CMA, need to support legislative moves to establish an auditor oversight body on a sound basis which will command international credibility. Such a body would support efforts to ensure that financial reporting is thorough, particularly in sustaining high levels of professional conduct on the part of the auditors.

Although internationally the securities regulator sometimes hosts the auditor oversight authority, it is more common for it to be housed as a separate authority. The decision on this in part depends on whether such a separate independent authority can be feasibly created. One option for aiding the creation of a strong independent body is to combine the role of setting the corporate governance code with independent auditor oversight in a single body with close links to the financial services regulators.

- 8.2.2. - **CMA will support ongoing work with the National Treasury to move forward with the speedy establishment of an independent Kenyan auditor oversight regulator in adherence to the Core Principles of IFIAR.**

9. INNOVATIVE, OPEN AND COMPETITIVE ENVIRONMENT

Innovation and competition are key requirements in ensuring that financial markets meet the needs of their users and that efficiency benefits are passed on. The development in Kenya of mobile money transfer is a fine example of how an innovative financial service has brought benefits to millions of people. The main driver of innovation must be market participants themselves, identifying opportunities and developing new products or services to meet them. In some cases a new product or service can be developed and rolled out by a single firm. In other cases, the launch of a new product, asset class or market will require a coordinated effort by a group of market participants and infrastructures to develop standard documentation, obtain regulatory approval and promote it to potential users. It is up to market participants to mobilise themselves in this way when needed.

The role of the regulatory authorities is to support innovation and competition, rather than to drive it. They can do this by maintaining open access to the financial system in order to make it possible for new entrants to challenge the incumbents. This policy is not always popular with established financial firms, but it needs to be championed to ensure that financial markets deliver benefits to the whole economy. Regulators can also support innovation by ensuring that they have the capacity and expertise to assess proposals professionally and that they can do so within acceptable time frames (see Section 7.3). In the long run, innovation and competition will drive market growth, with the potential to attract business from other markets. This in turn enables all market participants to benefit from access to a larger market.

9.1. Open Access to Market Infrastructure

All parts of financial market infrastructure - exchanges, clearing houses and CSDs - set criteria to be met by firms using their services. This is necessary to protect their financial position and their efficiency. However, the entry criteria should be set at the minimum level necessary to protect the integrity of the infrastructure and reviewed regularly to ensure that no unnecessary barriers are placed in the way of new entrants to the market. Open access and competition may result in the competing market infrastructures providing similar services. Supervisory standards should be the same for all market infrastructures providing the same service.
The principle of openness should also apply between market infrastructure providers. Thus, a clearing house or CSD should have transparent, objective standards on the basis of which they will provide clearing or settlement services to new trading platforms. This is particularly important if an incumbent exchange has a dominant ownership or governance role in relation to a clearing house or CSD.

- 9.1.1. - **Review market infrastructure membership criteria.** CMA will regularly review the membership criteria of market infrastructure providers to ensure they are transparent, proportionate and not acting as a barrier to entry.

9.2. Liberalise Fee Structure

At present a wide range of market fees are either set by or subject to minimum levels set by regulators. This is understandable when there is concern that market power may result in fees being set too high or that predatory pricing may be used to drive competitors out of the market. Over time, however, an innovative and competitive market depends on firms being able to innovate and having the freedom to set their own fees. It is only in this way that the more efficient and innovative will be able to pass on the benefits of their advantages to their customers, thus stimulating growth in market volumes through lower costs. The envisaged freedom to set fees is conditional on the existence of open, competitive markets and the potential for uncompetitive firms to exit particular markets. As market infrastructures provide services that are essential for all market users, their fees must be set and published in a transparent, non-discriminatory manner. There may be a part of the financial infrastructure that does not lend itself to competition as there is only room for a single provider - a so-called "natural monopoly". In most countries, the CSD is the only clear example. If such a case arises, we propose that its governance should be constructed so as to give a significant voice to its users as a means to ensure that the organisation generates efficiency benefits and passes them on to users.

However, in many cases where there is only a single provider today, the threat of new entrants in an open system can be sufficient to ensure the incumbent generates and passes on benefits to customers.
The liberalised approach to setting fees should be phased in over the period covered by the Master Plan, as concerns about market dominance are addressed either by creating more competitive conditions or by giving users a larger role in governance.

- 9.2.1. - **Phase in liberalisation of financial policies for financial firms and infrastructure providers.**

9.3. Involve the Competition and Consumer Protection Authorities

The existing financial sector regulators in Kenya have varying degrees, mandates to address consumer protection issues relating to regulated institutions. However without a robust integrated financial sector consumer protection framework retail consumer confidence may be undermined by the perception of the absence of an effective recourse mechanism or uneven coverage and enforcement across the system.

In addition to the existing regulatory agencies and the Competition Authority, whose main focus is on monopoly and price control related issues, alternative avenues for addressing consumer protection such as a financial sector. The Commission for Administrative Justice should be strengthened and leveraged upon to deal with matters such as individual complaints.
The backstop to the measures proposed here is the possibility that the Competition Authority of Kenya and other consumer protection authorities could intervene in any case where an institution or group of institutions abused their market position or consumers seek recourse on cross cutting conduct and market practice issues. It should be made clear that all the relevant authorities take responsibility for reviewing the financial markets from this perspective, based on their respective Mandates.

- 9.3.1. - **CMA should keep the Competition Authority advised of moves to liberalise markets** so that, if necessary, it can intervene to prevent abusive behaviour.

- 9.3.2. - **CMA should work with policy makers to ensure that appropriate frameworks for consumer protection are put in place.**

IMPLEMENTATION PROCESS AND ROADMAP

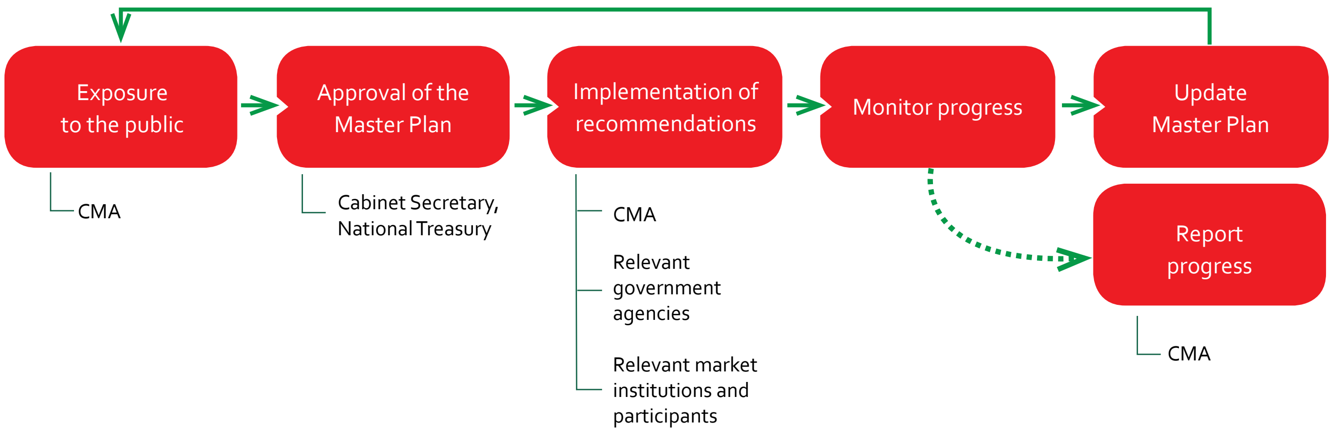
The previous section sets out a number of actions aimed at achieving the objectives and strategic initiatives of the Master Plan. Ultimately, the realisation of these objectives and strategic initiatives will depend on the effective implementation of the actions. To ensure this is achieved, this implementation framework:

- Sets out a mechanism for co-ordinating the implementation of the Master Plan;
- Highlights the skills, capacity and resources necessary for implementation;
- Provides guidelines for regular performance monitoring and progress reporting; and,
- Describes the communication programme necessary to spread awareness of the Master Plan.

Lastly it identifies the sequence in which the actions might be implemented as well as the priority areas which would benefit from immediate implementation and those which can only be implemented in the long term.

Implementation Process

The approach to implementing the Master Plan is illustrated below.



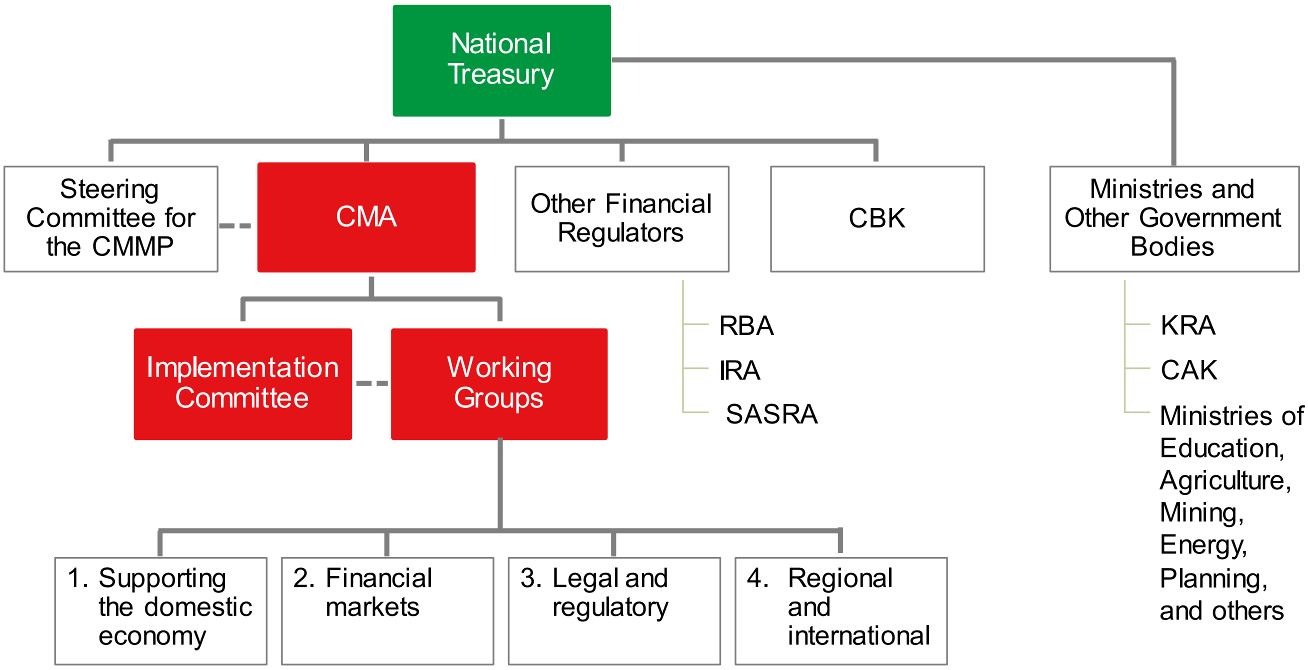
As shown, CMA will be responsible for managing the implementation of the actions contained in the Master Plan within the stipulated timeframes. In implementing the actions, CMA will rely on the support and assistance of a variety of other Government agencies as well as on that of market institutions and participants. From this perspective, implementation of the Master Plan is a collective process which depends on the efforts of the entire capital market in the country.

Progress in implementing the Master Plan will be monitored against the performance measures set out in the previous sections. Variances in performance will be analysed by an Implementation Committee formed under the CMA Board and highlighted to the relevant authorities and affected parties for further action. Progress reports will also be posted on the CMA and Vision 2030 websites to ensure that industry participants as well as the general public are kept informed of the progress.

Given that the external environment may play a role in shaping the evolution of Kenyan capital markets, it is anticipated that there may be developments that may affect the implementation timeframe and other details of certain actions. Thus, while the broad objectives and strategic initiatives of the Master Plan are expected to remain unchanged, a periodic review (at least every two years) of the actions contained in this document should be conducted to ensure the actions remain relevant and applicable. Where necessary, therefore, the Master Plan will be updated with appropriate revisions and additions. Any revised Master Plan will be circulated to the public for comment before being adopted by the National Treasury once again.

Implementation Structure and Management

The structure for the implementation and monitoring of the Capital Market Master Plan as well as the various parties that are involved in this process are depicted below.



National Treasury

The National Treasury is the implementing ministry for the deepening of capital markets under Vision 2030. The National Treasury will retain this role throughout the course of implementation but, as per the implementation structure of Vision 2030, will delegate implementation authority for the Master Plan to the Capital Markets Authority.

Capital Markets Authority

As the lead implementer for the Capital Market Master Plan, CMA will first and foremost commence work on the implementation of actions that directly affect its areas of responsibility. These include, for example, actions relating to the appointment of CMA board members, to review its human resource requirements and to enhancing its external communications and outreach.

In addition, CMA will take steps to facilitate the implementation of other actions that are outside of its typical jurisdiction. These include, for example, actions relating to the establishment of a national financial sector strategy or a cross-sectoral national consumer education strategy.

Steering Committee for the implementation of the Capital Market Master Plan

The implementation of the Master Plan will require interaction among senior officials such as the Cabinet Secretary, National Treasury; the Governor of the Central Bank of Kenya; The Attorney General; the CMA Chief Executive, ; other financial sector regulators (such as the RBA, IRA and SASRA) – which can be represented by the Financial Services Council, as well as the NIFC Steering Committee, the Chair of the Vision 2030 Secretariat, and any other Ministries that are affected by the implementation of the Master Plan (including, for example, the Ministry of Agriculture and the Ministry of Education). In addition, the implementation of the Master Plan will also require interaction with the NIFC Steering Committee.

Cognisant that each of these bodies may have their own strategic plan, it is important to have a high-level forum to achieve coordination in the development of the Kenyan financial services sector. Specifically, the coordination of the implementation of the Master Plan with the work of other Government bodies and regulators will look to:

- Facilitate cooperation and implementation strategies among all relevant agencies; and,
- Synchronise the communication of issues and developments in areas involving more than one jurisdictional authority.

To establish this forum the Cabinet Secretary for the National Treasury will appoint a Steering Committee for the Capital Market Master Plan through a notice in the Kenya Gazette. The Committee will be chaired by the Cabinet Secretary and its secretariat will be based at the National Treasury. The terms of reference of the Steering Committee will include:

- To take overall responsibility for the implementation of the Master Plan;
- To facilitate the work of the Implementation Committee and the Working Groups in implementing actions contained in the Master Plan;
- To oversee the establishment of Kenya as the heart of African capital markets;
- To identify, recommend and approve funding options as may be necessary for the implementation of actions contained in the Master Plan.

Implementing Committee

The Steering Committee above will establish an Implementation Committee to ensure effective and efficient implementation of the Capital Market Master Plan. This Implementation Committee will draw some of its number from the Capital Market Master Plan Steering Committee, as well as draw upon the expertise of industry participants and stakeholders, as well as financial sector regulators, professional advisors, academia, specialist resources and Working Groups as necessary. It will be chaired by the Chief Executive of the Capital Markets Authority or lead executive charged with oversight of the Capital Markets in an environment of consolidated regulation.

For coordination to work, these representatives must be given authority to commit their agencies and constituencies to the process of implementation, or alternatively must have a mechanism to rapidly obtain that authority. The Implementation Committee will then appoint a permanent project manager with adequate resources (and access to external support when needed) and liaison officers from each responsible institution or authority.

The key responsibilities of the Implementation Committee will include:

- Functioning as the secretariat for the implementation of the Capital Market Master Plan;
- Coordinating the implementation of actions, including liaising with the various Working Groups and other relevant parties;
- Identifying and managing the resolution of issues which may arise in the course of implementation;
- Undertaking the monitoring of progress and evaluation of performance based on specific targets; and,
- Coordinating the communication program for the Capital Market Master Plan.

Working Groups

The responsibility for the operational implementation of various actions will be devolved by the Implementation Committee to four Working Groups, whose proposed composition is set out below. These Working Groups will be established under the Implementation Committee and will be responsible for taking on the implementation of actions set out in the Master Plan.

As is the case for the Implementation Committee, these Working Groups will comprise representatives from relevant industry associations, market infrastructures, departments within the various financial sector regulators and a host of other market participants. The Working Groups will need to establish more-focused working groups to address individual issues. Where appropriate the Working Groups should draw upon external expertise provided by international or local consultants.

Overall, these Working Groups will be responsible for liaising and consulting with the various Government and regulatory bodies, industry associations and participants, professional bodies, and other affected stakeholders in the implementation of their specific actions.

To facilitate monitoring and coordination, each Working Group will also include representation from the Implementation Committee.

Working Group	Area of Responsibility	Key Members
1. Supporting the domestic economy	· Analysis of financing needs · County financing · Infrastructure finance · Islamic finance · Asset management, REITs · Consumer education	· National Treasury · Ministry of Devolution and Planning · LAPSSET Development Authority · CBK · CMA · IRA · KRA · SASRA · RBA · Vision 2030 · Islamic institution · Association of Fund Managers (AFM) · Academics · Representatives of the Ministry of Education · KASIB · COFEK · NSE · Controller of Budget · NOMAD
2. Financial markets	· Develop NSE · Develop bond markets · Modernise CDSC · Develop spot and derivatives markets and infrastructure	· National Treasury · KRA · CBK · CMA · NSE · CDSC · Kenya Bankers Association (KBA) · Bond Market Association (BMA) · KASIB · FMA · ACIS · NSSF · NCPB · Communication Authority · Nairobi Coffee Exchange · KACE · Diaspora Rep · Leasing Association of Kenya · Representatives of relevant Ministries where commodity derivatives are envisaged- Ministry of Industrialization & Enterprise Development; Ministry of Mining; Ministry of Energy & Petroleum; Ministry of Agriculture
3. Legal and regulatory	· Regulatory developments · Corporate governance · Review of legislation and process · Promote competition	· National Treasury · CBK · CMA · Attorney General · Competition Authority · ICPAK · ICPSK · Law Society of Kenya · Law firms · NSE · KASIB · COFEK

4. Regional and international	· Liaise with NIFC · Engage with international rating bodies such as MSCI Z/YEN and monitor progress toward improved ratings · Promote Kenya capital markets abroad · AML, tax issues · Regional initiatives	· National Treasury · CBK · CMA · NIFC SC · KBA · KASIB · KRA · NSE · Ministry of Transport & infrastructure · Ministry of East African Affairs, Commerce & Tourism · Financial Reporting Centre

Sequencing of Actions and Responsibilities

The high-level phasing for the implementation of actions set out throughout the Master Plan is set out below as follows. These actions are grouped according to their respective building blocks and the timing of implementation is consistent with:

- Short term: 2014 – 2016
- Medium term: 2016 – 2020
- Long term: 2020 – 2023

Short Term - Analysis, consolidation and modernisation (2014-16)
The immediate priority for the Master Plan is the modernisation and strengthening of the domestic capital market, including its legal and regulatory underpinnings. The financing needs of the country will be determined and obstacles to financing removed where possible. The long term aim of upgrading the skills of local professionals and educating investors begins here.

The priorities in this Phase are:

- Analyse financing needs and the obstacles in the way of development;
- Lay the foundations for growth in existing sectors;
- Modernise markets and infrastructures;
- Modernise legislation and regulatory approach; and,
- Progress development of EAC single market in financial services.

Medium Term - Building competitive markets (2016-20)
With the major improvements made in the first phase, this second phase will see the development of new markets (such as spot commodities and derivatives), the achievement of international standards in the underlying infrastructure and the achievement of Emerging Market.

The priorities in Phase are:
- Improve international competitiveness;
- Develop new markets (spot commodities, derivatives, stock lending);
- Open up markets to competition;
- Achieve international standards for market infrastructure; and,
- Achieve MSCI emerging market status.

Long term - Facing the international challenge (2020-23)
The work undertaken in the first two phases will have created the basis for an efficient and internationally competitive capital market. This latter phase will focus on consolidation of earlier gains, further market developments (particularly in the derivative space), further deepening of the markets and the active promotion of the Kenyan capital markets overseas. The priorities in Phase are, therefore:

- Consolidation of work done in earlier phases;
- Promote Kenya's developments and offerings internationally; and,
- Develop new markets (agricultural and commodity derivatives) based on earlier developments.

The sequencing of these three phases is illustrated below.

Short Term			Medium Term				Long Term		
2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Modernisation and strengthening of the domestic capital markets and removing obstacles to financing									
			Development of new markets, opening up markets to competition and achievement of international standards. During this period, Kenya should achieve MSCI Emerging Market Status						
							Consolidation of earlier gains, further market developments, and continuing to promote Kenyan capital markets overseas. At the end of this period Kenya will have a vibrant, internationally respected capital market		

Having set out the high-level phasing for the implementation of the Master Plan, the following tables provide a more detailed implementation schedule for each of the individual actions contained in the Master Plan. These actions are grouped according to their respective building blocks and the timing of implementation and prioritised according to the legend below.

In the tables that follow, actions that are very **important** to the realisation of the vision of this Master Plan are highlighted in Red.

Normal actions that still contribute to the achievement of the vision but that are less important are highlighted in Grey.

Domestic market accessibility and prosperity

No.	Action	Short term	Medium term	Long term	Status as at 30th April 2016
1.1.1	CMA will identify and analyse the funding gap at the national and county level to inform on product development				Consultancy funding support to undertake the financing gap study secured with analysis to be commenced in June 2016
1.2.1	CMA to host forums on county financing needs strategies				Forums held in 21 counties: Nairobi, Kericho, Mombasa, Kilifi, Taita Taveta, Kwale, Murang'a, Nyeri, Machakos, Makueni, Embu, Meru, Kitui, Kisumu, Homabay, Kakamega, Bomet, Uasin Gishu, Transnzoia, Nakuru and Kericho

1.2.2	CMA to partner with relevant stakeholders to develop an adequate legal and regulatory framework				***Continuous:*** The Authority has continued to engage stakeholders through workshops and public exposure on draft legislations.
1.3.1	CMA to support the development of a national consumer financial education policy and strategy				Development of white paper on consumer financial education to support the policy and strategy on course
1.3.2	CMA to continue implementing its own Investor Education and Public Awareness programme, subject to its own area of competence				***Continuous:*** Key achievements include National Trivia, Nairobi County University Challenge, and Recruitment of Resource Persons for outsourced education initiatives.

Gateway for regional and international capital flows

No.	Action	Short term	Medium term	Long term	Status as at 30th April 2016
2.1.1	Support discussion on regional financial integration				The first set of seven Council Directives were gazetted on 29th May 2015 in the East African Community Gazette Vol. AT 1 – No. 7. These are: Council Directives on Public Offers of Equities, Debt and Asset Backed Securities; Collective Investment Schemes; Regional Listing; Admission to a Secondary Exchange and Corporate Governance for Markets Intermediaries. The Authority has now embarked on transposition process to enact them in national law.
2.1.2	Develop creative products that promote investor confidence in regional products				Policy Guidance Note for the roll out of Exchange Traded Funds issued. Draft PGN for Global Depositary Receipts and Global Depositary Notes under development.
2.1.3	Support regional financial market infrastructure linkages				Scheduled for Medium Term
2.2.1	Remove obstacles to raising finance for infrastructure projects				Stamp Duty exemption for tax neutrality for Real Estate Investment Trusts (REITs) and Asset Backed Securities (ABS) achieved. Memorandum of Policy Proposals recommending additional exemptions (Value Added Tax) submitted to the National treasury in January 2016. New market segments for listing of Real Estate Investment Trusts (REITs) and Asset Backed Securities (ABS) have been established.

2.2.2	Assist potential infrastructure issuers in coming to market				Investor sensitization programs targeting potential issuers, arrangers/ transaction advisors and providers of guarantees have been implemented guided by Medium term Plan 2 Vision 2030 infrastructure flagship projects. Engagements undertaken with Kenya Maritime Authority, Kenya Ports Authority, Kenya Roads Board, County Governments Stanlib Fahari Income-REIT of Ksh 3.6 billion was listed on the Nairobi Securities Exchange on 27th November 2015 as the pioneer REIT product. CMA further approved Fusion Capital - a Real Estate Investment and Private Equity firm based in East Africa to issue two Development Real Estate Investment Trusts i.e. a commercial and a residential Development and Construction REIT
2.2.3	Implement actions contained in the World Bank/IFC report on mutual funds				Consultancy funding support secured to guide implementation of actions contained in the world bank report.
2.2.4	Review the tax structure of collective investment scheme products				Scheduled for Medium Term
2.2.5	Create a regulatory framework for Islamic capital markets				A Project Management Office on Islamic Finance has been established bringing together international experts and representatives of all financial sector regulators and. The PMO has commenced review of the Financial Services policy and regulatory framework to make it facilitative to the development of Islamic Finance. Initial set of statutory and regulatory amendments submitted for consideration by the National Treasury on March 31, 2016
2.2.6	Develop a separate policy, legislative and regulatory framework for Islamic products and services				On course under PMOs scope of work
2.2.7	Leverage existing relationships to develop Islamic finance expertise				The Project Management Office draws membership from all the financial regulators. The PMO has been set up with the support of Financial Sector Deepening (Africa) as a key partner. The office has also drawn up Terms of Reference to leverage from expertise in Islamic Finance through Ad Hoc policy and legal subcommittees drawn from market professionals and Islamic scholars

2.2.8	Identify and make policy proposals to facilitate development of Islamic finance in the annual Memorandum of Policy Proposals to the National Treasury and implement programmes through industry coordination and relevant partnerships.				Project Management Office finalised and through the CMA submitted specific tax and non-fiscal policy proposals to facilitate the development of Islamic Finance in Kenya to the National Treasury on March 31, 2016.

Providing access to international financial markets

No.	Action	Short term	Medium term	Long term	Status as at 30th April 2016
3.1.1	Implementation Committee, together with other relevant authorities, should establish a process for monitoring progress in international rankings				Development of a self-assessment tool for the purpose of achieving the MSCI ranking has been initiated.
3.1.2	CMA to be represented on the Steering Committee of the NIFC				A CMA staff seconded to the NIFC Authority Secretariat and the CMA will also be represented on the Board of the NIFCA once the relevant Bill is enacted
3.2.1	Kenya to take action to raise its AML/ CFT rating				Following the operationalization of the Financial Reporting Centre and the statutes on AML and Terror Financing Kenya was dropped from the FATF "Dark Grey" list. AML Guidelines for capital markets intermediaries were published in the Kenya Gazette by the Cabinet Secretary National Treasury in March 2016 in order to strengthen implementation and compliance with the AML and CFT statutes in the capital markets sector.
3.2.2	Extend Kenya's network of Double Taxation Agreements while managing the risks of investment practices such as transfer pricing				Scheduled for Medium Term. Outcome will be influenced by joint efforts of the National Treasury, State Law Office and the Kenya Revenue Authority
3.2.3	Ensure Kenya adopts OECD standards wherever possible				Scheduled for Medium Term. However, a sub-committee on tax matters has been constituted under WG3
3.2.4	Ensure standards for information exchange on taxes are in line with requirements of OECD Global Forum on Transparency and Exchange of Information for Tax Purposes				Scheduled for Medium Term. However, a sub-committee on tax matters has been constituted under WG3
3.2.5	Ensure personal and corporate tax are attractive to internationally mobile employers and employees				Scheduled for Medium Term. The NIFCA has implemented a consultancy to guide on the tax incentives to be put in place to support the establishment of Nairobi as an IFC.

3.2.6	Review the adequacy of the corporate and personal tax framework for financial services				Scheduled for Medium Term. The NIFCA has implemented a consultancy to guide on the tax incentives to be put in place to support the establishment of Nairobi as an IFC.
3.3.1	Put in place Regulatory MoUs to allow for the exchange of confidential information				CMA is a signatory of the IOSCO MMOU. CMA has signed MOUs with the following regulators: FSC-Mauritius, Securities and Futures Bureau, Financial Supervisory Commission-, Chinese Taipei (Taiwan), SEC- Nigeria , CMC- Angola, SEC-Ghana and EASRA Other MOUs have been signed with the Financial Reporting Centre (FRC) and the Unclaimed Financial Assets Authority (UFAA)

Deeper, more liquid domestic markets

No.	Action	Short term	Medium term	Long term	Status as at 30th April 2016
4.1.1	Introduce arrangements for market making in the equities market				Draft policy and regulatory framework for Securities Lending and Borrowing (SLB) which will form the foundation of market making has been developed and policy submissions to support tax neutrality in SLB transactions submitted to the National Treasury on March 31, 2016.
4.1.2	Introduce market making arrangements for the Government bond market				Guidelines for Government Securities Market Makers (GSMM) is under review for refinement by WG2 Bond Market Steering Committee has been reconstituted to address all issues with regards to development of Fixed Income Securities Market The members of the Kenyan Bond Market Association (BMA) with market-making capacity have commenced engagements with the Authority on the process of establishing a self-regulatory organization (SRO) that will be the market operator for the Over the Counter (OTC) trading and trade reporting infrastructure
4.1.3	Develop regulations to allow for short selling				Draft policy framework for SLB and short selling which will form the foundation for short selling has been developed and is being reviewed by a subcommittee of the BMSC

4.1.4	CMA to provide explicit recognition for SLB				Draft Amendments to the Capital Markets Act submitted to the National Treasury to recognize SLB as a unique transaction under the definition of Securities in Memorandum of Policy Submissions on March 31, 2016. The submissions also included proposals for the treatment of taxation and accounting of SLB in line with International Financial Reporting Standards (IFRS)
4.1.5	Regulators to change investment guidelines to permit SLB				It is a medium term activity. However, discussions with the Retirement Benefits Authority and the Insurance Regulatory Authority to review investment guidelines to permit SLB have been initiated
4.1.6	CDSC to put into place necessary technical arrangements to allow for SLB				It is a medium term activity. However, the process of acquiring a new system with SLB capabilities has been initiated by CDSC
4.1.7	CMA to remove its requirement for pre-funding				Work toward the implementation of this is underway by WG2
4.1.8	NSE to change rules to allow for DMA				NSE revised its rules to allow for sponsored DMA. Policy discussions are underway by WG2.
4.1.9	CMA to introduce rules to allow for block trading				Draft NSE rules for block trading developed.
4.1.10	Implement trading platform for the hybrid bond market				The National Treasury issued an action plan for the operationalization of OTC government bond markets with a target of July, 2016. Aggressive efforts are underway to meet this target including: expansion of scope of Authorized Securities Dealers to cover fund managers; amendment of the Capital Markets Act allow off -Exchange (OTC) bond transactions subject to trade reporting on approved platform; consensus reached on trade reporting infrastructure and market operator to be established in line with the Nigerian FMDQ model and reconstitution of the BMSC to include representatives in a stronger position to facilitate operationalization of OTC bond trading
4.1.11	Implement primary dealer arrangements for Government bonds				Bond Market Steering Committee has been reconstituted to progress implementation of the Government Securities Market Making Arrangements.
4.1.12	NSE to promote listing of international DRs				A draft policy guidance note for GDR/ GDN has been developed

4.1.13	CMA to issue regulations allowing for margin trading				Has been factored within the framework for SLB.
4.1.14	NSE to complete the demutualisation and listing process				On June 27, 2014, the Nairobi Securities Exchange (NSE) received formal approval from the Capital Markets Authority (CMA) to operate as a demutualized entity, launched IPO on 23rd July 2014 and was subsequently self-listed on 9th September 2014
4.1.15	NSE to implement a re-branding strategy				The new brand of NSE was launched on April 7, 2014
4.1.16	Treasury to grant NSE freedom on fee structure				Scheduled for Medium Term.
4.1.17	CMA to ensure approval process for new infrastructures is straightforward and efficient				All approval processes by CMA have been streamlined and requirements published on the website for transparency
4.1.18	NSE to remove any artificial barriers to membership for new participants				Trading Participant access fees for NSE platform reduced to Kshs 25 million from previous Kshs 250 million and Trading Participant Rules also put in place with effect from June 2014 to provide transparent criteria and procedures for admission of new participants
4.1.19	Industry (CMA, NSE and KASIB) to promote the benefits of listing				Continuous: Various initiatives such as county forums, leverage on electronic and print media, forums, open days, road shows, award ceremonies, workshops and use of outsourced resource persons have been implemented jointly by the CMA, NSE and KASIB which promote benefits of listing
4.1.20	CMA to publicise the streamlined listing application procedure				This has been published on the CMA's website
4.1.21	Solicitor General to streamline company registration and compliance				The state law office has taken significant strides toward ensuring that the registration process is more efficient, and that compliance is more stringent. The Companies Act No. 17 of 2015 was assented to by H.E. The President, with several parts effective November 2015.
4.1.22	Review law on foreign ownership capping framework				Revised vide Legal Notice 134 of 2015 to remove the cap with Cabinet Secretary having discretion to prescribe caps on companies deemed to be of national strategic importance. To date no companies have been subjected to any such cap.
4.1.23	Consider GDRs for both equity and debt issues to make them more accessible to international investors				Draft Policy Guidance Note (PGN) developed by WG2
4.1.24	Create KDRs as a potential alternative to creating CSD linkages				

4.1.25	NSE to more actively promote benefits of GEMS listing				4 companies listed on GEMS between July 2013 and December 2014. Recommendations of joint FSD(K)/ CMA/NSE report on SME capital raising and listing such as dedicated marketing function at the NSE already being implemented
4.2.1	CMA to improve rules and regulations relating to financial derivatives market				Consolidated Capital Markets (Derivatives Market) Regulations, 2015 published on the Kenya Gazette in March 2016
4.2.2	CMA to ensure all exchange traded derivatives markets and their clearing arrangements come under its effective remit				Incorporated in the legal and regulatory framework for Derivatives as prescribed by the Capital Markets Act and regulations. A dedicated license in respect of Derivatives Exchange business established with effect from December 2013 and the 3 year exemption granted to Nairobi Securities Exchange under Section 36A of the Capital Markets Act will lapse by end of 2016.
4.2.3	CMA to assess and where appropriate license a suitable provider of a financial futures market which seeks to start operating and up-skill as necessary to provide effective supervision				The NSE granted a license to operate a Derivatives Exchange in October 2015 subject to explicit conditions on raising capacity and resourcing.
4.2.4	CMA to work with the National Treasury to develop a supportive tax framework for the development of the derivatives market				Proposals on appropriate tax treatment for derivatives submitted to and discussed with the Kenya Revenue Authority and included in the formal policy submission to the National Treasury on March 31, 2016

4.2.5	CMA and industry to educate traders and investors on derivatives trading				The Kenya Association of Stockbrokers and Investment Banks (KASIB) has negotiated an MOU with the Chartered Institutes for Securities and Investments (CISI) to support capacity development initiatives on derivatives trading. The Capital Markets Authority has launched a 2 phase industry certification program to be subject to CISI international independent examination. Through the wealth of programs available at CISI intermediaries can take specialization exams in areas including derivatives markets ***Continuous:*** through the investor education strategies of both CMA and NSE
4.2.6	Undertake study of where Kenya has an opportunity to be the international price formation centre (e.g.: Coffee)				Long term initiative
4.2.7	Promote WRS schemes across the country				The Authority has made recommendations to Joint Technical Committee on the Development of Commodities Exchange chaired by State Department of Trade, Ministry of Industry, Development and Trade; the Inter –Ministerial Regional Committee on Trade on the appropriate policy, legal and regulatory framework for commodities exchange and to the taskforce on the development of a spot commodities Exchange in Kenya. A Cabinet Memorandum recommending the vesting of authority to oversee spot commodities exchanges in the CMA has been prepared and is awaiting adoption to inform the submission of necessary statutory amendments to the Capital Markets Act. A Warehouse Receipt Systems Bill with a focus on agricultural commodities has been developed and is currently under consideration by the National Assembly
4.2.8	CMA to be appointed regulator for spot commodity markets				
4.2.9	Provide necessary rules and regulations to allow for the development of spot commodities exchanges				
4.2.10	Develop pool or spot market arrangements for power				***Scheduled for Long term***

4.2.11	Determine regulator for spot power trading arrangements				***Scheduled for Long term.*** However, the Authority has been participating in appropriate forums including the development of a Warehousing Receipting Systems Bill, and Inter-Ministerial Committee on spot commodities exchanges and advocating for implementation of CMMP recommendations in respect of regulation of spot commodities exchanges

International standard market infrastructure

No.	Action	Short term	Medium term	Long term	Status as at 30th April 2016
5.1.1	CDSC to consider expanding existing scope of shareholders to include key users of its facilities				To be considered in the medium term
5.1.2	CDSC Board composition should be restructured to reflect usage and public interest				To be considered in the medium term
5.1.3	CDSC to set its own financial policy subject to competition and consumer protection controls				To be considered in the medium term
5.1.4	CDSC to modernise its systems				Modernization process has been initiated. Proposed systems to be subjected to continuous analysis of capacity and scalability in light of new products such as Securities Lending and Borrowing, ETFS and GDRs
5.1.5	CDSC to review its risk management approach				Some components progressed such as implementation of first phase of settlement in central bank money with effect from February 2015
5.1.6	CDSC to achieve SRO status and move to an outcome-based approach				Scheduled for medium Term.
5.1.7	CDSC to achieve full compliance with the CPSS-IOSCO Principles for Financial Market Infrastructures				CPSS-IOSCO Principles for Financial Markets Infrastructure (PFMI) assessment completed and being implemented in stages by the CDSC
5.1.8	Integrate Government bond and corporate securities in CDSC				Consultancy in place under the World Bank / National Treasury Financial Sector Support Program project to provide recommendations on policy and operational/technical aspects on the consolidation
5.1.9	CDSC to develop services to support the introduction of Stock Lending				The modernized CDSC infrastructure under implementation will support Securities Lending and Borrowing.
5.1.10	CDSC to ensure that there are no barriers to local DRs being issued				Modernization of the systems to accommodate new services and products
5.1.11	CDSC to develop links with other EAC depositories				Scheduled for medium Term.

5.1.12	A central counterparty for cash securities should be considered				Settlement in Central Bank Money already in force as a first measure towards reducing counter party risks.
5.1.13	CDSC should aim to build bilateral connections with Euroclear and Clearstream				The National Treasury has supported initiatives to explore connection with Euroclear through the implementation of their I-link product in Kenya as a first step towards full Euroclearability of Government bonds. A steering committee and technical committee has been set up by the Cabinet Secretary for the National Treasury to engage with Euroclear SA/ NV (Brussels) on the roadmap
5.2.1	Assess the adequacy of the legislative and regulatory framework to support derivatives clearing				The recently published Capital Markets (Derivatives Markets) Regulations, 2015 provides for derivatives clearing requirements
5.2.2	Survey the size of the existing OTC derivatives market in Kenya				TOR developed for a study on the nature and size of on and off exchange derivatives market
5.2.3	Establish a CCP for commodity derivative products (agricultural, energy, power, metals) alongside the development of a commodity market				Scheduled for medium to long Term.
5.2.4	Review the derivatives market structure				Structure reviewed to allow for outsourcing of clearing services
5.2.5	Introduce a CCP for financial derivatives				Licensed derivatives exchanges' settlement infrastructure is expected to follow a CCP model
5.2.6	All CCPs should carry out regular reviews to ensure compliance with CPSS-IOSCO principles				All CCPs are required to comply with CPSS-IOSCO principles

Institutional and capacity building initiatives

No.	Action	Short term	Medium term	Long term	Status as at 30th April 2016
6.1.1	Include financial services in Education Institutions including universities				KICD Financial & Literacy Education Curriculum Strategy Developed. Primary and secondary school matrix for integration of financial literacy approved by the Basic Education Course Panel and the Academic Committee. The curriculum is being piloted in 20 schools and training of teachers was held in February 2016
6.1.2	Assess options for training, examination and certification				The CMA-CISI certification programme was launched in November 2015. Nineteen (19) participants have since been certified.

Sound, responsive regulation and legal frameworks that inspires confidence

No.	Action	Short term	Medium term	Long term	Status as at 30th April 2016
7.1.1	CMA will support progression to full integrated financial regulation				Draft Financial Services Authority Bill (FSA) is targeted to be tabled before the National Assembly in June 2016. The proposed FSA structure will consolidate prudential and conduct supervision of non-bank financial institutions. Policy deliberation on the longer term structure of integrated financial regulation will continue into the longer term.
7.1.2	As steps towards integrated regulation progress the CMA will seek to ensure that the outcomes are optimal from the point of view of achievement of the goals of the Master Plan				CMA is pro-actively participating in the development of the policy, institutional framework, laws and transition arrangements relating to the integration of regulation to ensure that capital markets issues are well addressed.
7.1.3	CMA will play its proper role in ensuring that the arrangements for maintaining financial stability in Kenya as a whole function well at all times				The Authority will continue to engage with the joint Financial Sector Regulators to strengthen modalities for coordination supervision of market stability and the implementation of effective crisis response and resolution frameworks. The Authority led the planning and execution of a crisis simulation exercise by the Toronto Centre in November – December 2015 for all financial sector regulators. CMA provides input into the Financial Stability Report annually With effect from July 2015 CMA Market Development Department has been submitting capital markets specific stability reports to the CMA Board
7.1.4	CMA will consider whether the intent of its development objective would be better met by its replacement by a set of legislative and regulatory principles which would ensure that the regulatory burden was the minimum appropriate				The Authority has secured the revision of the Capital Markets Act to cater for principles based rule making powers exercised through the development and issue of Policy Guidance Notes
7.1.5	CMA will examine the case for amending the law formally to put in place "no-action" arrangements				To be reviewed in the context of the introduction of enforcement undertaking under the proposed FSA Bill

7.1.6	CMA will examine the case for some form of principles-based regulation				The Authority has been granted principles based rule making powers through an appropriate amendment to the Capital Markets Act
7.2.1	As Kenya moves over time to more comprehensive integrated financial regulation the CMA will support a parallel move to an integrated legal framework				The National Treasury has set up Steering Committee and Technical Committee supported by consultants to advise on a multi-phased approach to the integration of regulation beginning with the development and tabling before the National Assembly the Financial Services Authority Bill in June 2016
7.2.2	CMA will conduct a fundamental review of capital market legislation				***Continuous:*** The framework to be reviewed on an ongoing basis but informed by the developments under 7.2.1 above.
7.2.3	CMA will maintain consultation processes in line with international good practice				The Authority subjects or regulatory proposals to a 30 day public and industry consultation process to ensure active engagement of all stakeholders. The Authority also organizes regular sensitization and engagement workshops with industry on emerging risks, trends and priorities
7.2.4	National Treasury and CMA will explore with Parliament the scope for further improvement of process to ensure that capital markets legislation is properly considered with due account taken of public interest arguments.				CMA has re-submitted a memorandum jointly with other financial sector regulators proposing a review of the Statutory Instruments Act in order to support its regulatory mandate. The Authority has also held meetings with the National Assembly Committee on Delegated Legislation to build awareness and understanding of proposed subsidiary legislation
7.2.5	CMA will explore with National Treasury the case for exempting subsidiary financial services legislation from the requirements of the Statutory Instruments Act				
7.2.6	CMA will establish a financial law review panel under its auspices				Nominees identified and engagements with prospective members of the panel commenced
7.3.1	CMA will seek to ensure that the appointment process for board members is in line with emerging best practice and the board will review the skill sets it requires				The CMA Board members have been appointed in line with the emerging best practice and have signed and been independently trained on the Mwongozo Code (the Code for Corporate governance for State Corporations) The Authority submits an analysis of its skills needs to the Cabinet Secretary to the National Treasury to inform appointments

7.3.2	CMA will act on the conclusions of its current review of its human resource requirements and seek to ensure CMA budgets and funding match resourcing needs and stakeholder expectations				***Continuous:*** CMA has continued to enhance its resource capacity through the ongoing Uwezo Kipeo capacity and resource optimization/transformation project that is internationally benchmarked
7.3.3	CMA will seek to ensure its budgets and funding match resourcing needs over time and build in sufficient flexibility to meet stakeholder expectations including those arising from the Master Plan				***Continuous:*** The Authority continues to plan and budget in accordance with the requirements of the Public Financial Management Act including securing budgetary revisions as deemed necessary. In addition the CMA has consistently sought and received technical and funding support from development partners to supplement its revenue sources
7.3.4	CMA will ensure its external communications and outreach demonstrate careful thought leadership and that it maintains reasonable response times				***Continuous:*** Communication Strategy Policy developed and is being reviewed to incorporate communication in crisis management
7.3.5	CMA will ensure adequate access to external expert advice				***Continuous:*** The Authority has continued to engage external expertise whenever appropriate

Improved corporate governance and financial reporting

No.	Action	Short term	Medium term	Long term	Status as at 30th April 2016
8.1.1	CMA will continue to pursue its existing work programme on corporate governance covering both the corporate governance code itself and education in good corporate governance				The Code for Corporate Governance for Issuers of Securities to the Public was published in the Kenya Gazette of 4th March 2016.
8.1.2	CMA will undertake a review of the different ways in which good corporate governance can be achieved in practice and will act on its findings				The draft Stewardship Code was submitted to the National Treasury in December 2015 and is awaiting Gazettement.
8.1.3	NSE to develop a corporate social sustainability and responsibility index				To be progressed during medium term
8.2.1	CMA will review the arrangements for the enforcement of the sound financial reporting of listed companies, including the legal basis and the adequacy of resourcing				Proposals submitted to National Treasury to strengthen the requirements on the scope of disclosures to the Authority by listed companies in addition to introducing more specific conditions and requirements on auditors of listed entities

8.2.2	CMA will support ongoing work with the National Treasury to move forward with the speedy establishment of an independent Kenyan auditor oversight regulator in adherence to the Core Principles of IFIAR				The Authority continues to engage the National Treasury on the establishment of an accelerated timetable to put in place an independent audit oversight authority

Innovative open and competitive market

No.	Action	Short term	Medium term	Long term	Status as at 30th April 2016
9.1.1	Review market infrastructure membership criteria				Trading Participant access fees for NSE platform reduced to Kshs 25 million from previous Kshs 250 million and Trading Participant Rules also put in place with effect from June 2014 to provide transparent criteria and procedures for admission of new participants
9.2.1	Phased liberalization of financial policies for firms and infrastructure providers				Scheduled for Medium Term
9.3.1	CMA should keep the Competition Authority advised of moves to liberalise markets				The Competition Authority is represented in the CMMP working groups.
9.3.2	CMA should work with policy makers to ensure that appropriate frameworks for Consumer Protection are put in place.				Provisions for consumer protection for consumers of financial products and services included in the Financial Services Authority Bill with an increased move towards the design of a robust market conduct framework

Performance Monitoring

Performance monitoring is essential to achieving the objectives of the Capital Market Master Plan and can be broadly measured in terms of the:

- Timeliness of implementation
- Effectiveness of implementation

Performance monitoring is aimed at ensuring that the actions contained in the Master Plan are implemented within the stipulated timeframes to achieve the vision set for the Kenyan capital markets. Any delays or deviation from the actions set out in this document will be reviewed by the Implementing Steering Committee and taking into account what effect these will have on other dependent actions.

Further to monitoring the timely completion of the actions contained in the Master Plan, it is important to monitor performance against specific targets and measures to assess the effectiveness of implementation.
To this end, the section above has identified a series of measures to be used in assessing the performance of implementation of the actions made.

In addition, there are broad market indicators that are relevant to tracking the growth of the capital market as a whole and the primary and secondary markets in particular. These include:

Equity indicators	Fixed income indicators	Other markets	Generic indicators
· Equity market capitalisation to GDP · Ratio of equity market turnover to market capitalization · Number of GEMS listings	· Corporate bond market capitalisation to GDP · Ratio of corporate bond market turnover to market capitalization	· Exchange-traded financial derivatives: value of contracts outstanding · Assets under management in CIS by fund managers in Kenya · Islamic finance target	· Percentage of county financing raised through capital markets · Percentage of infrastructure investment funded by equity, bonds and private equity · MSCI rating · GFCI ranking

As part of performance monitoring these indicators should be measured on a periodic basis. Where possible, comparisons with frontier and other emerging market peers should be drawn to judge performance relative to other competing jurisdictions. Initially, this peer group could include:

Frontier market peers	Emerging market peers
· Argentina · Croatia · Mauritius · Nigeria · United Arab Emirates	· Colombia · Egypt · Indonesia · Mexico · Morocco · Peru · Philippines · Poland

Note: This peer group was determined as part of the market assessment conducted prior to the Capital Market Master Plan and includes markets with a market capitalization greater than 28% (and up to 54%) and with a turnover ratio of 6% (and up to 50%).

Over time, and as the capital markets develop more substantively, the Implementation Steering Committee should revise the composition of this peer group.

Though tracking performance across these broad indicators is useful to gauge performance and development over time, achievement of a certain indicator or group of indicators does not necessarily imply achieving IFC or Emerging Market status. Performance monitoring should thus be broadened to consider other indicators that are considered by rating organisations such as MSCMI or The Z/Yen Group.

MSCI criteria for an Emerging Market	
Size and liquidity requirements	Three companies meeting the following Standard Index Criteria: · Company size (full market cap) – USD 898 million · Security size (float market cap) – USD 449 million · Security liquidity – 15% average turnover ratio

Market efficiency criteria	Openness to foreign ownership: · Investor qualification requirement · Foreign ownership limit level · Foreign room level · Equal rights to foreign investors
	Ease of capital inflows: · Capital flow restriction level · Foreign exchange market liberalization level
	Efficiency of the operational framework: · Market entry o Investor registration and account set up · Market organisation o Market regulations o Competitive landscape o Information flow · Market infrastructure o Clearing and settlement o Custody o Registry/ depository o Trading o Transferability o Stock lending o Short selling
	Sustainability of the institutional framework

Source: MSCI

Z/Yen Group Global Financial Centre Index (GFCI) criteria	
People related factors	· Visa restrictions · Purchasing power · Quality of living
Business environment related factors	· World Bank Ease of Doing Business · Operational risk ratings · City economic growth
Market access related factors	· World Federation of Exchanges capital market indicators · Domestic credit provided by banking sector · Banks' external net position · Linear shipping connectivity
Infrastructure related factors	· Office occupancy costs · Global property index · Quality of roads and telecommunications
Competitiveness related factors	· Global competitiveness index · Global innovation index · FDI confidence

Source: Z/Yen Group

These indicators are not necessarily all quantitative and are based on qualitative assessments provided by market participants. It is thus important for the Implementation Committee to work closely with the likes of MSCI and Z/Yen Group to identify the basis for any qualitative measurement with a view toward identifying ways of improving Kenya's ranking.

Communication Programme

A coordinated communication program for the Master Plan is necessary given the need to generate broad awareness and understanding of the objectives, vision and actions contained in this document. This awareness needs to be communicated to international and domestic stakeholders, both public and private. Ensuring domestic stakeholders understand the content of the Master Plan is particularly important in view of the key role that market participants will play in ensuring the successful implementation of the actions.

The main objectives of the communication program are thus to:

- Create awareness amongst the relevant stakeholders of the objectives and strategic initiatives of the Master Plan;
- Establish clear communication and feedback channels with all the relevant interest groups and industry associations;
- Ensure that information about the Master Plan and updates on the progress of implementation are disseminated in a timely and consistent manner; and
- Enhance the transparency of the implementation process and ensure the accountability of the stakeholders involved.

In terms of audience, the primary audience for this communication will be parties that are directly or indirectly affected by the actions contained in the Master Plan.

These include the general public, domestic and foreign investors and intermediaries, existing and prospective issuers, financial market infrastructure, other financial sector regulators, industry associations, professional bodies and the local and international media.

In terms of process, communication will be made through the following channels:

- Press releases and other communiques issued by CMA and the Vision 2030 Secretariat (and the Implementation Committee);
- Updates posted on the CMA and Vision 2030 websites;
- Briefings, seminars, forums and conferences directed at specific audiences such as domestic or foreign investors or industry groupings; and
- Guidance notes or information circulars issued to industry groups or other stakeholders as necessary.

In addition to this communication, CMA will continue to consult affected stakeholders at least every two years to obtain their feedback and input throughout the course of implementation of the Master Plan. Before major actions are implemented, consultation papers will be published by CMA and the public and affected parties will be invited to submit their comments and feedback on key proposals made therein.

SCHEDULE OF ACTIONS

This section lists all the actions recommended in the body of the report above and provides, for each action:

- The title of the action itself;
- More details about the action (if necessary);
- The implementation activities;
- Which organisation is ultimately responsible for delivery of the action;
- The expect result of the action;
- How the success of the action should be measured and what constitutes success; and
- Timing, particular importance (indicated as 'Important') and any dependencies.

I. SUPPORT DEVELOPMENTAL AND ECONOMIC TRANSFORMATION

1. DOMESTIC MARKET ACCESSIBILITY AND PROSPERITY

1.1. Stimulate Devolved domestic prosperity

Action	1.1.1. - **CMA will identify and analyse the funding gap at national and county level to inform product and service development**
Details	As set out in Master Plan
Implementation	CMA will draw up a specification for a study, explore who would be best placed to undertake it (e.g. a university), estimate resource requirements and how they might be financed and then seek to have the study undertaken. The CMA will take account of comparable studies undertaken internationally
Responsibility	WG1
Result	Reliable analysis of publicly available information available to form the basis for private sector, regulatory and Government policy making
Measurement	Delivery first of the specification and resourcing need by mid-2014, appointment of analysts by end-2014 and then of the analysis by end 2015
Priority / Dependencies	Short term and ongoing (in the medium term to define more specific, county level indicators)

1.2. Address devolution funding needs

Action	1.2.1. - **CMA to host forums on county financing needs strategies**
Details	CMA to facilitate discussion between counties, National Treasury, venture capital, private equity and fund managers to develop range of products for potential investors and to develop plan for reform of public financial management law to make them possible
Implementation	CMA with National Treasury, county representatives, venture capital, private equity, fund managers
Responsibility	Short term – WG1 to arrange forums Medium term – Implementation Committee to address conclusions/findings of the forums
Result	Development of financing products for counties and accompanying regulatory structure
Measurement	Value of capital market financing by counties
Priority / Dependencies	Short term (host forums) Medium term (design of relevant frameworks and implementation of actions)

Action	**1.2.2. – CMA to partner with relevant stakeholders to develop an adequate legal and regulatory framework**
Details	CMA to work with National Treasury and other stakeholders to develop adequate legal framework both at the national and county level to support financial sector growth; that is, the legal framework should provide a platform for fiscal and financial stability at the counties.
Implementation	CMA with National Treasury, county representatives, venture capital, private equity, fund managers
Responsibility	Short term – WG1 to arrange forums Medium term – Implementation Committee to address conclusions/findings of the forums
Result	Development of financing products for counties and accompanying regulatory structure
Measurement	Value of capital market financing by counties
Priority / Dependencies	Short term (host forums) Medium term (design of relevant frameworks and implementation of actions)

1.3. Enhance consumer education and literacy

Action	**1.3.1. - CMA to support the development of a national consumer financial education policy and strategy**
Details	A framework (including a national committee and strategy) for collaboration and co-ordination of financial sector stakeholders around consumer financial education; Recommending the allocation of funding for consumer financial education programmes and initiatives; Key performance indicators, data and measurement of consumer financial education programmes to determine whether policy and programme goals are being achieved; and, Advising on the development of broad-based curricula and materials. The lower the age at which financial education commences, the sounder will be the longer term outcomes. Balanced against this is the need to achieve rapid results, which points to targeting those just at the point of entering the labour force.
Implementation	CMA working with Implementation Committee, other regulators, financial industry to form national committee and develop strategy - potential for input under CityUK MOU
Responsibility	WG1
Result	National committee formed in short term and financial education policy is in place in medium term
Measurement	n/a
Priority / Dependencies	Medium Term Important

Action	**1.3.2. - CMA to continue its own education programme**
Details	CMA continues its current education programme
Implementation	CMA
Responsibility	WG1
Result	Increase in level of consumer education
Measurement	Bi-annual Impact Assessment Survey
Priority / Dependencies	Ongoing Important

2. GATEWAY FOR REGIONAL AND INTERNATIONAL CAPITAL FLOWS

10.1. Leverage East Africa as an integrated market

Action	2.1.1. - Support discussion on regional financial integration
Details	CMA will promote continued discussion within Kenya and within the EAC to arrive at a common view as to the ultimate destination for the East African single market in financial services and on the optimum phasing, including timing, of the steps necessary to achieve this goal for the capital markets
Implementation	CMA to engage with Treasury, other national regulators and with other EAC regulators and agree on objectives and phasing. Short term. Implementation of steps dependent on negotiations with other EAC jurisdictions
Responsibility	WG4
Result	Delivery of an agreed common vision of the EA single market in financial services and full implementation of a single capital market
Measurement	Progress to be measured regularly by Implementation Committee and guidance given on future priorities and further steps (Medium term)
Priority / Dependencies	Ongoing

Action	2.1.2. - **Develop creative products that promote investor comfort in regional products**
Details	Implementation Committee to collect proposals from market players for financial products promoting regional investment and develop plans to promote them
Implementation	Item to be discussed regularly at Implementation Committee
Responsibility	Implementation Committee
Result	Development of new products
Measurement	Number of new products introduced
Priority / Dependencies	Ongoing

Action	2.1.3. - **Support regional financial market infrastructure linkages**
Details	NSE and CDSC are already involved in developing linkages with exchanges and depositories in other EAC countries. These may need support in the form of links to payment systems, regulatory approvals, legislative support and funding.
Implementation	CMA working with NSE, CDSC, CBK and National Treasury
Responsibility	WG4
Result	Exchange and CSD linkages with other EAC countries
Measurement	Number of cross-border trades and settlements Number of new regional products issued
Priority / Dependencies	Medium term

2.2. Capital Market Financing for Kenya's Core Strengths

Action	2.2.1. - **Review obstacles to raising finance for infrastructure projects**
Details	Implementation Committee to commission a review of institutional, legal, regulatory and tax obstacles to raising finance for infrastructure projects
Implementation	Review commissioned by Implementation Committee followed by proposals for action - potential for input under The CityUK MOU
Responsibility	Implementation Committee
Result	Plan to remove barriers
Measurement	Level of financing for infrastructure projects
Priority / Dependencies	Short term Important

Action	2.2.2. - **Assist potential infrastructure issuers in coming to market**
Details	CMA to organise support in the form of technical assistance for potential infrastructure issuers, following the example of support provided under the ESMID programme
Implementation	CMA with support from IFC or donors
Responsibility	WG1
Result	Infrastructure issuers are able to access the market
Measurement	Funds raised for infrastructure projects
Priority / Dependencies	Short term Important following 2.2.1

Action	2.2.3. - **Implement actions contained in the World Bank/IFC report on mutual funds**
Details	Report published in March 2013 identified barriers to development of investment funds in Kenya and proposed changes to legal, regulatory, tax and institutional arrangements to support development of the market
Implementation	CMA to work with National Treasury and leading fund management groups to develop and implement plan for removing barriers
Responsibility	WG1
Result	More rapid growth in investment funds in Kenya
Measurement	Number of funds and value of assets under management
Priority / Dependencies	Short term Important

Action	2.2.4. - **Examine the tax structure of collective investment scheme products**
Details	Implementation Committee to commission report on tax structure of collective investment scheme products and potential deterrents to their use by individuals and institutional investors
Implementation	Implementation Committee to commission report and work with National Treasury and KRA to address issues identified - potential for input under CityUK MOU
Responsibility	Implementing Committee
Result	Greater use of CIS products
Measurement	Value of assets under management
Priority / Dependencies	Medium term

Action	2.2.5. – **Create a regulatory framework for Islamic capital markets**
Details	This will include developing capacity within financial sector regulators (and the Kenya Revenue Authority) to regulate Islamic capital markets
Implementation	CMA, with other regulators, to review needs for further development. Short term. Potential for input under CityUK MOU
Responsibility	WG3
Result	The capital market regulatory and legislative framework provides for Islamic capital market products
Measurement	Islamic finance included in updated capital market legislation
Priority / Dependencies	Short term Important

Action	2.2.6. - **Develop a separate policy, legislative and regulatory framework for Islamic products and services**
Details	This will include: · Put in place an Islamic standard setting body. Develop (and give legal recognition to) a single national Sharia advisory board or council - to provide guidance on product authenticity through screening and qualification for the entire Islamic finance industry. This body would set rules, guidelines and policies for all subsectors of the Islamic finance industry. The Sharia board will be able to review the investment framework for Islamic finance in terms of permissible products and other requirements governing investment by Islamic finance providers. · Create an Association of Islamic Financial Institutions to act as a champion for the entire industry (with membership from banks, insurance providers, fund managers and SACCOs that provide Islamic financial products and services). This new Association needs to be recognised in regulation. · Give recognition to those standards: regulation to Islamic-based accounting and auditing standards. · CMA to facilitate approval by ICPSAK and for Islamic experts to single out issues and channel issues to ISB to make amendments
Implementation	
Responsibility	Implementation Committee
Result	The CBK, IRA, RBA, CMA, SASRA, KRA recognise Islamic products and services in their respective legislative frameworks
Measurement	Islamic products and services covered in each piece of financial sector regulation
Priority / Dependencies	Medium term

Action	2.2.7. – **Leverage existing relationships to develop Islamic finance expertise**
Details	Discuss with other bodies both nationally and internationally to see if they can help provide the level of expertise required for the effective development and regulation of Islamic produced
Implementation	Contact LSE, Central Bank of Malaysia to identify potential support to leverage existing CMA and Central Bank relationships
Responsibility	Implementation Committee
Result	The Implementation Committee receives support from LSE and/or the Central Bank of Malaysia
Measurement	
Priority / Dependencies	Ongoing

Action	2.2.8. – **Identify and make policy proposals to facilitate development of Islamic finance in the annual Memorandum of Policy Proposals to the National Treasury and implement programmes through industry coordination and relevant partnerships**
Details	Islamic capital markets need to be recognised in the legislation governing capital markets (among other financial services sub-sectors)
Implementation	Policy actions such as this need to be approved by the National Treasury and hence need to be included in CMA's annual Memorandum of Policy Proposals to Treasury which sets out its policy proposals for the current year. Annual programmes discussed and agreed with stakeholders should also be rolled out.
Responsibility	WG3
Result	2014 CMA budget to National Treasury includes a strategy for Islamic finance
Measurement	Included in 2014 budget and programmes implemented annually
Priority / Dependencies	Short term

3. PROVIDING ACCESS TO INTERNATIONAL FINANCIAL MARKETS

3.1. Alignment with NIFC

Action	3.1.1. - **Implementation Committee, together with other relevant authorities, should establish a process for monitoring progress in international rankings**
Details	MSCI and Z/Yen publish the criteria used in ranking markets as frontier/emerging markets and as financial centres respectively. Implementation Committee should establish an annual exercise to review Kenya's performance against these criteria and plan actions to remedy weaknesses
Implementation	Implementation Committee to monitor progress in relation to each of the criteria used, agree action plans to address them and engage with MSCI and Z/Yen to ensure progress is recognised
Responsibility	Implementation Committee
Result	Kenya progresses to emerging market status and enters and moves up the ranking of global financial centres
Measurement	Market status and GFCI ranking
Priority / Dependencies	Ongoing

Action	3.1.2. - **CMA to be represented on the Steering Committee of the NIFC**
Details	CMA to join NIFC Steering Committee in order to ensure full alignment of both NIFC and CMMP work programmes under Vision 2030
Implementation	CMA to discuss with National Treasury how to effect this
Responsibility	Implementation Committee
Result	Removal of risk of conflicting outcomes of NIFC and CMMP implementation and maximisation of benefits of both
Measurement	
Priority / Dependencies	Short term Important

3.2. Advocate for an attractive business environment

Action	3.2.1. - **Kenya to take action to raise its AML/CFT rating**
Details	CMA to contribute to the steps Kenya needs to take materially to upgrade its current poor rating by implementing the Action Plan set out by the Financial Action Task Force (FATF)
Implementation	All relevant agencies to take steps required by the FATF Action Plan. CMA to take any necessary steps within its own regulatory responsibilities
Responsibility	WG4
Result	Acceptable assessment by FATF
Measurement	Implementation Committee to monitor progress
Priority / Dependencies	Short term Important

Action	3.2.2. - **Extend Kenya's network of Double Taxation Agreements while managing risks of investment practices such as transfer pricing.**
Details	Kenya needs to have in place Double Taxation Agreements with all countries that are significant potential investors. However, measures must be put in place to ensure that tax payers do not use the Double Taxation window to evade payment of tax.
Implementation	Implementation Committee to identify priority list of countries and then KRA to put DTAs in place
Responsibility	WG4
Result	Improved ability of foreign investors to reclaim tax
Measurement	Increase in inward foreign investment
Priority / Dependencies	Medium term

Action	3.2.3. - **Ensure Kenya adopts OECD standards wherever possible**
Details	Kenya should adopt the standards set out in the OECD's Treaty Relief and Compliance Enhancement (TRACE) for cross-border portfolio income tax relief – Implementation Committee to review
Implementation	KRA
Responsibility	WG4
Result	Easier tax reclaims by foreign investors
Measurement	Increase in inward foreign investment
Priority / Dependencies	Medium term

Action	3.2.4. - **Ensure standards for information exchange on taxes are in line with requirements of OECD Global Forum on Transparency and Exchange of Information for Tax Purposes**
Details	Bring domestic arrangements into line with OECD Global Forum requirements
Implementation	KRA
Responsibility	WG4
Result	Avoidance of potential black-listing
Measurement	Move to full compliance under Phase 2
Priority / Dependencies	Medium term

Action	3.2.5. - **Ensure personal and corporate taxes are attractive to internationally mobile employers and employees**
Details	Implementation Committee to commission review of personal and corporate tax rates and structures to assess their impact on the willingness of foreign companies and individuals to locate in Kenya and propose changes based on result of the review
Implementation	Implementation Committee working with National Treasury, KRA and the NIFC - potential for input under The CityUK MOU
Responsibility	Implementation Committee
Result	Kenya is an attractive location for financial firms and individuals
Measurement	Increase in inward investment and relocation by individuals
Priority / Dependencies	Medium term

Action	3.2.6. - **Review the adequacy of the corporate and personal tax framework for financial services**
Details	Implementation Committee to commission review of how the tax code is adapted to financial instruments and participants in financial markets and propose changes based on the result of the review.
Implementation	Implementation Committee working with National Treasury and KRA - potential for input under CityUK MOU
Responsibility	Implementation Committee
Result	Financial services are comfortably accommodated in the tax code
Measurement	n/a
Priority / Dependencies	Medium term

3.3. Establish and develop international linkages

Action	3.3.1. - **Put in place Regulatory MoUs to allow for the exchange of confidential information (CMA)**
Details	As foreign institutions establish themselves in Kenya or Kenyan institutions establish themselves abroad, the CMA needs to put in place MOUs with the relevant foreign regulators to permit the bilateral exchange of confidential supervisory information
Implementation	In line with establishment of institutions
Responsibility	WG4
Result	MOUs in place
Measurement	n/a
Priority / Dependencies	Ongoing

II. THE INFRASTRUCTURE OF THE MARKETS

4. DEEPER, MORE LIQUID MARKETS

4.1. Enhance Securities markets

Action	4.1.1. - **Introduce arrangements for market making in the securities market**
Details	Make arrangements for qualifying entities to provide continuous two way prices for individual stocks
Implementation	· NSE to develop rules and contracts for market making with the broking community · CMA to approve rules for market making and to introduce any necessary regulations and guidelines · NSE to make any necessary changes to trading and surveillance systems · NSE to contract market making services with brokers
Responsibility	WG2
Result	Market making introduced for a range of NSE traded securities
Measurement	Tangible improvement in liquidity of stocks subject to market making
Priority / Dependencies	Short term

Action	4.1.2. - **Introduce market making arrangements for the Government bond market**
Details	Make arrangements for certain member firms to provide continuous two way prices for individual bonds
Implementation	BMA & CBK to develop rules and contracts for market making CMA to approve rules for market making and to introduce any necessary regulations and guidelines
Responsibility	WG2
Result	Market making introduced for a range of Government bonds
Measurement	Market making introduced for a range of Government bonds
Priority / Dependencies	Short term

Action	4.1.3. - **Develop regulations to allow short selling**
Details	To develop the legal framework to provide for short selling in Kenya
Implementation	CMA to draft regulations allowing for short selling
Responsibility	WG3
Result	Short selling is allowed in Kenya
Measurement	Increased liquidity
Priority / Dependencies	Short term Dependent on pre-funding requirement (4.1.7)

Action	4.1.4. - **CMA to provide explicit recognition for SLB**
Details	To make legal provisions allowing SLB in Kenya
Implementation	CMA to develop regulations to allow for SLB
Responsibility	WG3
Result	SLB introduced
Measurement	Liquidity improved due to SLB
Priority / Dependencies	Short term Dependent on CDSC implementing necessary system change

Action	4.1.5. - **Regulators to change investment guidelines to permit SLB**
Details	Each of the regulators responsible for issuing investment guidelines for the organisations they regulate to make changes so that these organisations can put up stock for borrowing
Implementation	IRA, RBA and CBK to consult with regulated firms on SLB IRA, RBA and CBK to make changes to its investment guidelines to permit SLB
Responsibility	WG3
Result	Investment guidelines in place
Measurement	IRA, RBA and CBK regulated firms make stock available for SLB
Priority / Dependencies	Medium term

Action	4.1.6. - **CDSC to put in place necessary technical arrangements to allow for SLB**
Details	With the introduction of stock lending, investors will be able to allocate all or part of their holdings at CDSC to a lending pool. Market participants (not restricted to market makers) will be able to borrow stock from this pool for a fee paid to the holders. The borrowed stock can be used to meet delivery obligations resulting from short selling
Implementation	CDSC to put the necessary technical arrangements in place to support SLB CDSC to develop the rules, procedures and contracts needed to support SLB CMA to approve rules and procedures for SLB
Responsibility	WG2
Result	SLB introduced at NSE
Measurement	Active use of the service by market makers and other market participants resulting in increased business
Priority / Dependencies	Medium term Dependent on CMA regulations for SLB

Action	4.1.7. - **CMA to remove its requirement for pre-funding**
Details	
Implementation	CMA to consult on removing requirement for pre-funding CMA to develop and implement updated regulations NSE to change rules CDSC to change rules and practices
Responsibility	WG3
Result	Pre-funding requirement removed
Measurement	Increase in liquidity following change
Priority / Dependencies	Short term

Action	4.1.8. - **NSE and other exchanges to issue rules to allow for DMA**
Details	NSE to develop rules governing Direct Market Access activities
Implementation	NSE to change and publish rules NSE promotes DMA to its member firms
Responsibility	WG2
Result	DMA allowed
Measurement	Overseas firms use DMA functionality
Priority / Dependencies	Short term

Action	4.1.9. - **CMA to introduce rules to allow for block trading**
Details	CMA to make rules governing block trading
Implementation	CMA to implement rule changes allowing block trading
Responsibility	WG3
Result	Rules changed
Measurement	Block trading under new rules takes place
Priority / Dependencies	Short term

Action	4.1.10. - **Implement platform for the hybrid bond market**
Details	There are now rules and regulations in place to allow for trading of bonds between Approved Securities Dealers (ASDs). This trading can be enhanced by the introduction of a dedicated electronic bond trading platform
Implementation	CMA to determine requirements for the platform CMA to issue RFP and choose system CMA to implement system
Responsibility	WG2
Result	Electronic platform for bond trading and reporting implemented
Measurement	Tangible increase in bond trading activity
Priority / Dependencies	Short term Important

Action	4.1.11. - **Implement primary dealer arrangement for Government bonds**
Details	To introduce primary dealers for Government bonds
Implementation	NT through CBK to make changes to law and regulations to allow for primary dealers NT to publish procedures for the operation of a primary dealer arrangement NT to approve primary dealers
Responsibility	WG3
Result	Primary dealer arrangement in place
Measurement	5 firms become primary dealers
Priority / Dependencies	Short term Important

Action	4.1.12. - **NSE to promote listing of international DRs**
Details	The creation of depositary receipts of international companies that would be listed on the NSE. Such DRs are created by investment banks
Implementation	NSE to promote benefits to investment banks Investment banks create necessary DRs CMA/NSE approves DRs for listing
Responsibility	WG2
Result	International DRs listed on NSE
Measurement	Trading in international DRs on NSE
Priority / Dependencies	Short term

Action	4.1.13. - **CMA to issue regulations allowing margin trading**
Details	CMA to make legal provision to govern margin trading
Implementation	NSE and its member firms to draw up rules and procedures for margin trading CMA to create the necessary regulations and guidelines to allow for margin trading NSE/CMA/CDSC develop tools for monitoring extent of margin trading for supervisory purposes
Responsibility	WG3
Result	Margin trading launched in the Kenyan market
Measurement	Increase in liquidity resulting from allowing margin trading
Priority / Dependencies	Short term

Action	4.1.14. - **NSE to complete the demutualisation and listing process**
Details	• Self-listing of the NSE • Improve infrastructural and human resource capacity of NSE • Strengthen the SRO function of NSE as an institution
Implementation	NSE to finalise self-listing
Responsibility	WG2
Result	NSE listed as an independent company on the NSE
Measurement	NSE demonstrates it is independent
Priority / Dependencies	Short term Important

Action	4.1.15. - **NSE to implement a re-branding strategy**
Details	NSE to take the opportunity on demutualisation and listing to re-brand itself to demonstrate its commitment to Kenya as a whole and that it is making a break from the past
Implementation	NSE to review options and undertake the necessary branding exercise
Responsibility	WG2
Result	NSE re-brand
Measurement	NSE re-branded
Priority / Dependencies	Short term

Action	4.1.16. - **National Treasury to grant NSE freedom on fee structure**
Details	The fee structure to be liberalised
Implementation	CMA to draft the necessary changes to its regulations and obtain Treasury approval to implement the same, subject to competition and consumer protection controls
Responsibility	WG3
Result	NSE is able to determine its own fee structure
Measurement	NSE fees structure is accepted by the industry and not subject to challenges by the Competition Authority
Priority / Dependencies	(Medium term) Dependent on NSE demutualisation and listing

Action	4.1.17. - **CMA to ensure approval process for new infrastructures is straightforward and efficient**
Details	In the interests of effective competition it is important that new suppliers of exchange and clearing infrastructure be permitted to operate in Kenya (assuming they meet the necessary criteria). CMA should ensure that the approval process for such new infrastructures is straightforward and efficient. This should include an SLA for the process.
Implementation	CMA to review its approval procedures and modify as necessary
Responsibility	WG3
Result	Any new infrastructure is approved in accordance with the SLA
Measurement	More capital markets infrastructure implemented in Kenya
Priority / Dependencies	Short term

Action	4.1.18. - **NSE to remove any artificial barriers to membership for new participants**
Details	Any firm meeting reasonable participation requirements can join NSE at a reasonable, non-discriminatory price
Implementation	NSE to publish non-discriminatory admission criteria CMA to approve admission criteria
Responsibility	WG2
Result	Publication of admission criteria
Measurement	New firms admitted to NSE
Priority / Dependencies	Short term Important

Action	4.1.19. - **Industry (CMA, NSE and KASIB) to promote the benefits of listing**
Details	Companies in Kenya need to be made not aware of the benefits of seeking a listing on NSE. An ongoing, coordinated campaign of education will assist the effort to facilitate more listings
Implementation	CMA to coordinate an education program with NSE and KASIB NSE & KASIB to promote the program to their members Members of NSE & KASIB to educate potential companies
Responsibility	WG2
Result	Coordinated educational campaign is launched and maintained over several years
Measurement	Increase in number of companies seeking listing
Priority / Dependencies	Ongoing

Action	4.1.20. - **CMA to publicise the streamlined listing application procedure**
Details	To streamline listing application procedure
Implementation	CMA to ensure potential companies for listing, advisors and intermediaries know about the streamlined application procedure
Responsibility	WG3
Result	Wide knowledge in the industry of the procedures
Measurement	More listings
Priority / Dependencies	Ongoing

Action	4.1.21. - **Solicitor General to streamline company registration and compliance**
Details	
Implementation	CMA to consult with the industry on changes required CMA to propose changes to the Solicitor General Solicitor General to implement changes
Responsibility	WG3
Result	Updated Companies Act
Measurement	More listings
Priority / Dependencies	Long term

Action	4.1.22. - **Review law on foreign ownership capping framework**
Details	The law to be changed to remove the blanket ownership ceiling which can unnecessarily inhibit foreign investment and replace it with other methods to achieve the policy objectives of ensuring Kenyan participation in the market and protection of strategically important companies
Implementation	CMA to initiate debate on the matter CMA to draft law changes CMA to implement regulations following law change
Responsibility	WG3
Result	Law changed and blanket 75% foreign ownership capping framework reviewed to make it more responsive to the overarching national policy objectives
Measurement	Greater foreign participation in the Kenyan market Achievement of MSCI emerging status by medium term
Priority / Dependencies	Medium to Long term Important

Action	4.1.23 - **Consider GDRs and GDNs for both equity and debt issues to make them more accessible to international investors**
Details	Promote GRDs and GDNs in the Kenyan market
Implementation	Implementation Committee to investigate idea and promote with potential investment banks who can facilitate this
Responsibility	WG2
Result	GDRs and GDNs listed in London or New York
Measurement	First GDR and GDN listed in London or New York
Priority / Dependencies	Short to Medium term

Action	4.1.24 - **Create KDRs as a potential alternative to creating CSD linkages**
Details	Develop and promote KDR
Implementation	Investigate idea and promote with potential investment banks who can facilitate this
Responsibility	WG2
Result	KDRs listed at NSE
Measurement	First KDR listed at NSE
Priority / Dependencies	Medium term

Action	4.1.25. - **NSE to more actively promote benefits of GEMS listing**
Details	Promote GEMS listings
Implementation	NSE to undertake campaign to make the ease of listing and benefits of listing on GEMS well known to advisors, intermediaries and companies suitable for listing
Responsibility	WG2
Result	More listings on GEMS
Measurement	3-4 GEMS listings per year
Priority / Dependencies	Short term

4.2. Develop SPOT and derivatives markets

Action	**4.2.1. - CMA to improve rules and regulations relating to financial derivatives markets**
Details	Current regulations relating to derivatives markets need dramatic improvement to make them fit for purpose
Implementation	CMA to consult with the industry and outside experts on the changes needed to current regulations and then implement the changes
Responsibility	WG3
Result	New set of derivatives regulations
Measurement	Regulations regarded by experts as fit for purpose
Priority / Dependencies	Short term

Action	**4.2.2. - CMA to ensure all exchange traded derivatives markets and their clearing arrangements come under its effective remit**
Details	It is important that all derivative markets in Kenya come under the supervisory remit of the CMA. Any exceptions to this need to fixed
Implementation	CMA to obtain legislative changes to ensure all derivative markets come under its remit
Responsibility	WG3
Result	All derivatives markets are supervised by the CMA
Measurement	First launched derivative market is regulated by the CMA
Priority / Dependencies	Short term Important Dependent on 4.2.1

Action	**4.2.3. - CMA to asses and where appropriate license a suitable provider of a financial futures market which seeks to start operating and up-skill as necessary to provide effective supervision**
Details	CMA needs the regulations and skills to effectively determine if a financial derivatives market should be authorised and also have the skills to effectively supervise it
Implementation	CMA to up skill as necessary. Rest is dependent on 4.2.1
Responsibility	WG3
Result	CMA has well respected derivatives and risk management staff
Measurement	First launched derivative market is regulated by the CMA
Priority / Dependencies	Short term Important Dependent on 4.2.1. and 4.2.2.

Action	**4.2.4. - CMA to work with the National Treasury to develop a supportive tax framework for the development of the derivatives market**
Details	The derivatives market requires a favourable tax framework that can support its growth
Implementation	CMA to work in collaboration with the National Treasury
Responsibility	WG3
Result	CMA has a favourable tax derivatives framework in place
Measurement	A derivatives tax framework in place
Priority / Dependencies	Short term

Action	**4.2.5. - CMA and industry to educate traders and investors on derivatives trading**
Details	Before a financial futures exchange in launched, and beyond, it is important for traders and investors to understand the risks and the mechanics of derivative markets. Therefore, a solid education process needs to be undertaken
Implementation	Provider of the financial futures exchange to develop educational material CMA to determine suitability of the material Industry (CMA, exchange, member firms) as a whole to undertake the education of traders and potential investors
Responsibility	WG2
Result	Well educated traders and investors
Measurement	Growth of the derivatives markets in Kenya
Priority / Dependencies	Short term Important

Action	**4.2.6. - Undertake study of where Kenya has an opportunity to be the international price formation centre (e.g. Coffee could be a candidate)**
Details	Kenya needs to determine if it has an opportunity to become the price setting centre for an internationally traded commodity
Implementation	Implementation Committee to undertake study or leverage any existing studies
Responsibility	Implementation Committee
Result	Decision on whether or not there is such an opportunity
Measurement	Decision made
Priority / Dependencies	Long term

Action	**4.2.7. - Promote WRS schemes across the country**
Details	A WRS scheme needs to be in place before trading in an agricultural commodity can take place
Implementation	Ministry of Agriculture to actively promote such schemes and discuss with external bodies including funding agencies and potential suppliers of the necessary infrastructure
Responsibility	WG2
Result	WRS schemes put in place
Measurement	First WRS scheme in place
Priority / Dependencies	Medium term

Action	**4.2.8. - CMA to be appointed regulator for spot commodity markets.**
Details	New spot markets need quality and effective regulation. The CMA is best placed to provide this
Implementation	WG3 to lobby Chief of Staff, Office of the President and Ministries of Agriculture and Minerals
Responsibility	WG3
Result	CMA appointed as regulator of spot commodity markets
Measurement	Develop spot market commodity markets
Priority / Dependencies	Medium term

Action	**4.2.9. - Provide necessary rules and regulations to allow for the development of spot commodity exchanges**
Details	Before spot trading can take place on a spot commodity exchange, the necessary rules and regulations need to be developed
Implementation	CMA to discuss with potential operators of such exchanges a suitable regulatory regime
Responsibility	WG3
Result	Rules and regulations created and adopted
Measurement	Rules and regulations published and approved
Priority / Dependencies	Medium term

Action	**4.2.10. - Develop pool or spot market arrangements for power**
Details	Once there is a reasonable number of power suppliers in the country then a pool or spot market trading arrangement could be beneficial for the industry and consumers
Implementation	Ministry of Energy to have discussions with the industry players and outside experts who have experience of such trading systems in order to determine the case for such a market
Responsibility	WG2
Result	Decision made on opening such a market
Measurement	Market opened
Priority / Dependencies	Long term Dependent on existence of multiple, competitive suppliers of power in Kenya

Action	4.2.11. - **Determine regulator for spot power trading arrangements**
Details	Once the opportunity is in place for the trading of spot power, it is necessary to determine the regulatory environment, in order to ensure no gap in the regulatory regime
Implementation	WG3 to lobby Chief of Staff, Office of the President and Ministry of Energy
Responsibility	WG3
Result	Regulator decided upon
Measurement	Regulator in place
Priority / Dependencies	Long term

5. INTERNATIONAL STANDARD FINANCIAL MARKET INFRASTRUCTURE

5.1. Enhance depository and settlement infrastructure

Action	5.1.1. - **CDSC to consider expanding existing scope of shareholders to include key users if its facilities**
Details	Restructure shareholding by encouraging users to become direct rather than indirect shareholders and non-users to sell shares to users so that new shareholding structure reflects usage New owners should inject capital to put CDSC on sound financial footing
Implementation	Management of CDSC with support from CMA
Responsibility	WG2
Result	A new shareholding structure for CDSC
Measurement	Shareholdings reflect usage of CDSC
Priority / Dependencies	Short term

Action	5.1.2. - **CDSC Board composition should be restructured to reflect usage and public interest**
Details	Realign board composition to reflect usage and remove conflicts of interest
Implementation	Management of CDSC
Responsibility	WG2
Result	New Board structure
Measurement	New Board reflects usage of CDSC
Priority / Dependencies	Short term follows 5.1.1.

Action	5.1.3. - **CDSC to set its own financial policy**
Details	CDSC Board takes responsibility for maintaining a sound financial position, setting CDSC financial plan, setting and publishing fee schedule, subject to competition and consumer protection controls.
Implementation	CDSC, CMA
Responsibility	WG3
Result	CDSC is able to fund developments out of its income
Measurement	`Financial stability of CDSC
Priority / Dependencies	Medium term Follows restructuring of ownership and governance

Action	5.1.4. - **CDSC to modernise its systems**
Details	CDSC needs to be able to provide: Full real-time DVP in central bank money STP using SWIFT standards CDSC also ensures removal of other obstacles to provision of services required by international participants (e.g. omnibus accounts, free of payment transfers), whether established by CDSC or another entity.
Implementation	CDSC implements new settlement infrastructure, working with CBK to implement settlement in central bank money
Responsibility	WG2
Result	CDSC provides modern services
Measurement	Modern CDSC systems
Priority / Dependencies	Short term

Action	5.1.5. **- CDSC to review its risk management approach**
Details	CDSC conducts an overall review of its risk exposures and risk mitigation measures to ensure that all potential risks are covered with resources that are proportionate to the size of risk
Implementation	CDSC
Responsibility	WG2
Result	Risk exposures are identified and mitigating measures are proportionate
Measurement	Risk management framework implemented at CDSC
Priority / Dependencies	Medium term Should follow modernisation of systems

Action	5.1.6. **- CDSC to achieve SRO status and move to an outcome-based approach**
Details	CDSC achieves SRO status CDSC sets standards for settlement performance with penalties for firms failing to achieve them CDSC ensures removal of pre-trade requirements (whether set by CDSC or by NSE)
Implementation	CDSC working with CMA and NSE
Responsibility	CDSC with approval from CMA
Result	WG2
Measurement	Improved settlement performance (i.e. percent of transactions settling on due date)
Priority / Dependencies	Medium term

Action	5.1.7. **- CDSC to achieve full compliance with the CPSS-IOSCO Principles for Financial Markets Infrastructures**
Details	CDSC should carry out regular assessments of itself against the CPSS-IOSCO Principles for Financial Market Infrastructures by independent external reviewers and take action to remedy any gaps identified
Implementation	CDSC appoints external reviewer and acts on gaps identified
Responsibility	WG2
Result	Understanding of gaps in compliance with CPSS-IOSCO Principles and reduction in gaps over time
Measurement	Degree of compliance with principles
Priority / Dependencies	Ongoing Repeated annually

Action	5.1.8. **- Integrate Government bond and corporate securities in CDSC**
Details	Ensure CDSC has the capacity to handle all services required for the government bond market Transfer holdings of Government bonds and the location of settlement from CBK to CDSC Review ownership and governance
Implementation	CDSC, CBK, CMA and National Treasury
Responsibility	WG2
Result	Government bond holdings and settlement transferred to CDSC
Measurement	Consolidated CSD for all classes of securities
Priority / Dependencies	Medium term Follows previous actions

Action	5.1.9. **- CDSC to develop services to support the introduction of Stock Lending**
Details	CDSC to investigate possibility of developing services to match borrowers and lenders Support lending by recording open loans, revaluing stock on loan, passing collateral, automatically returning borrowed securities when they are no longer needed and ensuring that benefits, such as dividends, are passed from the borrower to the lender · Implement services where feasible
Implementation	CDSC working with NSE and CMA
Responsibility	WG2
Result	Support for stock lending in Kenya
Measurement	Size of stock lending market
Priority / Dependencies	Medium term Needs to be coordinated with SLB regulation (action 4.1.4.)

Action	5.1.10. - **CDSC to facilitate issuance of local DRs**
Details	CDSC should ensure that there are no legal, technical or other barriers to local DRs being issued into CDSC
Implementation	CDSC
Responsibility	WG2
Result	DRs can be issued into CDSC
Measurement	Number of DR issues
Priority / Dependencies	Short term

Action	5.1.11. - **CDSC to develop links with other EAC depositories**
Details	Initially, CDSC opens accounts with other EAC depositories and enables them to open accounts with CDSC to support free of payment cross-border transfer of securities Subsequently, the accounts are linked to the East African payments system to support DVP transfers
Implementation	CDSC, working with EAC CSDs and Central Banks
Responsibility	WG4
Result	Transfers of securities are possible between CDSC and other EAC CSDs
Measurement	Number of Form of Payment and DVP links open Number of security transfers made
Priority / Dependencies	Medium term Follows modernisation of CDSC systems and dependent on other EAC CSDs

Action	5.1.12. - **A central counterparty for cash securities to be established**
Details	When securities trading volumes increase, there may be a case for introducing a CCP for cash securities to reduce operational risk and manage counterparty credit exposures. CMA to commission study to assess costs and benefits of introducing a CCP for cash securities and the institution best placed to provide the service.
Implementation	CMA with the industry
Responsibility	WG2
Result	Action on whether CCP is justified
Measurement	CCP in place
Priority / Dependencies	Medium term Follows increase in securities trading volumes

Action	5.1.13. - **CDSC should aim to build bilateral connections with Euroclear and Clearstream**
Details	Initially, CDSC should achieve a level of services that makes it feasible for Euroclear and/or Clearstream to open accounts through custodian banks, when customer demand justifies it. Subsequently, CDSC should open reciprocal links with Euroclear and/or Clearstream to enable CDSC to hold and settle international securities.
Implementation	CDSC working with local custodian banks, Euroclear and Clearstream
Responsibility	WG4
Result	Accounts opened
Measurement	Number of securities held in reciprocal accounts
Priority / Dependencies	Medium term Follows system modernisation

5.2. Develop clearing house infrastructure

Action	**5.2.1. - Assess the adequacy of the legislative and regulatory framework to support derivatives clearing**
Details	Review the currently proposed regulations and other legislation to ensure they cover all the requirements of a derivatives clearing regime, including support for novation, netting, segregation of client assets and default management
Implementation	CMA, National Treasury and Parliament
Responsibility	WG3
Result	Confirmation that legal and regulatory framework can support derivatives clearing
Measurement	Legal and regulatory framework supportive of derivatives clearing in place
Priority / Dependencies	Short term

Action	**5.2.2. - Survey the size of the existing OTC derivatives market in Kenya**
Details	Carry out a survey of the extent of trading OTC derivative instruments in Kenya, following the methodology of the BIS surveys
Implementation	CBK should construct questionnaire to be sent to all banks active in the market, collate responses and publish results
Responsibility	WG2
Result	Public data on size of OTC derivative market
Measurement	Size of OTC derivatives market established
Priority / Dependencies	Short term

Action	**5.2.3. - Establish a CCP for commodity derivative products**
Details	Establish a CCP as a new legal entity, with adequate financial resources, appropriate staffing and technical systems and the necessary regulatory approvals - may be combined with 5.2.5
Implementation	Potentially the new commodity derivatives exchange
Responsibility	WG2
Result	Opening of the CCP
Measurement	Successful clearing of commodity derivative products
Priority / Dependencies	Medium to Long term Should follow legal regulatory review and proceed with development of commodities exchange and warehouse infrastructure

Action	**5.2.4. - Review the derivatives market structure**
Details	Review development and structure of derivatives markets to determine appropriate ownership and governance structure for clearing house(s) for commodity and financial derivatives
Implementation	CMA and industry
Responsibility	Implementation Committee
Result	Action on future structure of derivative clearing houses
Measurement	
Priority / Dependencies	Long term After establishment of financial and commodity derivatives clearing house(s)

Action	**5.2.5. - Introduce a CCP for financial derivatives**
Details	Establish a CCP as a new legal entity, with adequate financial resources, appropriate staffing and technical systems and the necessary regulatory approvals - may be combined with 5.2.3
Implementation	Operator of the underlying exchange for financial derivatives
Responsibility	WG2
Result	Successful clearing of financial derivative products
Measurement	CCP for financial derivatives in place
Priority / Dependencies	Short to Medium term

Action	5.2.6. - **All CCPs should carry out regular reviews to ensure compliance with CPSS-IOSCO principles**
Details	Every clearing house should carry out regular assessments of itself against the CPSS-IOSCO Principles for Financial Market Infrastructures by independent external reviewers and address any gaps identified
Implementation	Clearing house appoints independent experts to conduct review
Responsibility	WG2
Result	Assessment of compliance with CPSS-IOSCO Principles and understanding of gaps
Measurement	Degree of compliance with principles
Priority / Dependencies	Medium term Important after establishment of clearing house and then annually

6. INSTITUTIONAL AND CAPACITY BUILDING INITIATIVES

6.1. Develop and retain professional talent

Action	6.1.1. - **Include financial services education in university law courses**
Details	The inclusion of content relevant to capital market products, infrastructure or law into under-graduate or post-graduate law courses will support the development of a pool of legal practitioners skilled in the operation of capital markets
Implementation	CMA to approach universities and examine the extent to which law courses cover issues relevant to capital markets Where necessary, the CMA and the universities to expand curricula to include courses relevant to financial services and to capital market products, infrastructure and law in particular
Responsibility	WG1
Result	Law courses in universities include issues relevant to capital markets
Measurement	Tangible course content in place
Priority / Dependencies	Medium term

Action	6.1.2. - **Assess options for training, examination and certification**
Details	The development of an organisation that can provide training, examination and certification for capital market participants and practitioners will support the growth of domestic and regional capital markets and the creation of an international financial centre by creating a pool of skilled capital market operators
Implementation	CMA to assess options for training, examination and certification
Responsibility	WG1
Result	Capital market participants in Kenya are trained, certified and licensed by a domestic provider with regional and international recognition
Measurement	SITI 5 year strategic plan implemented SITI's curriculum is recognised by the CMA A licensing framework for capital market participants established
Priority / Dependencies	Short Term Dependent on outcome of implementation of SITI's 5 year strategic plan

7. SOUND, RESPONSIVE REGULATION AND LEGAL FRAMEWORKS THAT INSPIRE CONFIDENCE

7.1. Strengthen and Streamline Financial Regulation

Action	7.1.1. - **CMA will support progression to full integrated financial regulation**
Details	As discussion on the integration of the financial regulators continues the CMA will argue for full integration of all regulators as the best model for most effective implementation of the Master Plan
Implementation	CMA to engage with Treasury and other financial regulators
Responsibility	WG3
Result	A regulatory structure best suited to the needs of the Kenyan capital markets and to attract international participation
Measurement	Implementation Committee to keep under regular review
Priority / Dependencies	Short term

Action	7.1.2. - **As steps towards integrated regulation progress the CMA will seek to ensure that the outcomes are optimal from the point of view of achievement of the goals of the Master Plan**
Details	CMA will take steps to ensure that the key success factors for integrated regulation are borne in mind as steps are taken towards integrated regulation and as the Master Plan is progressed
Implementation	CMA to engage with Treasury and other financial regulators
Responsibility	WG3
Result	Integration that is as effective and as supportive of the Master Plan as possible
Measurement	IC to review regularly
Priority / Dependencies	Short term

Action	7.1.3. - **CMA will play its proper role in ensuring that the arrangements for maintaining financial stability in Kenya as a whole function well at all times**
Details	CMA will help ensure that the dialogue between the financial regulators and the macroeconomic policy makers takes proper account of financial stability considerations
Implementation	CMA with other financial regulators, CBK and National Treasury
Responsibility	WG3
Result	Risk of disturbance to financial stability is minimised
Measurement	Implementation Committee to keep under regular review
Priority / Dependencies	Short term

Action	7.1.4. - **CMA will consider whether the intent of its development objective would be better met by its replacement by a set of legislative and regulatory principles which would ensure that the regulatory burden was the minimum appropriate**
Details	Development objectives can conflict with regulatory objectives. CMA to consider whether application of better regulation principles is a safer and more effective way to assist market development and report on its conclusions
Implementation	CMA to consider and consult with National Treasury and Attorney General
Responsibility	WG3
Result	Reduce risk of compromise of regulatory objectives and better targeted and more cost-effective regulation. Industry understands that development is its own responsibility
Measurement	Issuance by CMA of conclusions of its review
Priority / Dependencies	Medium term

Action	7.1.5. - **CMA will examine the case for amending the law formally to put in place "no-action" arrangements**
Details	CMA will study and bring a recommendation for implementation to the National Treasury
Implementation	CMA to consult with market participants, financial market lawyers, Attorney General and the National Treasury
Responsibility	WG3
Result	A more secure way of enabling market innovation
Measurement	Implementation of ''No action" arrangements
Priority / Dependencies	Short term

Action	7.1.6. - **CMA will examine the case for some form of principles-based regulation**
Details	As per the Master Plan
Implementation	CMA to consult with market participants, financial market lawyers, Attorney General and National Treasury
Responsibility	WG3
Result	A more effective and efficient regulatory regime
Measurement	Recommendation published for consultation. Action undertaken in light of results of consultation
Priority / Dependencies	Medium term

7.2. Restructure legal framework for regulation

Action	7.2.1. - **As Kenya moves towards a more comprehensive integrated financial regulation the CMA will support a parallel move to an integrated legal framework**
Details	As per Master Plan
Implementation	CMA to engage with Treasury and lawmakers, with input from financial services lawyers through The CityUK
Responsibility	WG3
Result	Combination of regulatory and legislative integration leads to optimum outcome for market users and participants
Measurement	Implementation Committee to review periodically
Priority / Dependencies	Medium term

Action	7.2.2. - **CMA will conduct a fundamental review of capital market legislation**
Details	Review existing legislation for financial transactions and institutions, including checking on progress with implementation of CMA Action Plan following IOSCO Self-Assessment exercise
Implementation	Review to be carried out under the auspices of CMA, potentially with input from international financial services lawyers through The City UK MOU and further technical assistance from IOSCO
Responsibility	WG3
Result	Improved, up to date capital markets legislation
Measurement	Revised cap[ital. markets legislation
Priority / Dependencies	Short term Dependent on decisions on market structure

Action	7.2.3. - **CMA will maintain consultation processes in line with international good practice**
Details	As per Master Plan
Implementation	CMA to review international good practice and consult with market stakeholders and Treasury on standards for consultation. CMA to introduce enhanced consultation procedures
Responsibility	WG3
Result	Better quality legislation, with improved buy-in from stakeholders
Measurement	Enhanced consultation processes implemented
Priority / Dependencies	Short term

Action	7.2.4. - **National Treasury and CMA will explore with National Assembly the scope for further improvement of process to ensure that capital markets legislation is properly considered with due account taken of public interest arguments**
Details	As per Master Plan
Implementation	CMA and National Treasury to discuss with National Assembly
Responsibility	WG3
Result	Parliamentary decisions are taken on a proper basis weighing in a balanced fashion both private and public interest
Measurement	Implementation Committee to review progress regularly
Priority / Dependencies	Short term Important

Action	7.2.5. - **CMA will explore with National Treasury the case for exempting subsidiary financial services legislation from the requirements of the Statutory Instruments Act**
Details	As per Master Plan
Implementation	CMA to discuss with National Treasury and National Assembly scope to fast-track subsidiary legislation. Enact changes to extent possible
Responsibility	WG3
Result	Reduction in delays in keeping legislation up to date with market developments
Measurement	Amendment of legislative process
Priority / Dependencies	Short term

Action	7.2.6. - **CMA will establish a financial law review panel under its auspices**
Details	As per Master Plan
Implementation	CMA to discuss with financial market lawyers arrangements for setting up a financial law review panel
Responsibility	WG3
Result	Detailed advice available to assist in keeping all legislation relevant to financial services activity as up to date as possible
Measurement	Establish a Financial Law Review Panel
Priority / Dependencies	Medium term

Action	7.2.7. - **CMA will support the development of financial expertise in the courts and support the establishment of an integrated Financial Services Sector Tribunal**
Details	As per Master Plan
Implementation	CMA to discuss with Attorney General the possibility of enhanced training for judges and the establishment of specialist tribunals to hear cases relating to financial regulation, where purely in relation to capital market cases or on an integrated basis
Responsibility	WG3
Result	More effective court arrangements
Measurement	Creation of a special tribunal
Priority / Dependencies	Medium term

7.3. Build capacity of capital market regulators

Action	7.3.1. - **CMA will seek to ensure that the appointment process for board members is in line with emerging best practice and the board will review the skill sets it requires**
Details	As per the Master Plan
Implementation	CMA Board to assess requirements and discuss any enhancements needed with Treasury
Responsibility	WG3
Result	Better-equipped Board of the CMA. Increased attractiveness of the Kenyan market place
Measurement	Board review undertaken and recommendations passed to National Treasury
Priority / Dependencies	Short term

Action	7.3.2. - **CMA will act on the conclusions of its current job evaluation and reorganisation project for its human resource requirements and will ensure over time that its staffing needs, remuneration arrangements and organisational structure continue to match evolving requirements**
Details	As per the Master Plan
Implementation	CMA to implement results of its current review and discuss recommendations with other stakeholders, including National Treasury, with a view to implementing recommendations on staffing and structure. Repeat the exercise in 2016. Put in place process for continuing assessment of changing needs
Responsibility	WG3
Result	A CMA resourced in HR and organisational terms to meet the requirements expected of it
Measurement	Delivery of recommendations. Implementation of recommendations Review/feedback loop to ensure the outcome of the project is consistent with the needs.
Priority / Dependencies	Short term Important

Action	7.3.3. - **CMA will seek to ensure its budgets and funding match resourcing needs over time and build in sufficient flexibility to meet stakeholder expectations including those arising from the Master Plan**
Details	As per the Master Plan
Implementation	CMA will undertake an assessment of its likely budgetary needs and review options for changing the basis of its funding. It will discuss the results of its review and consequent recommendations with other stakeholders, including National Treasury, with a view to implementing recommendations in relation to both the amount and composition of funding. The CMA will undertake periodic reviews of its continuing budgetary and funding needs
Responsibility	WG3
Result	A CMA resourced in financial terms to meet the requirements expected of it
Measurement	Delivery of recommendations. Implementation of recommendations Review/feedback loop to ensure the outcome of the review is consistent with the needs
Priority / Dependencies	Short term Important

Action	7.3.4. - **CMA will ensure its external communications and outreach demonstrate careful thought leadership and that it maintains reasonable response time**
Details	As per the Master Plan
Implementation	CMA to review all communication requirements and act on recommendations. CMA to publish target response times
Responsibility	WG3
Result	Cordial external working relationships. Better policy outcomes. Better informed public
Measurement	Cordial working relationship
Priority / Dependencies	Short term Important

Action	7.3.5. - **CMA will ensure adequate access to external expert advice**
Details	CMA to review the availability of external advice, whether from official or private sources, and take steps to access it
Implementation	CMA to establish requirements for external advice and act on them
Responsibility	WG3
Result	Improved CMA performance
Measurement	Implementation Committee to check that this has been done
Priority / Dependencies	Ongoing

8. IMPROVED CORPORATE GOVERNANCE AND FINANCIAL REPORTING

8.1. Strengthen and Enforce Corporate Governance Standards

Action	8.1.1. - **CMA will continue to pursue its existing work programme on corporate governance covering both the corporate governance code and education in good corporate governance**
Details	As per the Master Plan
Implementation	CMA to consult investors and ICPSK on Blueprint for corporate governance code and on education programme Potential for input under The CityUK MOU
Responsibility	WG3
Result	Enhanced standards of corporate governance. Heightened economic efficiency. Reduced risk of loss of confidence in market because of poor governance of issuers
Measurement	Publication of corporate governance code. Creation of education programme for issuers and potential issuers on good corporate governance
Priority / Dependencies	Code: Short term and ongoing Important Education: Medium term`

Action	8.1.2. - **CMA will undertake a review of the different ways in which good corporate governance can be achieved in practice and will act on its findings**
Details	As per the Master Plan
Implementation	CMA to consult investors, market participants, ICPSK, financial lawyers, Attorney General and Treasury on the range of tools available, including those described in the Plan, to bring about good corporate governance and bring about implementation of recommendations
Responsibility	WG3
Result	More robust policing of corporate governance
Measurement	Introduction of range of measures to achieve better corporate governance. Improved results as measured by ICPSK's Governance Index
Priority / Dependencies	Short term

Action	8.1.3 – **NSE to develop a corporate governance social responsibility and sustainability index**
Details	As per the Master Plan
Implementation	NSE in consultation with CMA and market participants
Responsibility	WG2
Result	High corporate governance standards with capital markets
Measurement	Corporate governance social responsibility and sustainability index
Priority / Dependencies	Short term

8.2. Ensure Adherence to International Reporting and Disclosure Standards

Action	8.2.1. - **CMA will review the arrangements for the enforcement of the sound financial reporting of listed companies, including the legal basis and the adequacy of resourcing**
Details	As per the Master Plan
Implementation	CMA to review international good practice and consult ICPAK, Attorney General and Treasury. CMA to strengthen internal capacity to evaluate financial reports and require changes Potential for input under The CityUK MOU
Responsibility	WG3
Result	More reliable financial reporting for investors
Measurement	Implementation of enhanced enforcement arrangements by adequately-resourced CMA
Priority / Dependencies	Short term Important

Action	8.2.2. - **CMA will support ongoing work with the National Treasury to move forward with the speedy establishment of an independent Kenyan auditor oversight regulator in adherence to the Core Principles of IFIAR**
Details	There are current initiatives between ICPAK and the National Treasury aimed at establishing a new auditor oversight body. This will require legislation, the appointment of a board, the provision of resources and choice of organisation to perform the function
Implementation	The National Treasury will in conjunction with ICPAK facilitate the establishment of an independent auditor oversight body
Responsibility	WG3
Result	Kenyan audit arrangements brought up to international standards
Measurement	Kenyan independent audit oversight regulator operational and accepted as a member of IFIAR
Priority / Dependencies	Short term Important

9. INNOVATIVE, OPEN AND COMPETITIVE ENVIRONMENT

9.1. Open Access to Market Infrastructure

Action	9.1.1. - **Review market infrastructure membership criteria**
Details	CMA to review membership criteria for market infrastructures to ensure they are public and do not create barriers to competition
Implementation	CMA and providers of market infrastructure
Responsibility	WG3
Result	Membership criteria are open and transparent
Measurement	Number of new entrants
Priority / Dependencies	Medium term Important

9.2. Liberalise Fee Structure

Action	9.2.1. - **Liberalisation of financial policies for financial firms and infrastructure providers**
Details	Progressively permit financial firms to set their own fees in an open and competitive market
Implementation	CMA
Responsibility	WG3
Result	Firms set their own fees
Measurement	Liberalised and competitive fee structure
Priority / Dependencies	Medium term Important Dependent on existence of open market access

9.3. Involve the Competition and consumer protection Authorities

Action	9.3.1. - **CMA should keep the Competition Authority and Consumer Protection Authorities advised of moves to liberalise markets**
Details	CMA to open contacts with Competition Authority to discuss their role in relation to competition in capital markets and then maintain contact
Implementation	CMA contacts Competition Authority to explain background to CMMP
Responsibility	WG3
Result	Competition Authority reviews operation of competition in capital markets
Measurement	Liberalised and competitive capital markets
Priority / Dependencies	Ongoing

Action	9.3.2 - **CMA to work with policy makers to ensure that appropriate frameworks for Consumer Protection are put in place.**
Details	CMA to work with National Treasury and other Financial Sector regulators to finalize the Financial Sector Consumer Protection Regulatory Framework
Implementation	CMA through the Financial Sector Regulators Forum spearheads the review of the draft Financial Consumer Protection Regulations and submits to Cabinet Secretary, Treasury for gazettement
Responsibility	WG3
Result	Other Consumer Protection Regulators review cases where an institution or group of institutions abused their market positions or where individuals seek recourse
Measurement	Financial sector consumer protection framework in place
Priority / Dependencies	Ongoing

CAPITAL MARKETS MASTER PLAN (CMMP) STEERING COMMITTEE

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SUBMISSIONS AND CONSULTATIONS

The Capital Markets Authority (CMA) would like to express its appreciation for the valuable insights and information provided by all the individuals and organizations, domestic and foreign, who made submissions and participated in meetings and discussions with staff members and its consultants. The CMA would particularly like to thank those listed below for their time and input.

Abraaj Capital
African Alliance Kenya Securities
African Development Bank
Amalgamated Chama Ltd
Anopolis
Apollo Asset Management Company Ltd
Association of Chartered Certified Accountants Kenya
Barclays Bank of Kenya Ltd
Barclays Capital
Bloomberg
Bond Markets Association
Britam Kenya Limited
Burbidge Capital Limited
Central Bank of Kenya
CFC (Stanbic) Holdings
Chartered Institute of Securities and Investments
C&R Group
Commercial Bank of Africa
Commission on Revenue Allocation
Communications Commission of Kenya
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East African Venture Capital Association
Energy Regulatory Commission
Financial Sector Deepening Africa
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Fund Managers Association
Genesis Kenya Investment Management Ltd
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Kenya Association of Investment Groups
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Kenya National Bureau of Statistics
Kenya News Agency
Kenya Private Sector Alliance
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Kenyatta University
KIPPRA
Law Society of Kenya
London Stock Exchange Group
Old Mutual
Metropol East Africa Ltd
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Ministry for Devolution and Planning
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National Economic and Social Council
National Social Security Fund
National Treasury
PineBridge Investments East Africa
Privatisation Commission of Kenya
Retirement Benefits Authority
Sacco Societies Regulatory Authority
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Promoting the Integrity and Growth of the Capital Markets

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