Challenges and opportunities ahead for the JSE

By Humphrey Borkum, Chairman of JSE Limited

Bond markets are regarded by many people as dark, secret places full of strange alchemy. They remember that it was the mortgage bond debacle in the US in 2008 that brought on the recession and led the world to the brink of financial collapse. A bond is simply a long term loan. Most people have at some stage applied for a loan at a bank and had to pay interest on the amount of the loan. The bond market operates in exactly the same way.

In the financial markets a bond is an instrument that promises the borrower (a company or government) will pay the investor (normally financial institutions) interest over a period of time and repay the full amount of the loan on a predetermined maturity date. The fact that a number of overleveraged countries in Europe, particularly Greece, are battling to repay their bonds at the predetermined dates has led to the nervousness and uncertainty in European markets.

In South Africa the government and state owned enterprises are by far the largest issuers of bonds.
It is usually large companies with significant assets which can be used as collateral that use the bond market to raise capital. The quality of the assets lower the interest rate charged.

Much like the United States and Britain, South Africa is equity centric with roughly 60% of our average asset allocation consisting of equity, 20% property and 20% bonds and cash. Germany and Japan on the other hand have populations with a far greater fear of risk and therefore bond holdings dominate equities by a considerable margin. In 2009 our market capitalisation was R5,66 trillion for equities and R1,1 trillion for bonds. The average size of our cash equity trades was R135 000 and R21,3 million for spot bonds.

During 2009 the JSE acquired the entire issued share capital of the Bond Exchange of South Africa (BESA) and together with our YieldX market formed the Interest Rate Division of the JSE. Proceeding with caution and in consultation with all the various stakeholders we are hoping to create a world class multi product exchange that will provide a sophisticated trading, clearing and settlement infrastructure for all its clients. A large, more transparent market will draw in more players which should in turn lead to economies of scale and lower the cost of capital for companies needing to fund new ventures. Due primarily to the interest rate differential between South Africa and the developed markets plus the growing efficacy of our Interest Rate Division, the bond market has attracted R30 billion of foreign direct investment to date this year.

Exchanges need to innovate continually to remain relevant to issuers and investors alike. In this regard our consolidation of BESA and YieldX means that by July this year we will have achieved one set of listings and by September one rule book and one trading platform. It is also our intention to bring the core liquid part of the bond market to a single place of anonymous electronic execution or the classic electronic exchange way of doing business. This should, among other benefits, extend the reach of the bond market to more retail investors.

Australia vs sub-Saharan Africa

Australia's investment climate has become a topic of conversation as the financial media pontificates on the Australian government's intention to impose a 40% super tax on resource firm's profits. It appears that BHP Billiton and Rio Tinto, two of the world's largest mining companies, are re-evaluating new capital and exploration projects on a continent that is one of our great rivals for mining investment.

This scenario presents a great opportunity for South Africa and indeed sub-Saharan Africa.

Mining companies already know the impediments to investing in South Africa. They usually cite BEE targets, power restraints and an inflexible labour market. Their main concern about sub-Saharan Africa is lack of infrastructure. However if Trevor Manuel's National Planning Commission can persuade our government to keep economic policy and mining regulations stable over the next couple of years this region can attract more foreign investment for exploration and new ventures. Oil has been discovered in Uganda and who knows what can still be extracted from beneath our soil. Mozambique, for example, is just starting on its voyage of mineral discovery and development.

The mineral resources of sub-Saharan Africa was a key consideration in the JSE launching its African Board - offering dual listings to firms from outside South Africa and setting fees that would only cover our costs. For the last fifteen years and, more recently at the World Economic Forum for Africa conference, we have been encouraging policymakers to harmonise their bourses electronically to the JSE with the aim of growing capital markets in the region.

Another fact that has come to my attention concerning Australia is that almost half of its equity trading is conducted by 5,7 million investors or roughly 27% of the population. In South Africa only 200 000 investors (0.4% of the population) invest directly in the stock market. This presents a challenge for us to try and emulate the Australian statistics.

In this regard the JSE sponsors a number of projects in an attempt to broaden our future investor base by familiarising the youth of South Africa with the workings of the JSE. The most recent is the JSE Investment Education Project (Jiep) which has the aim of growing the economy through taking financial knowledge and literacy to the schools. I wish these subjects had been included in my school curriculum!

Commencing in 2007 Jiep was first implemented throughout Gauteng in 250 schools. Kwa-Zulu Natal has 50 participating schools and we are now extending the project to 50 schools in the Eastern Cape. Grade 9 and 10 learners receive practical financial education on budgeting, saving and managing bank accounts in the first year and investment principals in the second year. The course material and lesson plans are provided by the JSE.

Another project is the JSE/Liberty Investment Challenge in which school teams test their share trading skills through an annual simulated ghost trading programme. In the Challenge which has been in place for over 30 years each team is given an imaginary sum of R1 million to invest in JSE listed shares and the performance is tracked and measured against other teams taking part. Substantial prizes are awarded to the top performers.

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