

The Role of the Dar es Salaam Stock Exchange in Safeguarding Securities Investors in Tanzania

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Abstract: This study examines the roles/functions of the Dar es Salaam Stock Exchange (DSE) in safeguarding the investors of securities in Tanzania. The business of securities, both bonds and shares has taken a new dimension since its establishment in Tanzania. It has attracted many people of different cadre. However, some investors have been doubtful on whether they should invest or not. The doubts seem to be cemented on risk associated with investing. This study therefore, expounds the role of DSE through narrating measures that have been put in place for safeguarding the investors of securities. The study utilizes mixed methodologies of data collection with documentary and the use artifacts taking the leading role. The study concludes that there are measures that have been put in place through rules and regulations with the view to protecting investors of stock exchange. However, it is the investors' responsibility to attain necessary information regarding the firms that sell bonds and or shares and studying, among others, the financial information of the firms so as to realize the performance and prospective opportunities of the firms.

Key words: Securities, Dar es Salaam Stock Exchange (DSE), investors, firms, CMS, Tanzania

INTRODUCTION

This study discusses the role/functions of the DSE in safeguarding the investors of securities (bonds and shares). The stocks exchange business has kept growing since its establishment in 1996 when the first firm, Tanzania Oxygen Limited (TOL) listed shares with the DSE. However, some people seem to be doubtful in deciding to invest for what is considered a risk business. It is from that point of view this study sets the functions of the DSE and its role in safeguarding the investors.

The first part therefore is the introduction which provides the background to the DSE and the Capital Market Security Authority (CMSA). The second part narrates the functions of the DSE, qualifications and procedures for listing securities. The advantages and disadvantages are provided in the 3rd part. Both advantages and disadvantages are essentially looked at from administrative point of view of the firms listing securities. The conclusion is set on part four.

Background to DSE: The Dar es Salaam Stock Exchange (DSE) was established by the capital markets and security authority under the Capital Markets and Securities (CMS) Act of 1994. The DSE was incorporated in September, 1996 as a company limited by guarantee without a share capital under the companies ordinance (Cap. 212) (DSE, 2008a). The enactment of DSE came as a result of

government's policy of transforming its economy from public government dominated economy to private sector driven economy. The Capital Markets and Securities Authority (CMSA) is a government agency established to promote and regulate securities business in Tanzania. It was established under Capital Markets and Securities Act, 1994. The legal framework for the regulation of the securities industry is the Capital Markets and Securities Act, 1994 (Act No: 5 of 1994 as amended by Act No: 4 of 1997).

The act is supplemented by various regulations that are promulgated by the Minister for Finance. DSE is a non-profit making organization created to facilitate the government implementations of the economic reforms in particular on enabling the private sector raise capital. The exchange became operational in April 1998 with TOL Gas Limited listing as the first company followed by the Tanzania Breweries Limited (TBL) during the same year.

The delay was due to the necessary background operational preparations that were inevitable such as training of brokers and formulation of issuance and trading rules (CMSA, 2008). Hence, a stock exchange is a secondary capital market where large and small investors can buy and sell securities (shares and bonds etc.). It is an organized market where buyers and sellers of securities meet as they are represented by dealers/brokers and acquire or dispose securities (DSE, 2007; Norman, 2006). It is a market which securities are traded by members of

the exchange who may act as both agents (brokers) and as principal (dealers) (Benning, 2007). The operation of the DSE is vested in the hands of the council which is the board of directors of the company. The first Board of Directors was elected in July, 1997.

Further, listing of shares and bonds at the Dar es Salaam Stock Exchange (DSE) provides companies, the government as well as municipal researchersities with a possible source of accessing funds from both the public as well as institutional investors. Listing of these securities facilitates secondary market trading of the bonds and shares and thus provides the necessary liquidity required on the market. Literally every market has a demand side and supply side.

Hence, both the central government and the local government are considered supply side of the stock exchange while the public is considered as the demand side. Therefore, the two sides meet when shares are issued for the first time (CMSA, 2008; DSE, 2003). The first issuance of shares is commonly known as Initial Public Offer (IPO). The general term of supply side does not exclude the various companies other than those owned partly or full by the government and other issuing companies.

In all sense, the importance of financial information or accounts information is inevitable to investors and most findings have indicated the imperativeness of these reports. Naser and Nuseibeh (2003) and Norman (2006) provide a number of studies which have investigated the usefulness of corporate information to the users and found the annual report to be important and primary source of information.

These include (Abu Baker and Naser, 2000; Mautz, 1968; Lee and Tweedie, 1975a, b, 1976, 1981; Epstein, 1975; Anderson, 1981; Arnold and Moizer, 1984; Day, 1986; Gniewosz, 1990; Epstein and Pava, 1993, 1994; Bence *et al.*, 1995; Anderson and Epstein, 1995; Abu-Nassar and Rutherford, 1996; Bartlett and Chandler, 1997).

Registered firms with the DSE: As of March 2009, 14 companies listed their shares with the DSE. Out of 14 companies, three are from Kenya and their shares not only cross listed at the DSE but also at the Uganda stock exchange and Nairobi stock exchange.

However, the concern has been what is the role of the DSE and to what extent do people understand the functions of the DSE and its importance in reducing the risks that may be encountered by the investors of securities. Most literature indicates that financial performance of the firms is a key factor or indicator on the reliability to purchase shares, though not the only.

MATERIALS AND METHODS

Functions of the DSE: CMSA and DSE have mandate to make rules and regulations for the purpose of fostering the exchange business. For example, the Dar es Salaam stock exchange has developed a two tier scheme of listing securities which are first tier and second tier. In Tanzania the most practiced Listing is the First Tier. On the other hand, the CMSA has made about 14 rules concerned with improving of the entire business (DSE, 2007; CMSA, 2008). DSE (2008b) provides functions of the company which are:

Provides a market for listed securities: It enables those wishing to join or leave the listed companies to do so and those wishing to leave to do so as well. The DSE therefore, provides liquidity by way of providing a continuous market for securities whereby securities are exchanged for cash.

Facilitates price discovery: The pricing mechanism ensures that buyers and sellers can do so at a price determined by demand and supply forces. Neither the exchanges nor brokers determine the prices of the securities traded on stock exchanges.

Facilitator of transparency: Disclosure requirements put in place by the DSE require listed companies to promptly disclose all price sensitive information so that investors may make informed decisions. This is achieved at two levels; first, at the initial offering period when companies have to meet stringent listing requirements relating to offering documents and second through continuous listing obligations. In this context, the DSE becomes information clearing point between listed companies and investors (information hub).

Facilitates privatization and wider ownership of resources: The DSE has facilitated and continue to facilitate the privatizations of the some parastatal organizations which were hitherto under the control of the government whose shares have been sold by the government through the DSE.

Facilitates raising of capital for enterprises: The DSE facilitates companies to sell new shares/bonds at better prices which lower the cost of capital to such companies and improves their chances of increasing operating profits. Experience has shown that investors accept higher prices for shares and lower interest rates for bonds, when the companies selling these securities are well known and have met stringent listing conditions and

reporting requirements as opposed to lesser known enterprises where the investors are faced with a greater amount of uncertainty and as a result they demand lower prices for shares or higher yields as a compensation for this increased risk.

Creation of wealth through investing in listed securities:

It has been proved in many occasions that shares offer investors the real return because shares out-perform inflation on average and have done so consistently since share markets came into existence. Shares listed at the DSE have performed very well above the inflation rate when compared with bank deposits. Shares are not passive store of value like banks' deposits. Bank's deposits do not increase in size during the lock-in period but shares do increase in value overtime.

Contributes to the cultural transformation of Tanzanians:

At the time the DSE was established, only a handful Tanzanians could claim to be knowledgeable with stock market operations. Operationalization of the DSE has contributed substantially towards public enlightenment which has caused a few Tanzanians to invest in listed companies as a result of this transformation. The public enlightenment exercise is a continuous one and will continue while taking into account past experiences. It is the DSE's goal that Tanzanians appreciate and eventually adopts a thrift culture that thrive an equity ownership in successful business concerns.

Listing requirements for shares: The DSE has set a number of requirements for listing. Procedures that govern the companies in order to be listed here:

- The company has to release initial and periodic information to the public so as to inform the investors regarding the company's position and progress over the period of time. Listed companies are required to publish interim reports covering six months and the annual report
- The company has to have a track record of adequate duration to allow for the possible investors to appraise its present and possibly future performance
- The company is of the size which makes the participation of the public in investing therein possible
- The minimum requirement of the capital of the company is TZS 400 million as of the year 2008 December

- The company must be a public company as required by the companies Act. 2002 that it has at least two shareholders and that the articles and memorandum of association should indicate that the company in question is a public company
- The public must hold at least 25% of the issued shares. Shares held by the employees are not considered in determining the 25% threshold
- The company must prepare and obtain approval of the Prospectus from the Capital Markets and Security Authority (CMSA). The requirement governing the conditions and contents of the prospectus are provided by the capital markets and securities (prospectus requirements) regulations, 1997
- The company must undertake to comply with the set of undergoing listing obligation

However, there are conditions that apply before listing and others apply after a listing is done. When the listings is already effected the conditions following thereto is known as continuous listing obligation. Moreover, some conditions are critical and thus applied when listing of shares (equities) while others are crucial when listing of bonds (debt securities).

Listing procedures for debt securities: The DSE (2008b) hand book further provides listing procedure for securities. The listing of debt securities can be termed as a secondary listing. The logic behind such conception is the fact that debt security listing is done after the company has sufficed most conditions for listing equities. Hence, the following are the qualities for listing debt securities:

- It must have already obtained a listing of its ordinary share capital
- It should offer at least Tshs. About 50 million of issued loan capital of the class to be listed. Further issues of shares of a class already listed are not subject these limits
- Its total loan capital should not exceed 100% of shareholders' funds less intangible assets
- It is required to enter into a contract with the exchange on such terms as the exchange may require for the protection of stockholders

The procedures in listing shares imply that a bad company is not likely to sell their shares in the market. No broker and bank would like to be involved in selling the shares of the company whose financial analysis indicate that is a poorly performing or which its future profitability is questionable. So, the fact that banks and brokers agree

to be involved in the issuing of shares of a particular company implies that that company is relatively good. Also, it should be made clear that loss may occur even if there is financial analysis largely because the price of a share reflect investor sentiment about the company and not always necessary that price reflect fundamental value.

However, getting information on whether investors consider financial analysis before investing is important aspect and may justify the survey particularly the prudence of financial information (Norman, 2006). Rules set for listing shares is one thing and investor's drivers to investing are another and one of the fundamentals for making such decision is to know the financial information of the interested firm.

The roles of the stock exchange: The principal role of the stock exchange company is the mobilization of the resources and directing such resources to the productive sectors of the economy (CMSA, 2008; DSE, 2008a, c). It offers a relatively convenient and an alternative access to capital in comparison to the traditional financial instruments such as bank loans. The resource directing strategy has up to 2001 enabled about 40,000 Tanzanians to be owners of various companies through purchase of shares (DSE, 2008c).

On the government side the DSE has made possible for the gain of 17.6 billion Tanzania shillings through sale of its shares of Tanzania Breweries Company Limited (TBL) and the Tanzania Cigarette Company Limited (TCC) (DSE, 2001). Obviously, the current number of the people owning shares is big.

RESULTS AND DISCUSSION

Advantages and disadvantages of listing shares: There are many advantages for investing in shares. However, there is also what may be considered disadvantages for listing shares.

Advantages: With the ever increasing techniques in terms of investment and technological advancement, the choice to allocate finances as a strategy for investment is crucial. It has been however noted in this literature that there are potentials in investing in securities such as bonds and shares compared to the cardinal practice of depositing finances with the financial institutions such as banks and wait for the accrued money through interests.

The vitality of investing in the stocks is a reality that no sane person can deny. Thus, this part provides advantages for listing securities specifically at the DSE.

- The company can raise capital relatively cheaply from the public. While the normal practice for financial increases of the firms are raising capital through loan acquisitions from banks and other financial institutions which culminates for the interest of about 16-23% in favor of the banks and other financial institutions
- On the contrary the stock exchange does the same role of raising the capital of the firm without subjecting the entire firm in interest charged against it. Thus, the firm listing the securities with the DSE does so with minimum risk of loosing its capital
- The performance of the company is monitored by the market and therefore a listed company is likely to perform better to meet the expectations of the public. The qualifications for the companies' listed as indicated in this study limits to the maximum the possibilities of a company to perform contrary to the wishes of the investors. Thus, it can be added that it is of paramount importance of the company to list her shares with the stock exchange, since it further helps the company to assess itself on whether it has a favorable future survival
- Listing of securities is a marketing tool for a company as it would be referred to frequently during the release of the market information to the public. The DSE is currently conducting five trading per week. Thus, a company listed would be enjoying marketing benefits whenever trading results of listed companies are announced in either electronic or print media
- Listed companies are generally considered to be good performers and therefore are perceived to have the potentials of providing a good return to the investors. Thus, listed companies experience other benefits
- Listing widens the range of financing choices of the company. Thus, a company is not bound to raise its capital through a certain means only. Rather has variety of options including listing shares, financial institutions, directors and banks
- Listing of shares lowers financing cost of the enterprises. This could be associated with raising capital without incurring any substantial amount as a fee to the capital such as interest. Thus the burden for the company would be reduced
- Listing facilitates share ownership changes or privatization. The listing company paves a way for transfer of shares from one individual to another. Thus it enables individuals to enjoy ownership of the company for time they want

- Listing attracts foreign portfolio investors. Just as local investors are attracted through listing, the same happens to foreign investors. It enables foreign investors realize where to invest. Among the components important for investing is market and capital availability. An assurance of the market and ability to raise capital facilitates foreign investors to bring their intended capital from outside and raise some capital within
- Listing enables both firm and individuals to realize the value of the company through the interplay of the demand and supply of the company shares at the SE. Normally, assessing oneself can be a difficult thing and some time challenging. Since, self assessment means giving value of your self using the criterion set. Nevertheless, listed companies can easily know their value through the interplay of the markets. This can be termed as facilitates open assessment as opposed to self assessment. Since, it is the market which gives the value of the company, therefore the assessment attained is an open and done by the mixtures of professionals, businessmen, firms representatives and the public in general
- Listing of shares enables the company to increase the opportunities to venture into new investments and expansions by having alternative means of raising capital for such investments. Currently, there exists cooperation between the east african securities regulators as well as cooperation of East African Stock Exchanges. The said cooperation has enabled the company wishing to expand its wings in the region, to list shares in other East African countries such as Kenya, Uganda and Tanzania thus, raising the opportunities for raising capital. Today there are three Kenyan companies namely; Kenya Airways and East African Breweries Limited and Jubilee Holding Limited that are listed in the three stock exchanges of Kenya, Tanzania and Uganda

There are other packages that are associated with the listing of the shares with the DSE and have been listed in the DSE (2008b) hand book as fiscal incentives.

Fiscal incentives: The government has deliberately provided several incentives in order to encourage active participation in capital markets by issuers and investors. DSE (2008b) hand book further provides some incentives for the companies that list shares with it. The privileges include:

Incentives to issuers:

- Reduced corporate tax from 30- 25% for the period of three years where the Issuer has issued at least 35% of the issued shares held by the public. The reduced rate is applicable for 5 years starting from listing date

- Tax deductibility of all Initial Public Offering (IPO) costs for the purposes of income tax determination. All IPO costs are accepted by the Tanzania Revenue researcharsity (TRA) as acceptable expenses used in the generation of income and profits and therefore are taken into consideration when determining profit for tax purposes

Withholding tax on investment income made by Collective Investment Schemes (CIS) is final tax. Investors in CIS are not charged with tax on the income.

Incentives to investors:

- Zero capital gain tax as opposed to 10% for unlisted companies
- Zero stamp duty on transactions executed at the DSE compared to 6% for unlisted companies
- Withholding tax of 5% on dividend income as opposed to 10% for unlisted companies
- Zero withholding tax on interest income from listed bonds whose maturities are three years and above
- Exemption of withholding tax on income accruing to fidelity fund maintained by DSE for investor protection

Income received by the Collective Investment Scheme (CIS) investors is tax-exempt.

Disadvantages for listing shares: While there seem to be many advantages, equally there exist some opposing forces as to the extent of such benefits of listing. For example the Virgin Company Limited of the United Kingdom, deregistered its shares from the London stock exchange for what it named improper management of resources by the new shareholders. The Virgin Company had the view that it had experienced difficulties in terms of progress after listing compared to the period before listing its shares with the LSE (Proshare, 2001). Below are some disadvantages:

- Prolonged period for decision making even in circumstance of urgent need for such decision. This is because meetings are scheduled on specific dates and numbers of such meetings are known
- Weak ideas in meetings because the qualification for purchasing shares are essentially money rather than skills in that area. Hence, when the majorities shareholders are not familiar with the entire business the possibility of not assenting to viable solutions become slim, hence distorting the performance of the company

Investors protection: The qualifications for listing shares entail to protecting investors in stock exchange. DSE and CMSA study to ensure that firms that list shares are

worthy and have no doubtful reputation in terms of professional performance. It is professional performance as opposed to necessarily reality of the firms' performance. The financial statements and thus indicators presented in annual financial reports will solely depend on stewardship of the firms preparing such accounts information.

As, Norman (2006) puts it, the beauty of laws including rules and regulations depends on the professional people administering such laws. Mere good accounts information does not necessarily mean real good performance.

In protecting investor, the provisions of the Capital Markets and Security ACT, 1994 the DSE has established a fidelity fund account to be used to compensate investors who suffer financial loss arising from fraud and misappropriation of funds by Licensed used to compensate investors who suffer losses as a result of Licensed Dealing Members (LDMs) negligence. The compensation amount is currently limited to TZS 100,000/ (DSE, 2008a, c).

CONCLUSION

It can be observed that the DSE and the entire business researchersities such as capital market and securities authority have put in place rules and regulations that act as qualifications for listing shares in a manner that saves to safeguard the investors of securities in Tanzania.

The rules are evaluative and monitory in nature. They are evaluative in the sense that they examine the performance of the firms before registering. And they are monitory since they keep on eying on the firms after listing with the DSE to see that they conform to healthy investment. Despite the presence of rules and regulations; securities are traded and thus do behave just like any other business.

Henceforth, the risks associated with the business must be born by the investor. An investor must be able to realize good reasons for investing to each firm. In this regard investors may use professional firms such as brokers, on determining the best firms for investing.

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