

Chapter 6

THE FURTHER DEVELOPMENT AND RELIABLE OPERATIONS OF THE SECURITIES MARKET IN KYRGYZ REPUBLIC

by
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Winning investors' confidence so that they invest money in securities and keeping and consolidating that confidence are the main tasks of any professional activity on the stock market.

We all know that a small failure in the mechanism for attracting investor capital to the stock market can cause major problems and financial loss for all participants in securities trading. Regarding the competent government body, even a tiny negative event affecting investors' capital takes a heavy toll, sometimes lasting many years, on the reputation and image, not only of the body that regulates the securities market, but also of the government. Harm to investors' interests can seriously damage the reputation of the whole country in terms of its attractiveness for investors, as well as cause social disturbances and instability.

A national securities market founded with its corresponding infrastructure and legislation in a short space of time, with the coincidental aim of promoting the development of a market economy in our country, unfortunately cannot be a reliable guarantor of the interests and rights of stock-market investors.

It is clear that to establish a system for attracting investor capital through securities, we need more time and financial inflows, particularly for work with the population, who in the future must become active domestic investors.

The work and measures that must be accomplished to improve confidence among stock-market investors include: improving corporate governance; achieving transparency of securities market operation; improving regulation of securities issuance; developing market infrastructure and financial instruments; improving investment conditions and protecting the rights of investors; strengthening and broadening international cooperation on issues relating to stock-market development.

In this regard, active work is under way in Kyrgyzstan on creating an adequate system to protect investors' interests. The implementation of such a system should boost the confidence of all investors, be they large companies, the general public or institutional investors, both domestic and foreign.

The State Commission on the Securities Market of the Government of the Republic of Kyrgyzstan, which my colleagues and I represent at this conference, has drafted a special bill "on the protection of the rights and legal interests of investors on the securities market". In our view, the adoption of this law will address many legal aspects that were not covered in previous legislation, such as the introduction of reliable mechanisms to protect the rights and interests of stock-market investors. In addition to existing legal requirements, the bill defines the main requirements in terms of disclosure of information, the obligations of professional participants in the securities market, public companies,

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public sale of securities, price manipulation, insider trading, and the role and powers of the government body for the protection of investors' rights.

The rapid adoption in our country of this law and its proper implementation will make it possible to establish a reliable system of instruments and mechanisms to prevent fraud involving the capital and securities of investors and to stop illegal activity on the stock market. This is directly linked to the prevention of strife, which can, in the largest events, easily escalate into social upheaval.

Given that consolidation of the financial system is one of the most important tasks for any government, since steady economic growth requires the mobilisation of the necessary financial resources, every effort must be made to raise the confidence of domestic and foreign investors in the securities market.

To achieve this, we must:

- ensure transparency on the securities market;
- define the regulation of public and private issuers of securities;
- establish a segment of first-class financial instruments on the securities market;
- provide a reliable system for registration of securities ownership;
- establish unified standards for the sale of securities;
- broaden the range of financial instruments available on the securities market;
- popularise securities among potential investors;
- create the conditions for attracting the resources of institutional investors on the securities market;
- develop the potential of the competent government body on the securities market;
- integrate the national stock market into the capital markets of Central Asia and other countries.

Achieving transparency in the securities market requires transparency in the activity of market participants and access to information about the securities market. This is a necessary condition for market development, since transparent activity on the stock market and access to information can help reduce risks, which makes it possible to make appropriate investment decisions and raise investor confidence in the market.

Currently in Kyrgyzstan transparency in activity on the securities market is achieved through disclosure of necessary information by market participants, according to the methods established by the legislation, i.e. the compulsory publication of information required by law, the presentation of accounts, and the registration of prospectuses for securities issues and access to the information contained therein.

An important part of the work of the competent securities body consists in monitoring and supervision of the activity of professional securities market participants and securities issuers.

Unfortunately, disclosure levels remain low – some issuers and professional market participants fail to present the necessary accounts, while others do not comply with the rules on content and presentation or do not disclose significant facts. Consequently, for repeated infringement of the legislation on the presentation of accounts to the competent body, in 2002-2003 the State Commission on the Securities

Market revoked the licences of 12 professional participants, suspended the licences of 10 professional participants, and warned a number of other professional participants. In 2003, 57% of the fines applied by the State Commission on the Securities Market for infringement of the legislation on securities were for infringements of the rules on the presentation of accounts, and 5% were for infringement of the right of investors to receive full and objective information about securities.

The competent body must tighten measures for enforcing compliance by securities issuers and professional participants with the legislation on the presentation of accounts, and improve the quality of analysis of accounts presented by market participants. Regarding the presentation of quarterly accounts by public issuers, we are about to draft interim financial accounting rules, in strict compliance with international standards of financial accounting. This will tighten the disclosure requirements for professional securities market participants.

To achieve this, it is essential to design a programme of measures to raise the standards of disclosure and the transparency of information on the securities market, including:

- completion of the regulatory and legal base on disclosure by issuers and professional participants in the securities market;
- implementation of an effective system for the collection and dissemination of information subject to disclosure, i.e. an information centre (where any interested person may consult information about issuers, professional participants and other information about the securities market);
- cooperation of information agencies, the media, consultancies and professional participants in the securities market to circulate information subject to disclosure to particular groups of investors;
- fulfilment of legal disclosure requirements.

With the development of information technology, we are working on disseminating information via the Internet and e-mail. This can be a valuable way to provide advice to unqualified market investors.

The law "on joint-stock companies" adopted a year ago divided securities issuers into two categories, public and private, to facilitate their regulation. In accordance with the existing legislation, public issuers are companies that sell securities to the public or whose securities are held by 500 or more owners. In accordance with the abovementioned law, work is under way to establish separate requirements for public and private issuers – tightening requirements for public issuers and simplifying them for private issuers. Until now, the requirements for public and private issuers were identical. For example, all issuers had to publish annual financial accounts.

Tightening the requirements for public issuers is necessary to avoid various negative consequences for investors, since public issuers raise capital by selling their securities publicly to an unlimited number of people.

Today the priority of the supervisory work of the competent body on the securities market is to strengthen control of public issuers. In this regard, the requirements on public and private issuers will be defined in relation to:

- the issue and sale of the issuer's securities,
- the disclosure of information,
- supervision.

Standards for the issue of securities will be defined for public and private issuers, including stringent requirements on prospectuses for securities issues by public issuers, and the repeal of the requirement for private issuers to register prospectuses. The sale of securities of private issuers should be allowed outside the trading places run by the organisers of trade on the securities market.

Requirements on the disclosure of the necessary information by public issuers will be established, providing for the presence of a department or person at the issuer's, responsible for the disclosure of information about its activity. For private companies work will be conducted to simplify disclosure requirements, with the exception of companies subject to disclosure requirements under the special law of the Republic of Kyrgyzstan (commercial banks, insurance companies, etc.).

In addition, the whole policy of regulation of issuer activity is being reconsidered – in the sense of easing the regulation of private issuers and strengthening the supervision of public issuers. The competent government body on the securities market will conduct audits of public issuers. Special requirements for the audit of public companies will be established and the requirements regarding indicators of financial-economic activity and disclosure of information by issuers of listed securities will be tightened.

Regarding the listing of securities, the government must be able to establish minimum requirements for organisers of trade on the securities market. It is important to improve the responsibility of organisers of trade on the securities market for the listing of securities. This creates double supervision of issuers of listed securities – by the government and by the organiser of trade, which will lead to a higher status for listed securities.

With a view to protecting protect stock-market investors, measures will be taken to improve standards and rules for the activity of professional participants in the securities market. Requirements for indicators of the financial-economic activity of professional participants must be raised. Rules must also be drafted on brokers' advice to their clients, which will include the compulsory disclosure by brokers to all potential investors of the information contained in the prospectus for securities issues, as well as information about the risks associated with securities. The rules must also provide for the compulsory recommendation of brokers for the provision of securities to investors.

When these measures are implemented, investors will be able to make appropriate investment decisions, which in turn will avoid various negative consequences. They should also prevent untransparent and risky companies from raising capital from unqualified investors.

Considering that a reliable system for registration of securities ownership is one of the necessary conditions for a stable and attractive national stock market and for investors' confidence in the securities market, a registration system must be developed in order to minimise the risk of infringing investors' rights.

In this regard, we intend to conduct work to complete the legislation and adopt measures to raise standards of activity of professional participants in the securities market, particularly registrars. These measures include: a policy to ensure the reliability of registrars and their independence from issuers; stricter requirements regarding the minimum amount of registrars' own funds; minimum requirements on the composition and structure of registrars' assets; a requirement for registrars to keep compulsory duplicates of information about securities ownership off their premises; compulsory insurance of risks of the accounting system for those keeping registers of securities owners; a minimum amount of compulsory insurance and a list of the risks insured (technical failure, errors or illegal action by staff, damage to the issuer, etc.).

The other important area of work on building investor confidence in securities is the popularisation of the securities market. Efforts in this area will not only attract new participants to the stock market, but also protect them from possible errors and risks.

The stock exchange can be popularised through work in the following two main areas:

- information and education,
- training.

Information and education on the securities market will be achieved by the systematic disclosure of information about the securities market by market participants – the government and professional securities market participants. It is important to look at ways to disseminate information about the stock market through the media. Information on the development of the securities market can be provided through close cooperation with the media and by organising seminars and conferences on market issues, including the rights and obligations of investors, investment risks and the activity of securities market participants.

Cooperation with the media must be regular with the aim of providing frequent information on the abovementioned issues, the activity of the government body (drafting regulations, enforcing compliance by issuers and professional participants with the legislation governing the securities market, the results of audits of issuers and professional participants in the securities market, etc.), and the current situation on the stock market. Timely and full information for investors about the securities market of Kyrgyzstan should also be posted on the official website of the State Commission on the Securities Market.

The development of the securities market and its increasing complexity requires an organised process of drafting new frameworks and constant raising of the qualifications of the main participants (issuers, dealers, brokers, analysts, etc.). Training is key to popularising the securities market. This mainly consists in preparing market specialists and raising their professional standards.

In addition, given the content of the regulations governing securities market issues, there is a need for educational seminars on issues related to market operation. In this regard, the government body, together with educational facilities, needs to draft educational programmes to train securities market specialists that encompass all the regulatory issues of stock market operation.

The popularisation of the stock market is one of the main conditions for further market development. It is also a complex task, because it requires significant financing. We therefore need to design a programme that provides for the achievement of all the main aspects of popularising the securities market, including financing.

Starting last year, as part of the project on strengthening corporate governance, the State Commission on the Securities Market, together with experts from the Asian Development Bank, started work on strengthening the capacity of the State Commission on the Securities Market to build public confidence in the capital market.

An important step for the further development of the Kyrgyz stock market is its integration with other regions, first of all with other Central Asian countries. The stock markets of these countries are currently at different stages of development – some have fairly developed markets with large reserves of investment capital; whereas infrastructure is only just developing in others. The integration of the stock markets of the Central Asian countries will spur their development, and which will enable the

Kyrgyz market to attract investment through a broader investor base and through the provision of services on the markets of other countries.

Given that consolidation of the financial system is one of the most important tasks for any government, since steady economic growth requires the mobilisation of the necessary financial resources, every effort must be made to raise investor confidence in the securities market.

To achieve this, we must first remove barriers preventing issuers, professional participants and other participants on the Kyrgyz market from operating on foreign securities markets; increase their attractiveness for foreign investors, by raising the quality of their investor services; and improve the activity and lower the risk of securities market operators.

We must also draft and enact unified principles and rules for the regulation of the activity of professional participants in the securities markets of Central Asia, which provide for:

- access to professional activity on securities markets;
- unified principles of activity on the organised securities market (system of listing and disclosure, organisation of trading and supervision of securities transactions);
- reliable registration of securities ownership.
- an unified approach to creating a system of disclosure by participants on the securities market;
- more accessible ways to exchange of information between securities market regulators in Central Asian countries.

To achieve these aims, the State Commission on the Securities Market:

- has initiated work on harmonisation of legislation with the competent bodies on securities market regulation in the Central Asian republics;
- is making propositions to hold meetings and consultations with the competent bodies on securities market regulation in the Central Asian republics on a regular basis, with the aim of providing effective cooperation.

An important aspect of integration is cooperation between our governments on the supervision of the activity of professional participants in the securities market.

As you have gathered from this paper, nothing extraordinary is happening in Kyrgyzstan to build investor confidence in securities. This is quite true, because to tackle this issue, we have chosen the path, already approved by many countries, of painstaking, intensive and consistent work, which, unfortunately, has been paved not only with successes, but also with errors and losses. In almost 13 years of the independence of Kyrgyzstan and the existence of our stock market, we have realised this, which I think is already an achievement. I wish you all every success on the paths you choose to win the hearts of investors.

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