

# The Role of Stock Market on Economic Development of Rwanda; A Case Study of Rwanda Stock Exchange

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**Abstract:** *In Rwanda there is need to provide funds to start new businesses and to expand existing businesses and industries. The stock market provides companies and the government with an avenue to raise Stock through the sale of shares and bonds to the public. The stock markets bring together those with surplus funds and those with a deficit and facilitate the exchange of the monies. This has however not gotten to its optimal level due to the following challenges facing the Rwanda stock market. First, in RSE there are a limited number of companies listed in the Rwanda Stock Exchange, the investors in Rwanda have limited investment portfolio and another challenge is the limited access to long term securities. The general objective of this study examined the role of stock market on economic development of Rwanda. This study was adopted descriptive research design. The target population of this study is 12 employees of Rwanda Stock Exchange. The researcher was used an open ended questionnaire as data collection. This means that that researcher collected the data through questionnaire. Researcher was used primary data. The Rwanda economic development has an overall correlation with stock market products of 0.776 which is strong and positive. This means that approximately 77.6% variations of economic development of Rwanda are explained by the stock market products at 5% level of significance. These indicate good fit of the regression equation used. Results indicate that Treasury bond is the most significant in explaining the economic development of Rwanda with a significance of 0.000 which is less than a p-value of 0.05 and beta value is 0.872. Pearson correlation coefficient, ( $r=0.864$ ) shows that there is a positive and high correlation relationship between stock market and economic development where the P-value ( $0.000<0.05$ ). Stock markets also help finance the public sector borrowing requirement while reducing fiscal pressure of debt redemption if maturities of securities are lengthened. To increase the stock market products in the market should ensure an increase in economic growth.*

## 1. Background of the study

The main role of Stock markets is to make funds available for investors undertaking long-term projects at a competitive cost of Stock (Jensen, 2007). Most of the banks in an economy are lenders of short-term. And banks that are specialized in long-term financing are few and usually not equipped with either human or financial resources to handle the financing of all the long-term development projects, especially those related to agriculture, education, and other economic development projects of a country (Werner Baer, 2008).

The economists and policy makers had high expectations about the prospects for domestic Stock market development in emerging economies and, particularly, in Latin America. Unfortunately, they are now faced with disheartening results. Though many still hope that securities markets will develop, the reality is that equity and corporate bond markets in most emerging economies remain highly illiquid and segmented, with trading and capitalization concentrated on few firms (Rajan, William & Zingales, 2013). Stock market in many developing countries, particularly in Latin America and Eastern Europe, have seen listings and liquidity decrease, as a growing number of firms have cross-listed and raised Stock in international financial centers, such as New York and London. Debt tends to be concentrated at the short end of the maturity spectrum and denominated in foreign currency, exposing countries to maturity and currency risks. Moreover, government debt is crowding out corporate bond markets in many countries.

Economic development in a modern economy hinges on an efficient and effective financial sector that pools domestic savings and mobilizes Stock for productive projects (Akingbohunge, 2008). Absence of effective Stock market could leave most productive projects which carry developmental agenda unexploited. Stock market connects the monetary sector with the real sector and therefore facilitates growth in the real sector and economic development.

Stock market increases the proportion of long-term savings (pensions, funeral covers, etc.) that is channeled to long-term investment. Stock market enables contractual savings industry (pension and provident funds, insurance companies, medical aid schemes, collective investment schemes, etc.) to mobilize long-term savings from small individual household and channel them into long-term investments (Kolapo & Adaramola, 2012). It fulfills the transfer function of current purchasing power, in monetary form, from surplus sectors to deficit sectors, in exchange for reimbursing a greater purchasing power in future. In this way, Stock market enables corporations to raise capital/funds to finance their investment in real assets.

Recent empirical research linking Stock market and economic development suggests that Stock market enhances economic development. Countries with well-developed Stock markets experience higher economic development than countries without. Evidence indicates that, while most Stock markets in African countries are relatively underdeveloped, those countries which introduced reforms that are geared towards development of Stock markets have

been able to grow at relatively higher and sustainable rates (Perkins & Block, 2012). A study in 2011 showed that South Africa, the country whose Stock market is the largest and most developed in Africa, in terms of market capitalization and trading volume, has been growing significantly since 2000.

Countries like Egypt, Ghana, Tanzania, Botswana and Mauritius, whose Stock markets have been developing recently, were able to realize average per capita growth rates of more than 2.8% for the past 8 years. However, some economies which did not have formal or effective Stock market like Lesotho, Seychelles and Ethiopia could not manage to realize average per capita growth rates above 2.7 % over the past 8 years. Even those countries with small and less developed Stock market like Swaziland and Uganda did not manage to realize average per capita growth rates above 2.7 % during the past 8 years (CBL Economic Review, August 2009).

In Rwanda, Stock market also provides equity Stock and infrastructure development Stock that has strong socio-economic benefits through development of roads, power plant ,water and sewer systems, housing, energy, telecommunications, public transport, etc. These projects are ideal for financing through Stock market via long dated bonds and asset backed securities. Infrastructure development is a necessary condition for long-term sustainable growth and development. In addition, Stock market increases the efficiency of Stock allocation by ensuring that only projects which are deemed profitable and hence successful attract funds (Mathu, 2014). This will, in turn, improve competitiveness of domestic industries and enhance ability of domestic industries to compete globally, given the current momentum towards global integration. The result will be an increase in domestic productivity which may spill over into an increase in exports and, therefore, economic growth and development.

Moreover, Stock market promotes public-private sector partnerships to encourage participation of private sector in productive investments. The need to shift economic development from public to private sector to enhance economic productivity has become inevitable as resources continue to diminish. It assists the public sector to close resource gap, and complement its effort in financing essential economic development, through raising long-term project based capital. It also attracts foreign portfolio investors who are critical in supplementing the domestic savings levels. It facilitates inflows of foreign financial resources into the domestic economy. The aim of this research is to examine the role of Stock market to the economic development in Rwanda.

## 2. Statement of the Problem

More liquid markets can create long-term investment and hence economic development through lower transaction cost. Rajan and Zingales (2008) argued that stock market size is correlated to growth of financial dependent firms. Many of the studies done have supported the view that stock markets promote economic development. It has been observed that well functioning stock market increases

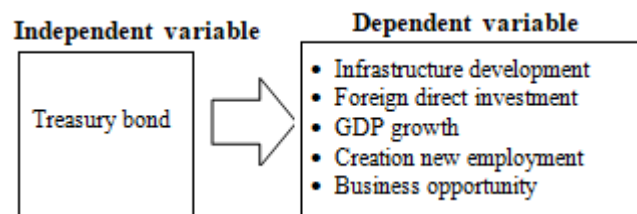
economic efficiency, investment and growth. Rwanda stock market has been described as narrow and shallow. There has been significant focus on the stock market with for example the institutional development of the stock market and introduction of new instruments in the bonds market. It has been assumed that these efforts will facilitate mobilization of adequate resources and allocation of these resources efficiently to achieve development objectives. In the last three decades, the correlation between financial sector and economic development has been a subject of high interest among scholars, policy makers and economists on the entire globe.

In Rwanda there is need to provide funds to start new businesses and to expand existing businesses and industries. The stock market provides companies and the government with an avenue to raise Stock through the sale of shares and bonds to the public. The stock markets bring together those with surplus funds and those with a deficit and facilitate the exchange of the monies. This has however not gotten to its optimal level due to the following challenges facing the Rwanda stock market. First, in RSE there are a limited number of companies listed in the Rwanda Stock Exchange, the investors in Rwanda have limited investment portfolio and another challenge is the limited access to long term securities. It is on this regard that the researcher was enthused to carry out the research on the role of stock market on developing economy.

## 3. Objective of the Study

To examine the influences of Treasury bond to the economic development of Rwanda.

## 4. Conceptual Framework



## Research Design

Research design is “a blueprint for conducting a study with maximum control over factors that may interfere with the validity of the findings. This study was adopted descriptive research design. This approach provides an opportunity to establish the relationship between Stock market and economic development in Rwanda (Glass & Hopkins, 2008).

## Population of the Study

According to (Grinnell & al., 2008), Study population is a totality of persons or objects with which a study is concerned. The population under this research consists of organization staff from different levels will conduct mainly in Rwanda Stock Market. In other words, the target population is individuals who are in position to respond the questionnaire and to whom the results of the survey apply. The target population of this study is 12 employees of Rwanda Stock Exchange.

**Data Collection Instruments**

The researcher was used an open ended questionnaire as data collection. This means that that researcher collected the data through questionnaire.

**5. Research Findings and Discussion**

**Table1:** The role of Treasury bond on developing Rwanda economy

Statements	SA	A	UN	D	SD
1. Those who have already invested in TB gets more profit	4 (33.3%)	8 (66.7%)	-	-	-
2. TB pays more profit	4 (33.3%)	8 (66.7%)	-	-	-
3. Invested in TB is more profitable than others investment.	10 (83.3%)	-	-	2 (16.7%)	-
4. Government use TB as one source of its budget deficit	12 (100%)	-	-	-	-
5. Government use TB to finance its infrastructure project and others government programs	12 (100%)	-	-	-	-
6. Those who have invested in TB got profit twice a year	12 (100%)	-	-	-	-
7. Government of Rwanda has been financed many projects through TB	12 (100%)	-	-	-	-
8. Government bond is consider as zero investment risk	10 (83.3%)	2(16.7%)	-	-	-

Source: Primary data, 2018

Nowadays government of Rwanda issues Treasury bond after three months, through Central bank of Rwanda (BNR). The investors appreciate so much the profit they get from Treasury bond. 33.3% were strongly appreciated and 66.7% were appreciated too. Nowadays government of Rwanda use Treasury bond as one of the source of government budget for financing the government infrastructures development, 100% of respondents were strongly appreciated. Those who invested in TB they get profit twice a year, after six month. Currently many big project of Rwanda Government was financed by the issues of Treasury bond and Euro bond. In 2013 Government of Rwanda issued the Euro bond of \$ 400 million in order to finance the big infrastructure projects, e.g: Convention Center, Nyabarongo hydro power and buying new Airplane of RwandAir.

On April 25th 2013, Rwanda completed the issuance of a 10-year \$400m on Irish Stock exchange market the first of its kind in East Africa. The bond was highly over-subscribed and priced to perfection. The bond which carries a coupon (price) of 6.625%, recorded large order book with a total subscription of \$3.5 billion, more than 8.5 times over and above the intended amount of \$400 million with over 250 investors across the globe participating.

The 10-year bond was sold at a yield of 6.875 percent and sold off marginally early on Friday before going back to par later in the day. Strong investor demand pushed the yield lower than the initial guidance. Orders worth more than US\$3bn were placed for the ten-year bond, bringing the yield down to 6.875%. The Eurobond is an attractive investment owing to Rwanda's low debt burden, rapid

economic growth, stable macroeconomic performance and relative political stability. However, the yield, although lower than expected, is still higher than the yield on other African bonds, including Nigeria (4.1%), Senegal (5.4%) and Tanzania (6.3%). Strong, consistent economic policymaking has boosted the Rwandan economy since the genocide in 1994, but the landlocked country has only a small domestic market, little access to international markets and few natural resources, leaving it unable to offer the same revenue stream to potential creditors as oil-exporting countries such as Nigeria.

Rwanda will need to invest the Eurobond funds smartly if it is to expand the economy's productive capacity and lead to faster economic development in the future. Half of the funds was used to retire more expensive debt (US\$120m for the Kigali Convention Centre and US\$80m for RwandAir), while US\$150m was towards completing the Kigali Convention Centre and US\$50m to completing the Nyabarongo hydropower station. This appears to strike a sensible balance between reducing the servicing costs of expensive short-term debt and improving the country's power and tourism infrastructure.

**6. Conclusion**

Stock markets also help finance the public sector borrowing requirement while reducing fiscal pressure of debt redemption if maturities of securities are lengthened. Governments can also raise long term funds through the stock market and enhance the creation of a robust yield curve. The stock market contributes to the economic development of Rwanda. The results of the study suggest that the stock market growth and economic development have long-run relationship. It reveals that the stock market liquidity do help to improve the future economy development of Rwanda. The findings are consistent with existing theoretical framework as illustrated by several authors about the relationship between stock market and economic development. This study also concludes that stock market development affects the development of Rwanda. This study also revealed that stock market products change in stock market price and trading volume affect economic the economic development.

**7. Recommendations**

- To increase the stock market products in the market should ensure an increase in economic growth.
- Increasing the number of listed companies there is need to ensure stable macroeconomic environment, encourage foreign multinational companies (MNCs) or their subsidiaries to be listed on the Rwanda Stock Exchange.

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