

Raising Finance in the Kenyan Bond Market (A Case of Listed Companies on the Nairobi Stock Exchange)

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Abstract
This study sought to establish the potential of the bond market in raising corporate finance in Kenya. The study was guided by the following specific objectives: to evaluate the benefits derived from raising corporate finance in the bond market in Kenya; to analyze challenges faced in raising corporate finances in the bond market in Kenya; and to examine the possible interventions that can be used to address the challenges faced in raising finances in the bond market and enhance performance of the bond market in Kenya. The study focused on all the firms listed on the Nairobi Stock Exchange, whose number stood at 48 was obtained from the Nairobi Stock Exchange report (March 2011). Stratified random sampling was used to arrive at the sample size. From each stratum, 50% of the companies listed on the Nairobi Stock Exchange were selected at random, making a sample of 25 companies. Each of the organizations was represented by five respondents: the Head of the Finance function, and four employees from the treasury and shares/bonds departments. Primary data was collected using a semi-structured questionnaire, which was self-administered. A sampling frame is a list from where the population is drawn. A list of Further, a listing of the Heads of Finance of each of the listed firms that have issued corporate bonds was obtained from the respective human resource departments. Out of the 125 questionnaires that were sent out, 95 of them were returned completed (76%) response rate. The high response rate could be attributed to the personal efforts of the researcher, who made a follow up of every questionnaire sent out. The data pertaining to the profile of respondents was analyzed by employing content analysis while descriptive statistics were used to analyze data pertaining to the objectives of the study. Computation of frequencies and percentages, standard deviations and were used in data presentation. The possible interventions include: undertaking corporate sector and banking reforms; ensuring effective information disclosure; formulation and implementation of policies to strengthen market infrastructure; making regulations favorable to both bond issuance and to the operations of local and foreign investors; development of the money market maybe in terms of the system; diversification of investor base; enhancing taxation policies for both issuers and investors; ensuring a secure and efficient custodial system; and undertaking education. In view of the findings and conclusions of the study, the following recommendations are made for policy and practice: For a bonds market to contribute significantly to the development process, it requires that the market caters for a diverse risk preference, is liquid, efficient and has minimal volatility. To achieve this, there must be a sound fiscal and monetary policy, effective legal and regulatory framework, secure and efficient settlement and custodial system, effective information disclosure system, a diversified investor base, and favorable tax policies. For treasury bonds especially, there is need for an effective financial system, a sound and prudent debt management and credible and stable government. In addition, the development of a well-functioning money market is essential in enhancing liquidity of the market. An active money market is the precursor to an active secondary bond market.
Keywords: Bond Market, Listed Companies, Nairobi Stock Exchange, Corporate Bonds, Stock Market

ABBREVIATIONS AND ACCRONYMS

AIMS	Alternative Investment Market Segments
CAPM	Capital Asset Pricing Model
CBK	Central Bank of Kenya
CMA	Capital Markets Authority
EADB	East African Development Bank
ER	Ericsson and Renault
FISMS	Fixed Income Securities Market Segments
GDP	Gross Domestic Product
IFC	International Finance Corporation
IOU	I Owe You
IPO	Initial Public Offer
MDGs	Millennium Development Goals

MIMS	Main Investment Market Segments
MRM	Mabati Rolling Mills
NPV	Net Present Value
NSE	Nairobi Stock Exchange
OECD	Organization for Economic Cooperation Development
OTC	Over-The-Counter
SPSS	Statistical Package for Social Sciences
SPV	Special Purpose Vehicle
US	United States

1.0 INTRODUCTION

This chapter introduces the study. The chapter presents background of the study, statement of the problem, objectives of the study and significance of the study, the research questions, and the scope of the study.

1.1 Background of the Study

The 1980s and 1990s have seen developing countries embark on revitalizing capital markets to enhance mobilization of long-term capital. The evidence that long term capital is positively related to economic growth has justified this effort. Further, the recent need to meet the Millennium Development Goals (MDGs) demands mobilization of adequate financial resources, and this has kept the momentum for capital market development high (Mbewa, Ngugi and Kithinji, 2007).

Kenya has followed suit in developing its bonds market in the capital market reform process. Although treasury bonds were introduced into the market in the early 1980s, the market faced various challenges that constrained its development. Until 2001 when the government took a deliberate effort to shift domestic debt to long term instruments, government bonds maturities were short. Corporate bonds were introduced in mid-1990s, but the growth momentum was not maintained. Ten years after the first bond was listed, there are less than ten corporate bonds listed in the market. (Ngugi, 2006). Further, the demand to diversify the bonds with mortgage-backed bonds among the banking institutions and infrastructure bonds has not been successful.

Bonds market is an alternative vehicle for mobilizing finance for both the government and the private sector in financing long term projects such as housing and infrastructure development, in addition to financing government deficit. The development of bonds market plays a crucial role in promoting partnerships in the development process between the government and the private sector. Successful development of bonds market requires a number of conditions such as a developed money market, favorable macroeconomic policies, market participation, appropriate trading system and a sound legal and regulatory framework.

Experience also shows that development of government bonds market is crucial in paving way for development of corporate bonds market.

This study examines the factors influencing raising corporate finance in the bond market, the benefits derived from raising corporate finance in the bond market, the challenges faced in raising corporate finances in the bond market, and the possible interventions that can be used to address the challenges faced in raising finances in the bond market and enhance performance of the bond market in Kenya

1.1.1 Corporate Bonds

Corporate bonds are debt instruments that are issued by corporations considered to be publicly held (McGee, 2002). Generally, a corporate bond is issued as a means of raising necessary funds to allow the company to engage in an expansion project, or to address other corporate projects that are anticipated to increase the profitability of the company over the long term. According to McGee, the expectation is that the corporation will begin to benefit from the project before the bond issue matures, allowing the company to comfortably honor both the face value of the bond and any accrued interest due to the bondholders.

According to Emerick and William (2004), purchasing a corporate bond is usually accomplished through investment brokers. However, it is also possible to acquire a bond issue from a secondary market as well. In general, choosing to purchase the corporate bond through a broker will mean paying the current par value associated with the bond. A third option is to invest in a mutual fund that focuses on the purchase of corporate bonds as part of the fund strategy. Investors who prefer to leave most of the investigation into bond issues with the managers of the mutual fund often favor this approach. There are five main classifications of issuers representing various sectors that issue corporate bonds: public utilities; transportation companies; industrial corporations; financial services companies; and conglomerates. Such issuers may be locally owned or foreign owned companies (Chordia *et al,* 2003).

Why does a firm issue bonds and what influences that decision? In the presence of information asymmetries in capital markets, firms prefer internal to external finance, but at some point as firms grow, self-funding typically becomes insufficient to finance their investment projects and so they turn to sources of external finance either from the markets for equity and debt or banks (Calomiris *et al,* 1995). Most models of firm finance assume that firms require some external finance, from either banks or financial markets, to pursue investment projects and that is available subject to minimum standards of creditworthiness in the eyes of the lender. If creditworthiness grows with size and age then this might suggest that there is simply a life-cycle effect that influences a firm's decision to issue bonds, and if this were the case, in an asymmetric information world, net worth would be an important determinant of that decision. In this paper we argue that there is more to the story.

The evidence in Datta *et al.* (2000), who discuss the factors influencing firm's decisions to enter the public debt market for the first time, and more recently, Hale and Santos (2003), who have addressed the timing of the firm's decision to issue a debt IPO argue that reputation, liquidity as well as firm size and market conditions influence the decision. We attempt to shed further light on the question of the determinants of bond influence by considering the role that financial characteristics, reputation in the bond market, and liquidity incentives motivate firms to raise finance from the repeated issues in the bond market. The current study therefore extends Datta *et al.* (2000) and Hale and Santos (2003) by considering factors that influence firms decisions beyond the bond IPO.

1.1.2 Nairobi Stock Exchange

The Nairobi Stock Exchange (NSE) was established in 1954 as a voluntary association of stockbrokers registered under the Societies Act. The NSE currently has 54 companies with equity listings in the Main and Alternative Investment Market Segments (MIMS and AIMS). There is also a third segment for trading of government and corporate bonds and other fixed-income securities market segment - the FISMS. A fourth segment for trade of derivative instruments is envisioned for the near future. The total equity market capitalization of these 54 companies as at June, 2008 was KShs 1.3 trillion. In 1994, the NSE was at it's peak and was rated by the International Finance Corporation (IFC) as the best performing market in the world with a rate of return of 179% in US Dollar terms. At that time, the NSE had a market capitalization of KShs 137 billion (equivalent to US $ 3.1 billion at the then prevalent exchange rate of KShs 45 to 1 US$).

The Stock Market is a market which deals in the exchange of shares of publicly quoted companies, and government, corporate and municipal bonds among other instruments for money (Nairobi Stock Exchange, 2008). The Kenyan stock market; the Nairobi Stock Exchange, which was formed in 1954 as a voluntary organization of stockbrokers, is now one of the most active markets in Africa. It is located on 2nd Floor, Nation Centre on Kimathi Street, in Nairobi.

Nairobi Stock Exchange is Africa's fourth largest stock exchange in terms of trading volumes, and fifth in terms of market capitalization as a percentage of GDP. According to the Nairobi Stock Exchange report (December, 2007), as a capital market institution, the Stock Exchange plays an important role in the process of economic development: It helps mobilize domestic savings thereby bringing about reallocation of financial resources from dormant to active agents; Long-term investments are made liquid, as the transfer of securities (shares and bonds) among the participating public is facilitated; The Exchange has also enabled companies to engage local participation in their shares ownership, thereby giving Kenyans a chance to own shares of reputable firms; Companies can also raise extra finance essential for expansion and development.

1.1.3 Corporate Bond Market in Kenya

The bonds market in Kenya trades in both the treasury and corporate bonds. While treasury bonds were introduced as early as mid-1980s, corporate bonds came to the market in 1996 during the reform period. Despite the early initiation of treasury bonds in the market, the market remained almost stagnant, with the government using treasury bills to finance domestic debt. It was not until 2001 when the government took a deliberate effort to develop the market that activities of the treasury bonds market increased. However, corporate bonds market is yet to gain its growth momentum (Mbewa, Ngugi and Kithinji, 2007).

Central bank of Kenya has multiple interests in the development of bond markets. At a fundamental level the government Treasury bond helps to fund budget deficits. It is important to note that Central Bank of Kenya has increased its issuance of long-term Treasury bonds currently with 12-year tenor thus increasing the maturity period of government debt. Also Central Bank acts as agents for the government in various aspects of the management of government debt. They oversee clearance and settlement system and they are responsible for the stability of the financial system often directly supervising banks. This multiplicity of interest means that the policy issues that arise are very diverse.

Though Kenya's financial sector is well diversified, it needs to be developed further. The banking sector is dominated by ten largest commercial banks, which accounts for over 77% of all deposits held by banking institutions. Insurance and banking sector's are quite competitive, but need to be restructured so that we have competitive bidding for government Treasury bills auction. The assertion is that "limiting" participation in the Treasury bill auction to only a few players would restrict competition and consequently the result not market driven. A developed Treasury bond market has a direct impact on the capital market. The two sectors could be strengthened through more mergers and consolidations, which will ensure efficient competition and further deepening of the capital market

Without a functioning bond market firms lack a clear measure of the opportunity cost of funds. They will rely on commercial banks for debt financing. The same constraint that prevents the development of bond markets also leads banks to prefer short term credit which implies higher risks for business. The government massive infrastructure development i.e. reconstruction of our depilated roads network can be privately funded. Often in such cases the commercial feasibility depends on the funding structure that minimizes considerably risks. This requires long term (usually 20 years or longer) flexible or fixed interest rate, attractively priced debt instruments. Debts of this nature can be provided by a liquid traded bond.

Moreover in the 2005/2006 budget speech by the Minister of Finance securitization based on bankable assets were a given a boost particularly for institution offering infrastructural services to raise long term capital by encouraging such institution to set up special purpose vehicles (SPV) for the purpose of issuing asset backed securities. The Minister's proposal that income from SPV to be exempted from income tax is highly commendable. Now that the Minister paved the way in the budget speech we would see more of structured corporate bonds issued through a special purpose vehicles (SPV) i.e. securitization of credit card receivables, infrastructure bond and mortgage backed bonds in our capital market. It is equally important to note that the limited role of corporate bond market is a function of how companies have been financing their investments projects-especially medium to long term fixed investments. The yield of a bond has to compensate investor for the opportunity cost of funds, default and liquidity risk If the return of the bond is distorted among clients and there is no active secondary market investors will be reluctant to participate in the development of the corporate bond market. In any case a flourishing corporate bond market contributes to deepening of the capital market, is a source of fund for infrastructure and facilitates competition in the financial services. With developed bonds market banks can price debt more efficiently.

Broader use of corporate bonds in Kenya is impossible without making a number of changes that will involve, for one thing, the legislative and procedural areas (amendments to selected rules of law, ensuring effective functioning of the court structure, another possibility is also creating a specialized court for the capital market), then the areas of the capital market (ensuring better transparency and maximum possible information openness, and that, among others, with help of modern information and telecommunication technologies, connecting the Nairobi Stock Exchange with other leading stock exchanges or finding new ways of using debentures for securitizing of assets, for example), but also the corporate field (particularly successful restructuring, or enhancement of the information facilities of the company), and the macro-economic situation in Kenya (especially creating a stable market environment or changing the pension scheme, which will use bonds as a suitable investment instrument)

1.2 Statement of the Problem

Raising corporate finances on the bonds market remains one of the greatest enigmas of modern finance. Hasbrouck and Duane (2001) argued that there was no convincing explanation for issuance of corporate bonds. To resolve the dividend puzzle, Chen *et al,* (2005) conclude that the cardinal thrust of academic research must turn toward learning about motivation and on what perceptions this motivation is based. There is scarcity of literature on corporate bond issuance. Previous studies indicate that there is a life cycle in the firm's financing behavior. Firms borrow from banks initially but may later go to public debt markets for debt finance. This sequence is often described as the "pecking-order" hypothesis of Myers and Majluf (2001). This raises the question of what influences a firm's decision to issue public debt. Strikingly, little research has been devoted to bond IPOs, in sharp contrast to equity IPOs. This is somewhat surprising given that bond financing is more important for firms than equity financing in terms of the dollar value of funds raised. In this paper we attempt to shed some light on this question.

Studies related to the bond market in Kenya include the following:

Ayieye (2004) studied the factors considered by individual investors in investing shares of companies quoted at the NSE; Gakuru (2004) focused on the relationship between stock returns and bond returns in the NSE; Njogu (2003) studies the price impacts of commercial paper issue announcement. a case of quoted companies which have issued commercial papers in Kenya; Muriuki (2003) focused on the determinants of priority structure of corporate liabilities for firms quoted at the NSE; Mbugua (2003) focused on the factors influencing development of the corporate bond market in Kenya; Abai (2003) studied the determinants of corporate debt maturity structure for companies quoted at the NSE; Ng'ang'a (2000) focused on commercial paper as a source of finance for Kenyan companies

None of the above studies focused on the potential of the bond market in raising corporate finance in Kenya. Whereas research has tended to focus on the technicalities of corporate bond market development in the developing countries, this study attempts to complement this work with research into the factors influencing issuance of corporate bonds in the developing countries. Referring to the experiences of Kenya, this study tries to shed light on why these markets have remained limited in size and, in comparison with equity markets, failed to expand significantly during the decade prior to the economic crisis. The study also assesses some changes brought about by the economic crisis and suggests some broad policy preconditions for corporate bond market development.

1.3 Purpose of the Study

This study sought to assess the potential of the bond market in raising corporate finance in Kenya.

1.3.2 Specific Objectives

The study will be guided by the following specific objectives:

(i) To evaluate the benefits derived from raising corporate finance in the bond market in Kenya
(ii) To analyze challenges faced in raising corporate finances in the bond market in Kenya
(iii) To examine the possible interventions that can be used to address the challenges faced in raising finances in the bond market and enhance performance of the bond market in Kenya

1.4 Definition of Terms

The following is the definition of the various terms used in this study:

Corporate Bonds: Corporate bonds are debt instruments that are issued by corporations considered to be publicly held (McGee, 2002).

The Stock Market: is a market which deals in the exchange of shares of publicly quoted companies, and government, corporate and municipal bonds among other instruments for money (Nairobi Stock Exchange, 2008)

2.0 LITERATURE REVIEW

2.1 Introduction

This chapter presents a review of the literature related to the purpose of the study. The chapter is organized according to the specific objectives in order to ensure relevance to the research problem. The review was undertaken in order to eliminate duplication of what has been done and provide a clear understanding of existing knowledge base in the problem area. The literature review is based on authoritative, recent, and original sources such as journals, books, thesis and dissertations.

2.2 Benefits derived from raising corporate finance in the bond market

Corporate bonds (also called corporates) are debt obligations, or IOUs, issued by private and public corporations. According to Glosten and Lawrence (1988), companies use the funds they raise from selling bonds for a variety of purposes, from building facilities to purchasing equipment to expanding the business. When you buy a bond, you are lending money to the corporation that issued it. The corporation promises to return your money, or principal, on a specified maturity date. Until that time, it also pays you a stated rate of interest, usually semiannually. The interest payments you receive from corporate bonds are taxable. Unlike stocks, bonds do not give you an ownership interest in the issuing corporation (Fleming, 2003). Corporate bonds are one of significant capital market instruments and at the same time a potential source of company finance. They are long-term, mass issued, tradable, debt securities issued by corporate bodies, confirming the obligation of an issuer to pay the bondholder revenues and pay off the nominal value under set terms.

Provides relatively lower funding cost to the issuer than the traditional banking loans and information disclosure about the firm that helps to access public funds rapidly: Bond market development is highly recommended for the fact that it provides lower funding cost to the issuer than the traditional banking loans and information disclosure about the firm that helps to access public funds rapidly. Hakansson (2001) documented the following advantages of corporate bond market when examining principal differences between an economy with a well developed corporate bond market and an economy with a well developed bank based market: there is greater accounting transparency; large community of financial analysts; respected rating; wide range of corporate debt securities; derivatives demanding sophisticated credit analysis; efficient procedures for corporate reorganization and liquidation.

Option of raising large amounts of money as compared to raising funds using equities: From the point of view of an issuer, i.e. a company, corporate bonds represent an alternative source of financing. Issuing corporate bonds can be used firstly for cash flow improvement, secondly for financial structure optimization, however also within ownership restructuring (Choe, Masulis, Nanda, 2003). Cash flow improvement can be achieved also by applying measures in terms of profit rate (decreasing costs and increasing returns), property (particular parts of property control including receivables) and further by gaining external financial sources of both a long-term and a short-term nature. Corporate bonds are one of alternative external long-term sources.

Corporate bonds represent an instrument that can be used by company managements for implementing both the rule of a horizontal property-financial structure and the rule of a vertical financial structure, however also for meeting the effort to reach an optimal financial structure. Currently, though, the financial sources selection by Kenyan company managers complies with a hierarchical order theory; companies generally prefer financing from internal sources and if they are forced to use external finance sources, they prefer gaining money from credits or issuing corporate bonds to gaining it from share emissions (Njogu, 2003). Within a process of ownership restructuring corporate bonds can be applied in integrations in a form of acquisitions. They can also be used by strategic alliances based on a common property – either in a form of a holding or a joint venture. Corporate bonds may play their roles even in other types of ownership restructuring that may rest in an exchange of convertible corporate bonds for shares or in setting up a claim with put bonds. Corporate bonds can be used as an active or preventive tool for protection against a hostile take over.

Provides a diversification of fund sources and allows to tailor risk reward profile to its preferences: According to Herring and Chatusripitak (2000), the absence of a bond market may render an economy less efficient and significantly more vulnerable to financial crisis. In the same vein, Trigueros (2000) concludes that a proper legal environment and the protection of minority shareholders and bondholders could foster the development of the financial sector and, in turn, contribute more efficiently to the economy's rate of growth. Development of the bond market provides diversification of fund sources and allows to tailor risk reward profile to its preferences concludes Hakansson (2001). Hotchkiss and Ronen (2002) noted that company bond and stock returns positively correlate implying both securities move in response to issuer-specific information (Kwan, 2006). Thus, the bond market is intricately linked to the stock market underscoring the importance of bond market to corporate financing.

According to Myers (2004), there are several good reasons for developing bond market. The most fundamental reason is to make financial and capital market more complete by generating market interest rates that reflect the opportunity cost of funds at each maturity. This is essential for efficient investment and financing decisions. Moreover the existence of tradable instruments helps risk management. Further the use of financial guarantees and other types of underwriting is becoming increasingly common in corporate debt market as financing deals become more complex (Pagano *et al,* 2002). If borrowers have available to them only a narrow range of instruments (in terms of maturity and currency) then they can be exposed to significant mismatches between their assets and their liabilities.

The risks entailed by such mismatches have to be managed and the ability to do so will often depend on whether certain exposures can be adequately hedged (Kaplan and Zingales, 2003). Liquid markets help capital market participants to hedge their exposures. If bond market is not well developed for instance firms may have to finance the acquisition of long-term assets by incurring short-term debts. As a result their investment policies may be biased in favor of short-term projects and a way from entrepreneurial ventures.

According to Krishnaswami *et al,* (2000), the relationship between intermediation through banks and disintermediation through capital markets is controversial. Even in developed economies this two rather distinct systems have grown up one where capital markets are very important and one where banks dominate. A question that arises concerns the role commercial banks can play in developing our bond markets. The view that increased corporate bond issuance just takes away profitable business from commercial banks is oversimplified.

According to OECD (2005), investors buy Corporate Bonds for a variety of reasons:

Attractive yields: Corporate bonds usually offer higher yields than comparable-maturity government bonds. This high-yield potential is generally accompanied by higher risks. Yield is a critical concept in bond investing, because it is the tool you use to measure the return of one bond against another. It enables you to make informed decisions about which bond to buy. In essence, yield is the rate of return on your bond investment. However, it is not fixed, like a bond's stated interest rate. It changes to reflect the price movements in a bond caused by fluctuating interest rates (OECD, 2005).

Dependable income: People, who want steady income from their investments, while preserving their principal, include Corporate Bonds in their portfolios. Like all bonds, corporate bonds tend to rise in value when interest rates fall, and they fall in value when interest rates rise. Usually, the longer the maturity, the greater the degree of price volatility. By holding a bond until maturity, you may be less concerned about these price fluctuations (which are known as interest-rate risk, or market risk), because you will receive the par, or face, value of your bond at maturity. Some investors are confused by the inverse relationship between bonds and interest rates - that is, the fact that bonds are worth less when interest rates rise; safety - corporate bonds are evaluated and assigned a rating based on credit history and ability to repay obligations and the higher the rating, the safer the investment; diversity - corporate bonds provide the opportunity to choose from a variety of sectors, structures and credit-quality characteristics to meet your investment objectives; and marketability - if you must sell a bond before maturity, in most instances you can do so easily and quickly because of the size and liquidity of the market (OECD, 2005).

A real and optimal structure of financial sources is a topical problem about which there has been a lively discussion. There are vast discrepancies between the opinions on the shares of internal and external, one's own or extraneous financial sources. Holmstrom and Tirole (2002), state that 60 to 90 % of financial needs in developed countries of European Union and Northern America are financed from undistributed profits, i.e. from one part of internal finance sources. However, the role of depreciation write-offs as an indispensable part of internal financial sources should not be ignored.

Corporate bonds can present an instrument of increasing of company competitiveness and can contribute to creation of competitive advantage: According to Chordia, Sarkar, and Subrahmanyam (2003), the advantages of issuing corporate bonds can be seen in achieving a higher degree of company capital structure flexibility, and a company is thus more able to react promptly to constantly changing conditions, which consequently leads to generating larger financial sources. Liu, Qi, and Wu (2004) assert that corporate bonds can present an instrument of increasing of company competitiveness and can contribute to creation of competitive advantage.

Corporate bonds emissions can make up a considerable amount of money provided by a large number of creditors: Another advantage means that corporate bonds emissions can make up a considerable amount of money provided by a large number of creditors. As a consequence of a risk distribution among a large number of creditors the bond emission is a lower costs alternative in comparison to bank loans under a certain debt level condition. Also a procedure used by certain foreign companies in terms of reaching and maintaining an optimal financial source structure is worth mentioning (Levin *et al,* 2004).Companies first accept bank loans, and that is to the degree to which the loan is cheaper and otherwise more advantageous than bonds emissions. Then they issue bonds and use a part of the gained finance to paying loans and other liabilities off, which increases the ability to accept other bank loans. After reaching the top limit of bank loans a company issues bonds again and the cycle repeats itself. In the third cycle a company issues shares and a part of sources is used for paying off the bank loans, paying off the bonds and the rest is used to finance a further development. Then a company increases bank loans and the cycle repeats itself again.

Returns of corporate bonds represent a tax base and in case of a company profitability an interest tax shield can be used: According to Myers and Majluf (2001), a significant advantage rests in the fact that returns of corporate bonds represent a tax base and in case of a company profitability an interest tax shield can be used. Furthermore shareholders do not lose a company activity control when issuing corporate bonds, while issuing them often does not even need a collateral in a form of a property pledge (Mikkelson and Partch, 2001). It is due to say that as a consequence of an obligation to pay back the principal and returns of bonds managers get a clearer view of rate of returns and that successful issuing of corporate bonds (especially their placement) is considered a prestigious thing helping the company to gain respect by the public and business partners (Merton, 2005).

2.3 Challenges faced in raising corporate finances in the bond market

Market imperfections such as underdeveloped financial system may constrain firms' ability to fund investments: Corporate finance theory suggests that market imperfections such as underdeveloped financial system may constrain firms' ability to fund investments. To this extent, development economics have largely documented the role of financial market development on economic growth. Well developed stock markets provide liquidity, diversification, and information acquisition, resource mobilization for corporate finance, investment and growth. An active and liquid stock market makes it easy and relatively cheaper for firms to finance their operations through equity capital than debt (Acharya and Lasse, 2005).

Administrative pricing of corporate bonds and price controls fails to reflect risks, thereby preventing effective risk management by issuers and investors: According to Acharya and Lasse (2005), one of the impediments to the development of bond market in Kenya include administrative pricing of corporate bonds and price controls failed to reflect risks, thereby preventing effective risk management by issuers and investors.

Authorities require bank guarantees for corporate bond issuance: Acharya and Lasse (2005) assert that authorities required bank guarantees for corporate bond issuance and still do so today.

Lack of effective market discipline leads to recourse to administrative means, which can give rise to a series of problem: Lack of effective market discipline can lead to recourse to administrative means, which can give rise to a series of problems. In addition, in order for the OTC market to play a dominant role, a proper trading mode should be established to ensure proper assessment of counterparty risks and pricing flexibility; Investor education was not sufficient. To a large extent, many investors used to treat corporate bonds as just another savings deposit product. Whenever a default of corporate bonds occurred, they would turn to government agencies and demand redemption by underwriters. (Pastor *et al,* 2003).

The current Bankruptcy Law does not provide investors with effective liquidation as a form of recourse in the event of default: The protection given by local governments to bond investors undermined the incentive for them to evaluate the risks involved; the current Bankruptcy Law did not provide investors with effective liquidation as a form of recourse in the event of default. In China for instance, the residual assets - and even the issuer - could often simply disappear without going through legal procedures (Pastor *et al,* 2003). Although we have been working hard on a new bankruptcy law, the current one does not provide adequate protection for creditors; the underwriter's role was not properly defined. Underwriting and redemption typically came under the umbrella of central planning and administrative intervention. Furthermore, the underwriter was considered liable when the issuer failed, an arrangement that blurred distinctions between the underwriter, sales agent and redemption agent; and administrative intervention was even stronger in cases of corporate issuer default (Piqueira, 2004).

Lengthy approval procedures for the local issuance of corporate bonds: Regarding the formal procedures for the local issuance of corporate bonds, the approval process in Kenya is a bit lengthier than in other countries in the region with prosperous financial markets. Another restraint on market development is the fact that only 9 corporate bonds are currently listed in the Nairobi Stock Exchange (NSE). Listing more of these bonds in the NSE would accomplish two important goals to promote this market: first, it would provide a valuable safeguard for small investors, and secondly, it would promote the standardization and flow of information through disclosure requirements, which in turn would enhance the price discovery process (Park and Rhee , 2006).

Credit issuer credibility: According to Miller and Puthenpurackal (2002), the disadvantage of corporate bonds rests in the fact that investors require a lot from credit issuer credibility, while returns and principal must be always paid in time regardless the company profit.

Considerable emission costs created by costs of issue: A substantial disadvantage of bonds emissions lies in considerable emission costs created by costs of issue (costs directly connected with issuing corporate bonds) and costs of bonds life cycle (costs connected with the particular emission, arising in course of the life cycle and in connection to paying back the emission).

Illiquidity – A bond may not be fully taken up and this may affect the funds raised by a company: Firms may therefore substitute long-term debt with equity and this would certainly affect their capital structure. The improvement in the quality of information provided by the market to investors and financial intermediaries like banks might lead to increased borrowing and hence more debt. In this regard, debt and equity might complement each other. A good customer-bank relationship could also make it easier and cheaper for firms to obtain debt from banks than through equity market. The literature principally classifies financial structure into whether it is financial developed bank based or financial developed stock market based. Even though literature considers these two structures, another important dimension of financial market worth considering has to do with the impact of bond market development on corporate financing.

Kenya's underdeveloped corporate bond market has distorted the financing structure in the economy, which poses a threat to financial stability, as well as to social and economic development. Setbacks and mistakes had their roots in the specific circumstances of the past. According to Acharya and Lasse (2005), even today, some of these mistakes may still be impeding the development of the corporate bond market in Kenya. Acharya and Lasse listed the following as being some of the impediments to the development of bond market in Kenya: (i) the administrative allocation of quotas for issue size and number of issuers was mandated by the central government to provincial and lower-level governments; (ii) administrative allocation of quotas was often used as a relief measure for financially distressed enterprises; (iii) the absence of a credit rating system made it impossible for investors to obtain a clear idea of risks; (iv) there was a lack of information disclosure to investors, due to (a) inadequate accounting and external audit standards and (b) lack of regulatory emphasis on proper disclosure by issuers as well as prudent analysis by investors; (v) administrative pricing of corporate bonds and price controls failed to reflect risks, thereby preventing effective risk management by issuers and investors; and (vi) authorities required bank guarantees for corporate bond issuance and still do so today.

Since issuance quotas were administratively allocated and prices controlled, and neither information disclosure nor credit ratings were available, bank guarantees seemed to be the natural solution. However, once guaranteed by a bank, the product was no longer a standard corporate debt but, rather, akin to a high-yield deposit at a commercial bank; bond issues were targeted at retail rather than institutional investors, who were capable of risk assessment; effective market discipline was not established. Market forces can discipline both the issuance and trading of corporate bonds as investors exercise their judgment in the choice of products - thereby giving them the final say on issue conditions, prices and consequences of default.

The default of a corporate issuer was not dealt with according to market principles; rather, for reasons of social stability, the underwriter would be requested to issue bonds on its own to meet the obligations of the corporate issuer -with the consequence that the liability of the default issuer was transferred to the underwriter. The problems of some securities companies undergoing liquidation or restructuring were partly attributable to the burden they had to shoulder for the defaulted corporate issuers (Piqueira, 2004).

To foster the development of a corporate bond market, the authorities should consider: increasing the cap on a companies' permissible amount of outstanding debt (currently set to equal the company's paid-up capital); reducing the time necessary to obtain approval from the CBK and the Treasury to issue corporate debt ; reducing the number of track-record years required for a company to be able to issue debt; and facilitating the listing of corporate bonds in the KSE in order to broaden the bond market, safeguard small investors interests, and promote the standardization and flow of information through disclosure requirements (Schinasi and Smith, 2003).

2.4 Interventions that can be used to address the challenges faced in raising finances in the bond market and enhance performance of the bond market

For a bonds market to contribute significantly to the development process, it requires that the market caters for a diverse risk preference, is liquid, efficient and has minimal volatility. To achieve this, there must be a sound fiscal and monetary policy, effective legal and regulatory framework, secure and efficient settlement and custodial system, effective information disclosure system, a diversified investor base, and favourable tax policies. For treasury bonds especially, there is need for an effective financial system, a sound and prudent debt management and credible and stable government. In addition, the development of a well-functioning money market is essential in enhancing liquidity of the market. An active money market is the precursor to an active secondary bond market.

World Bank (2001), Jones (2002) and Christensen (2004) identify various requirements in development of a successful bonds market. They include:

2.4.1 Active money market

An active money market is the precursor to an active secondary bonds market as indicated in Table 2.1. Money markets are essential for conducting indirect market-based monetary policy operations and providing the liquidity necessary for a market in government bonds and private sector debt securities. They also make it easier for financial institutions to cover short term liquidity needs. In addition, it becomes less risky and cheaper to warehouse securities for on-sale to investors and to fund trading portfolios of securities. The development of a well-functioning money market calls for the existence of banks and other financial institutions that are commercially motivated to respond to incentives, so as to actively manage risk and maximize profits. They (banks) must have adequate incentives to develop treasury capacity, which is the ability to actively manage liquidity and interest rate risk. Multilateral trading, where price discovery is by all institutions in the market, is key otherwise large differences in pricing will arise within the market over relatively short intervals, which will reduce the information content of market price signals. Weak banks cause segmentation in the inter-bank market, which leads to volatility in the overnight rate and lack of unified pricing.

Table 2.1: Prerequisites for a successful bonds market

Prerequisite	Benefits
Active money market	Enhances liquidity in the bonds market
Effective policy framework	Defines the path clearly for bonds market development
	Builds credibility
Legal and regulatory framework	Provides necessary oversight of the market and ensures its stability
	Defines parameters linking fiscal budget with security issuance, showing the ceilings, and legal properties of bonds
	Ensures fair, efficient and transparent markets
	Minimizes systematic risk through clearly defined roles and obligations of market participants
Secure and efficient trading and settlement systems	Proper surveillance, settlement, trade and dispute resolution
	Improves market integration
	Increased liquidity
	Reduced operational risk
Quality information disclosure	Improves market access and transparency
	Improves investor confidence Improved participation and liquidity
Broader investor base	Improves competition
	Improves participation and liquidity
	Stabilizes demand
Functional sinking fund and issuer guarantee	Reduces investment risk
	Improves investor confidence
Benchmark issues	Prices corporate bonds and other debt instruments accurately
Favorable tax policies and tax incentives	Improves participation and in turn liquidity through increased transaction volume
	Checks excessive speculation
	Improved savings and investment liquidity
	Increased market competitiveness from decreased cost of capital

2.4.2 Institutional framework

A sound institutional framework for debt management embodying good governance practices, prudent procedures, and strong capacity for managing operational risks is essential for bonds market development. A clear legal framework, well specified organizational arrangements, public disclosure and auditing procedures are key elements of an effective governance structure for debt management. The soundness and credibility of a financial system can be supported by assurances that the debt portfolio is being managed prudently and efficiently. The organizational framework for debt management should be well specified, and must ensure that mandates and roles are well articulated. Sometimes, a risk management office is established to undertake risk analysis, monitor and report on portfolio-related risk, and assess the performance of debt managers against any strategic benchmarks. Debt management activities should be supported by an accurate and comprehensive management information system with proper safeguards.

2.4.3 Legal and regulatory framework

Financial markets do not develop without a sound legal, regulatory and supervisory framework. The regulatory framework for securities markets is usually seen as having three distinct objectives - assurance of fair, efficient and transparent markets; minimization of systemic risk; and, protection for investors and consumers of financial services. The fundamental parts of the legal framework supporting an efficient domestic securities market usually include an explicit empowerment of the government to borrow budgetary rules for the issuance of government securities, rules for the organization of the primary market, the role of Central Bank as a government agent for debt management framework, rules governing issuance of securities, and rules pertaining to the secondary market. A legal framework is important in defining the exact parameters under which fiscal budgeting process will be linked to securities issuance, limiting issuance through debt ceilings or other devices such as sinking funds and defining the legal properties of securities and their use as collateral in transactions.

The rights and obligations of parties to debt contracts in the primary and secondary markets for issuers, investors, and intermediaries need to be defined. Thus, minimum guidelines should exist for disclosure of material information, liability for entities handling third-party investment accounts, and vehicles to allow proper legal recourse against mutual funds, pension funds, and even the government and corporations as issuers.

Effective regulation of the secondary market should include: regulations of market intermediaries, market conduct (including trading rules), market surveillance and transparency requirements. More importantly, providing incentives for the preparation and disclosure of high-quality information, and breaking the hold of banks as monopolisers/controllers of information is important for bond market development.

The regulatory structure of securities markets is, in many cases, built around Self Regulatory Organizations (SROs) such as exchanges and security dealers' associations as a supplement to the government regulatory authorities. SROs typically provide the first layer of regulatory oversight, guiding their members to meet the objectives of regulation.

Non-uniformity of capital requirements across different classes of market participants can be an important factor in creating incentives for self-regulation. If members of securities depository and settlement corporations are required to hold higher levels of capital than nonmembers, the members will have greater incentives to monitor those financial institutions with lower capital requirements.

2.4.4 Trading and settlement systems

This looks at the method of matching trades, settlement, surveillance, dispute resolution, failed trades and defaults. In determining the potential efficiency of the bonds market, an important factor is whether bonds are issued as paper or are paperless (dematerialized) securities registered in security accounts. Dematerialization of securities ensures that transactions take place quickly and cheaply and that security accounts protect investors against destruction, loss, theft, or forgery of paper securities, eliminating the problem of tainted script.

Organizing the central depository as a separate agency, even if located within the Central Bank, allows for a clear delimitation of responsibilities, the possibility of independent oversight and, at a later stage, full independence of the system. If custody is fully or in part

privately provided, governance arrangements and oversight must be sound. Because of the centralized nature of a securities depository, policy makers might find regulation of the fee structure necessary to prevent monopoly pricing. Efforts to link custody arrangements on a cross border basis should be sought at a later stage to broaden the market base.

For an effective secondary market infrastructure, trading and information systems that facilitate an efficient completion of transactions are key. The automated trading systems are increasingly the preferred avenue for most countries; with their costs three to four times lower than those of traditional exchanges using a floor and open outcry method.

2.4.5 Information disclosure

This entails adopting internationally accepted accounting practices, and corporate governance guidelines. Improving market access and transparency by providing high quality information about debt structure, funding needs and debt management strategies to market participants and the public at large is essential. It is the prerogative of the government in consultation with capital markets and Central Bank to provide appropriate guidelines on disclosures. In designing the overall regulatory and disclosure framework applicable to secondary market trading systems (extent of entry or exit or whether to allow internalization or force disclosure of order flow), policy makers will need to consider the rapid advances in technology, the size of the country, and the extent of its integration in regional and global capital markets.

In order to attract and maintain investor interest, bond issuers need to disclose objective, relevant, and timely information about themselves and the securities being offered to the public. The existence of an equity market is practically a prerequisite for private sector bond market development as it often sets an example for disclosure practice. In addition to meeting regulatory disclosure requirements, the development of private sector bond markets could be aided by voluntary disclosure. The voluntary public release of credit rating agency of a private sector bond issuer could form an important element of a voluntary disclosure system.

Most fixed-income securities markets have traditionally been opaque, with scant and delayed information on transactions available to the public. Major intermediaries should voluntarily provide pre-trade, indicative prices to the market through business information vendors, as well as hold regular meetings with the market makers, the Central Bank, investors and other market participants to ensure a shared understanding of developments in the capital market and appropriate consultation on reform options.

2.4.6 Investor base

A diversified investor base for fixed-income securities is important for ensuring high liquidity and stable demand in the market. This calls for a heterogeneous investor base with different time horizons, risk preferences, trading motives and high liquidity. Where one group of investor exits or gains entry in the market over a short period and where there are no counterbalancing order flows from other investor groups, even liquid markets can become illiquid in such instances. Some of the questions to address include: how can mutual funds and other collective savings schemes play a role in the securities market? Should foreign investors be allowed in the market and what role should they play in the bonds market? How can retail investors be effectively and efficiently served in the bonds market? Should banks continue to dominate trading in bonds, particularly government bonds?

Having access to major savings pools, such as retail or foreign investors, structural reforms of pension and retirement funds to encourage their investment in bonds and reforming or creation of mutual funds and other collective investment schemes need critical consideration. Foreign investors tend to be relatively more sensitive to risk, and manage their portfolios actively, which means a stable macroeconomic environment and prudent capital account liberalization is essential to maintain a stable and growing participation of foreign investors in debt securities markets.

2.4.7 Sinking fund provision and issuer guarantee

The laws in various countries provide for establishment and maintenance of a fund out of which any liability of a member arising from buying and selling of listed securities for different categories of claims is paid for if such a member fails to discharge her liability. Protection provided by the fund is based on the principle that in those instances in the buying and selling of securities on the exchange where a client has performed under a statutory duty (that is, in terms of the Act) the fund will provide general protection. In other instances, the quantum of protection is restricted. The fund has liability for losses in respect to both general protection and limited protection.

2.4.8 Benchmark issues and other debt instruments

Development of government benchmark securities by concentrating new issues of debt securities in a relatively limited number of popular, standard maturities can assist governments in the development of liquidity in those securities and thereby lower their issuance costs. Markets can then use such liquid issues as convenient benchmarks for pricing a range of other financial instruments. Spreading the relatively few benchmark issues across a wide range of maturities (building a benchmark yield curve) can facilitate better risk management in financial markets. Accurate pricing of less liquid debt instruments such as corporate bonds is needed for fairness among different groups and generations of investors, and this would be difficult without reference points provided by benchmarks.

A number of countries are developing matrices for the valuation of less-liquid debt instruments based on net present value, where the rate of discount is calculated by reference to the relationship between the rating of a particular bond and the rating of a risk-free benchmark government bond. Policy makers need to weigh the advantages of longer-term benchmark issues against the possibility of higher cost associated with longer-term benchmark bonds, the refinancing risk that comes with focusing on maturities, and the needs of government debt financing and benchmark development.

In many emerging economies, Kenya included, both tradable debt securities (such as treasury bonds, corporate bonds, municipal bonds, etc) and non-tradable debt instruments (such as special purpose government bonds issued for financing specific projects and not traded in the secondary debt market) are issued. Issues of special purpose bonds should be discouraged, since they limit the liquidity of debt instruments. Consequently, the market should generally narrow the variety of debt instruments by consolidating and standardizing debt securities issues, with an emphasis on marketable debt securities.

2.4.9 Favorable tax policies

Taxation of capital gains and income from bonds affects consumption, savings and investment decisions, influencing the general level of savings, the demand for financial assets, and investment. An inappropriate tax system hampers the emergence of new financial instruments such as mutual funds and asset-backed securities. Tax authorities in most developing countries often skew the tax regime to take advantage of a relatively well-institutionalized financial sector from which revenue can be raised easily. As a way of stimulating national savings, many countries have employed various tax incentives for certain financial assets. Tax incentives used with care can be effective in achieving certain economic goals, such as promoting a long-term bond market. Contributions to pension plans are tax exempt in many countries, and savings through life insurance receive special tax treatment in many countries.

Contributions to private pension funds are a major source of national private savings, hence representing an important source for institutional investment in the capital market, including debt securities such as bonds. Policy makers should give careful consideration to designing a tax regime for pensions and other collective investment vehicles that are conducive to bond market development.

3.0 METHODS

3.1 Introduction

This chapter covers a description of the study design, target population, sample design, data collection methods, research Procedures and data analysis and presentation.

3.2 Research Design

According to Brown, Askew, Baker, Denvir and Millett (2003), research design provides the glue that holds the research project together. A design is used to structure the research, to show how all of the major parts of the project, which include the samples or groups, measures, treatments or programs, and methods of assignment that work together to try to address the central research questions. For purposes of this study, a case study design was used. Yin (2004) defines the case study research method as an empirical inquiry that investigates a contemporary phenomenon within its real-life context; when the boundaries between phenomenon and context are not clearly evident; and in which multiple sources of evidence are used. A case study generally aims to provide insight into a particular situation and often stresses the experiences and interpretations of those involved. It may generate new understandings, explanations or hypotheses. However, it does not usually claim representativeness. Therefore, researchers using case studies should be careful not to over-generalize (Ball, 2004). Case studies involve collecting empirical data, generally from one or a small number of cases. It usually provides rich detail about those cases, of a predominantly qualitative nature (Yin, 2004).

Case study research excels at bringing researchers to an understanding of a complex issue or object and can extend experience or add strength to what is already known through previous research (Hamel, Dufour and Fortin, 2003). According to Eisenhardt (2004), case studies emphasize detailed contextual analysis of a limited number of events or conditions and their relationships. Social scientists, in particular, have made wide use of this qualitative research method to examine contemporary real-life situations and provide the basis for the application of ideas and extension of methods (Miles and Huberman, 2003). Many well-known case study researchers such as Stake (2005), Simons (2003) and Yin (2004) have suggested techniques for organizing and conducting the case study research successfully. This case study research draws upon their work and proposes six steps that the should be used are, determine and define the research questions, select the cases and determine data gathering and analysis techniques, prepare to collect the data, collect data in the field, evaluate and analyze the data, and prepare the report.

The study took a holistic, in-depth approach and as such, the case study is the most appropriate methodology. According to Feagin, Orum and Sjoberg (2004), case study is an ideal methodology when a holistic, in-depth investigation is needed. Case studies are multi-perspective analyses. The researcher considered not just the voice and perspective of the actors, but also of the relevant groups of actors and the interaction between them. This one aspect is a salient point in the characteristic that case studies possess. However, case studies tend to provide in-depth information about a limited number of subjects, and may produce new insights that generate additional studies. The major challenge expected in using the case study approach is that the researcher is required to have excellent knowledge of the topic when designing questions. The researcher approaches the subjects of study with an inquisitive mind and an openness that permits subjects to respond in an unlimited number of directions. This less structured approach may take the researcher down avenues he did not anticipate traveling and open doors to new kinds of understanding.

3.3 Population and Sampling Design

3.3.1 Population

The study focused on firms listed on the Nairobi Stock Exchange that have issued corporate bonds, whose number stood at 9 as at 31st March 2011 (See Appendix I). The Heads of Finance of the firms under study were the respondents.

3.3.2 Sampling Design

Sampling Frame: A sampling frame is a list from where the population is drawn. A list of all the firms listed on the Nairobi Stock Exchange, whose number stood at 48 was obtained from the Nairobi Stock Exchange report (March 2011). Further, a listing of the Heads of Finance of each of the listed firms that have issued corporate bonds was obtained from the respective human resource departments.

Sampling Technique: Stratified random sampling was used to arrive at the sample size. From each stratum, 50% of the companies listed on the Nairobi Stock Exchange were selected at random, making a sample of 25 companies. Each of the organizations was represented by five respondents: the Head of the Finance function, and four employees from the treasury and shares/bonds departments. Table 3.1 below presents the sample size

Table 3.1: Sample Size

Strata	A = Population	B = Sample Size (A x %)
Agriculture	3	2
Commercial and Services	11	5
Finance and Investment	13	7
Industrial & Allied	16	8
Alternative Investment Market Segment	6	3
Total		**25**

3.4 Data Collection Methods

Both primary and secondary data was collected. Secondary data was collected in order to ensure relevance to the research problem and eliminate duplication of what has been done and provide a clear understanding of existing knowledge base in the problem area. The sources of secondary data included authoritative, recent, and original sources such as journals, books, thesis and dissertations. Primary data was collected using a semi-structured questionnaire. A self-administered questionnaire was used since the level of understanding of the questions by the respondents is expected to be relatively high and the method is also considered since it is not time consuming. The questionnaires were hand delivered to the respondent firms that are based in Nairobi, while those outside Nairobi was sent their questionnaires via email.

3.5 Research Procedures

The semi-structured questionnaire used to collect data was structured into two sections. Section I of the questionnaire consists of items pertaining to profile of the respondents, in which closed questions are used. Section II consists of items pertaining to the specific objectives of the study. Both open-ended and closed questions were used in this section. The questionnaires were pilot tested on three randomly selected respondents before they are administered. The purpose of the pilot testing was to ensure that the questionnaires are understood in their correct perspective, in order to meet the research objectives. The procedure that will be used in collecting data was through distribution of the questionnaires that is, dropping and picking questionnaires from respondents at their most convenient time that will be agreeable to both parties.

Data pertaining to background information was collected using closed questions with alternative choices of possible responses from which the respondents was required to tick as appropriate. A letter of introduction, stating the purpose of the study, was attached to each questionnaire. In addition, the researcher made telephone calls to the respective respondents to make follow up on the questionnaires that are delivered to the respondents. Once completed, the researcher will personally collect the questionnaires from respondents based in Nairobi, while those from outside Nairobi were required to fill in their questionnaires and send them back via email.

3.6 Data Analysis Methods and Presentation

According to Marshall and Rossman (2003), data analysis is the process of bringing order, structure and interpretation to the mass of collected data. Data analysis involved preparation of the collected data - coding, editing and cleaning of data so that it would be processed using SPSS package. The coded data was keyed into the SPSS program where it was developed into a database and hence analysis. The data pertaining to profile of the respondents and their respective organizations was analyzed using content analysis. Cooper and Schindler (2005) states that content analysis may be used to analyze written data from experiments, observations, surveys and secondary sources. Content analysis is a research tool used to determine the presence of certain words or concepts within texts or sets of texts. Researchers quantify and analyze the presence, meanings and relationships of such words and concepts, then make inferences about the messages within the texts, the writer(s), the audience, and even the culture and time of which these are a part. Texts can be defined broadly as books, book chapters, essays, interviews, discussions, newspaper headlines and articles, historical documents, speeches, conversations, advertising, theater, informal conversation, or really any occurrence of communicative language.

To conduct a content analysis on any such text, the text is coded or broken down, into manageable categories on a variety of levels - word, word sense, phrase, sentence, or theme - and then examined using one of content analysis' basic methods: conceptual analysis or relational analysis.

Data pertaining to the objectives of the study was analyzed by employing descriptive statistics. Descriptive statistics were used to describe the basic features of the data in the study. Together with simple graphics analysis, the formed the basis of virtually every quantitative analysis of data. Descriptive statistics help to simplify large amounts of data in a sensible way. Each descriptive statistic reduces lots of data into a simpler summary. Presentation of the information was done using percentages, frequency, mean scores and standard deviations

4.0 FINDINGS AND DISCUSSIONS

4.1 Introduction

This chapter covers the data analysis, presentation and interpretation. The data used was obtained from the questionnaires distributed to Heads of Finance of firms listed on the Nairobi Stock Exchange. This study sought to determine the potential of the bond market in raising corporate finance in Kenya. The main types of statistics used to achieve this objective were mainly descriptive statistics such as measures of central tendencies, frequency distributions, percentages and charts. A combination of both quantitative and qualitative techniques was used in data collection. Out of the 115 questionnaires that were sent out, 95 of them were returned completed (82.6%) response rate. The high response rate could be attributed to the personal efforts of the researcher, who made a follow up of every questionnaire sent out. The information is presented and discussed as per the objectives and research objectives of the study.

4.2 Benefits derived from raising corporate finance in the bond market

In order to satisfy the first objective of the study: to determine the benefits derived from raising corporate finance in the bond market in Kenya, the respondents were provided with a listing of possible benefits derived from raining corporate finance in the bond market and asked to indicate the extent to which their company will benefit if it uses bonds to finance its operations; responses are summarized and presented in table 4.1 below. Scale: 1;(Not at all),2; (Neutral),3 (Minimal),4(Much),5(Very much).

Table 4.1: Benefits derived from raising corporate finance in the bond market

Benefits derived from raising corporate finance in the bond market		1	2	3	4	5	Mean	Standard Deviation
Lower funding costs	Frequency	3	4	7	42	39		
	Percentage	3.2	4.2	7.4	44.2	41.1	4.16	0.960
Raises large amounts of money	Frequency	7	1	8	38	41		
	Percentage	7.4	1.1	8.4	40.0	43.2	4.11	1.106
Diversifies financial resources	Frequency	2	2	11	59	21		
	Percentage	2.1	2.1	11.6	62.1	22.1	4.00	0.786
Increases a company's competitiveness	Frequency	2	8	34	30	21		
	Percentage	2.1	8.4	35.8	31.6	22.1	3.63	0.990
Lower cost alternative	Frequency	7	12	52	-	24		
	Percentage	7.4	12.6	54.7	-	25.3	3.98	0.825
Tax allowance for interest cost	Frequency	5	4	12	31	43		
	Percentage	5.3	4.2	12.6	32.6	45.3	4.08	1.108
Diversification of risks	Frequency	5	5	8	37	40		
	Percentage	5.3	5.3	8.4	38.9	42.1	4.07	1.094

Other Benefits

The respondents were asked to suggest other benefits of using bonds as a source of raising capital. The other suggested benefits include the following:

A more cost effective and private affair; Aids in planning; Allows for product diversification; Allows the owners to retain ownership and control as opposed to equity; Promotes public interest in the company; Assigned funding; Awareness of company; Bond funds enjoy tax shield; Can be converted to equity; Can borrow long-term funds cheaply; Cheaper listing cost i.e. advertisement and registration; Competitiveness of company; Create more awareness of company; Debt financing is cheaper than equity financing; Debt holders are eventually paid off unlike equities; Debt holders do not have a say in the running of the company unlike enquiries; Deepens customer relations/loyalty; Diversification of risk; Effective planning due to option to refinance; Enhances company visibility; Faster ways of raising capital; Funding long term investments; Good for planning/budgeting since the interest rate is fixed; Good publicity- could cause customer loyalty; Enhance credit rating of the issuing company especially if they repay; Helps create more awareness of the bond markets in Kenya to the wider public hence making bond market more active; Helps organization (Banks) to match LT liabilities to LT assets; Increases competitiveness of security instruments in the bond market and diversification of the same; Increases investor confidence; It's a form of advertising to potential investors when probably are customers which will make them loyal if they decide to be clients as they will investors seeking after a return and willing buyers spend on own company; It's taken long time to mature; Mopping up excess liquidity in the economy which in turn lowers inflation for favorable/affordable credit by financiers; No security required; Raising capital through issuing bonds would afford the bank the much needed long term capital which is lacking in terms of deposits or share issue. Long term capital will give the bank the comfort of offering long term loans like mortgages and venture capital; Reflects the health of the company simply by its ability to repay debt; Return on debt (interest) is tax deduction whereas return on equity (dividends) is paid out of profits which are taxed before paying out the dividends; Source of long term capital; The company still maintenance its ownership; The share holding structure doesn't change. The status-quo remains and the majority shareholder's position and influence is not threatened by creating new shareholders or diluting their shareholding; they increase organizations acceptance in the community around where it operates; Trading, buying debt doesn't make economic sense; Transfer of cost of benefits; Valuation- yields on a company's debt are used to evaluate cost of debt in the CAPM-WACC computation; You can maximize on returns by fixing a good interest for the fixed time of the bond; and You know your cost of funds for a specified period.

4.2 Challenges faced in raising corporate finance in the bond market in Kenya

In order to satisfy the second objective of the study: to establish the challenges faced in raising corporate finances in the bond market in Kenya, the respondents were asked to indicate the extent to which they agree/disagree that following factors will be a challenge to their company when using bonds to finance their operation, responses are summarized and presented in table 4.4 below. Scale: 1 ;(Strongly disagree), 2; (Disagree), 3 (Neutral), 4(Agree), 5(Strongly agree).

Table 4.2: Challenges faced in raising corporate finance in the bond market in Kenya

Challenges faced in raising corporate finance in the bond market in Kenya		1	2	3	4	5	Mean	Standard Deviation
Underdeveloped financial system	Frequency	7	11	13	34	30		
	Percentage	7.4	11.6	13.7	35.8	31.6	3.73	1.233
Administrative pricing of corporate bonds	Frequency	1	7	14	59	14		
	Percentage	1.1	7.4	14.7	62.1	14.7	3.82	.812
Requirement of bank guarantees	Frequency	6	7	24	35	23		
	Percentage	6.3	7.4	25.3	36.8	24.2	3.65	1.118
Lack of effective market discipline	Frequency	2	16	26	36	15		
	Percentage	2.1	16.8	27.4	37.9	15.8	3.48	1.020
The Current Bankruptcy Law does not provide recourse in the event of default	Frequency	2	7	37	29	20		
	Percentage	2.1	7.4	38.9	30.5	21.1	3.61	0.971
Lengthy approval process	Frequency	2	10	11	31	41		
	Percentage	2.1	10.5	11.6	32.6	43.2	4.04	1.081
Requirement of credit issuer credibility	Frequency	2	12	13	40	28		
	Percentage	2.1	12.6	13.7	42.1	29.5	3.84	1.055
Considerable cost of bond life cycle	Frequency	-	5	22	42	26		
	Percentage	-	5.3	23.2	44.2	27.4	3.94	0.848
Illiquidity	Frequency	-	9	21	37	28		
	Percentage	-	9.5	22.1	38.9	29.5	3.88	0.944

Other challenges

The respondents were asked to suggest other challenges arising from the use of bonds as a source of raising capital. The responses are presented as follows:

Absence of sufficiently large underwriters; Agreed rates are hard to establish; Bonds are like debts with payment obligations; Cash flow; Corporate bonds do not comprise liquidity, qualification of CBK; Corporate Bonds do not qualify as Repo instruments; Cost of financing the debt/bond in terms of interest payment may eat into the cash flows; Determining market appetite; Hard to establish interest rates; Expensive; High interest rates and slow uptake; Ignorance by investors and banks; Investors are not sure on how rating is done; It's a time consuming process requiring advisory services that are very expensive; Lack of investor education on debt finance; Marketing timing; Payment of long term interest; Penetration of corporate bonds still very minimal; Poor liquidity at NSE may curtail trading thereby sending signals to future investors; *Pricing:* assessment of risk & pricing levels; Properly competition because the government is also using the same meals to raise capital for social development; Public apathy/ignorance on bonds; *Risk* - the borrower may not be able to pay back; Secondary trading; Short-selling of bonds in the secondary market needs to be introduced; Slow trading at NSE i.e. low liquidity; Structuring the bond such that the interest (coupon) is not unfavorable to the issues but attractive to investors; The market does not factor in credit rating of issuer; and Unclear rating.

4.3 Possible interventions that can be used to address the challenges

In order to satisfy the first objective of the study: To determine the possible interventions that can be used to address the challenges faced in raising finances in the bond market and enhance performance of the bond market in Kenya, the respondents were asked to indicate the extent to which they agree/disagree with the possible interventions stated below, responses are summarized and presented in table 4.6 below. Scale: 1 ; (Strongly disagree), 2; (Disagree), 3 (Neutral), 4(Agree), 5 (Strongly agree)

Table 4.3: Possible interventions that can be used to address the challenges

Possible interventions that can be used to address the challenges above and enhance performance of the bond market in Kenya		1	2	3	4	5	Mean	Standard Deviation
Corporate sector and banking reforms	Frequency	-	2	7	33	53		
	Percentage	-	2.1	7.4	34.7	55.8	4.44	0.725
Effective information disclosure	Frequency	-	5	2	35	53		
	Percentage	-	5.3	2.1	36.8	55.8	4.43	0.781
Policies to strengthen market infrastructure	Frequency	-	2	3	36	54		
	Percentage	-	2.1	3.2	37.9	56.8	4.49	0.666
Favorable market regulations	Frequency	-	2	5	38	50		
	Percentage	-	2.1	5.3	40.0	52.6	4.43	0.694
Development of the money market	Frequency	1	3	7	32	52		
	Percentage	1.1	3.2	7.4	33.7	54.7	4.38	0.840
Diversification of investor base	Frequency	-	2	15	32	46		
	Percentage	-	2.1	15.8	33.7	48.4	4.28	0.808
Enhancing taxation policies	Frequency	-	3	14	37	41		
	Percentage	-	3.2	14.7	38.9	43.2	4.22	0.814
Ensure a secure and efficient custodial system	Frequency	-	5	23	31	36		
	Percentage	-	5.3	24.2	32.6	37.9	4.03	0.916
Investor Education	Frequency	-	1	5	23	66		
	Percentage	-	1.1	5.3	24.2	69.5	4.62	0.639

Other interventions that can be used to address the challenges

The respondents were asked to state any other interventions that could be used to address the challenges identified so as to enhance performance of the bond market in Kenya. The responses are summarized and presented as follows:

Ability to list external markets; CBK should recognize the bonds for liquidity purposes; CBK to recognize the bonds on the repurchase agreements; Creating a risk free environment to boost investor confidence; Creation of strong regional stock exchange; Do away with secondary market; Domestic bonds should be encouraged, as opposed to international bonds to raise the living standards of the 'home' market (local); Government can engage various stakeholders and come up with policies; Government intermediaries should work together to ensure efficiency; Hybrid bond market; Improve bankruptcy procedures related to bond transactions; Improving related infrastructure for the bond market e.g. settlement, professional services; Investor education and awareness of bonds market and its performance in terms of return of investment to a investor which has relative low risk in spite of little but assured fixed rate of return; Legal reforms aimed at enhancing corporate governance and administration; Market to take into account the credit rating of the banks; More accessible trading system; Procedures to venture into the market should be made faster and simpler for more companies to seek such finance which is rather cheaper as companies to equity finance; Proper monetary policies that would guard against dramatic changes in interest rates; Short-selling of bonds in the secondary market needs to be introduced; The government through its arms the CMA,NSE and CBK should work together towards ensuring more activity of the bond market in Kenya and hence efficiency of the financial market; and Trading outside the NSE. (Exchange).

5.0 DISCUSSIONS, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter presents a summary of important elements of the study, including the purpose of the study, specific objectives, methodology and major findings of the study. The chapter also presents the discussion and conclusions drawn from the research findings. The chapter further presents recommendations for practice and for further studies.

5.2 Discussions

This section presents the discussions

5.3.1 Benefits derived from raising corporate finance in the bond market

Diversification of financial resources was considered a benefit by majority of the respondents. Corporate bonds emissions can make up a considerable amount of money provided by a large number of creditors. As a consequence of a risk distribution among a large number of creditors the bond emission is a lower costs alternative in comparison to bank loans under a certain debt level condition. Also a procedure used by certain foreign companies in terms of reaching and maintaining an optimal financial source structure is worth mentioning (Levin *et al,* 2004).Companies first accept bank loans, and that is to the degree to which the loan is cheaper and otherwise more advantageous than bonds emissions. Then they issue bonds and use a part of the gained finance to paying loans and other liabilities off, which increases the ability to accept other bank loans. After reaching the top limit of bank loans a company issues bonds again and the cycle repeats itself.

Findings of the study indicate that *lower funding costs* were considered a benefit, which corroborates the finding by Hakansson (2001) who documented the following advantages of corporate bond market when examining principal differences between an economy with a well developed corporate bond market and an economy with a well developed bank based market: there is greater accounting transparency; large community of financial analysts; respected rating; wide range of corporate debt securities; derivatives demanding sophisticated credit analysis; efficient procedures for corporate reorganization and liquidation.

Findings of the study also indicate that the use of corporate bonds enables organizations to *raise large amount of money*. From the point of view of an issuer, i.e. a company, corporate bonds represent an alternative source of financing. Issuing corporate bonds can be used firstly for cash flow improvement, secondly for financial structure optimization, however also within ownership restructuring (Choe, Masulis, Nanda, 2003). Cash flow improvement can be achieved also by applying measures in terms of profit rate (decreasing costs and increasing returns), property (particular parts of property control including receivables) and further by gaining external financial sources of both a long-term and a short-term nature. Corporate bonds are one of alternative external long-term sources.

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Tax allowance was considered a benefit by majority of the respondents. According to Myers and Majluf (2001), a significant advantage rests in the fact that returns of corporate bonds represent a tax base and in case of a company profitability an interest tax shield can be used. Furthermore shareholders do not lose a company activity control when issuing corporate bonds, while issuing them often does not even need a collateral in a form of a property pledge (Mikkelson and Partch, 2001). It is due to say that as a consequence of an obligation to pay back the principal and returns of bonds managers get a clearer view of rate of returns and that successful issuing of corporate bonds (especially their placement) is considered a prestigious thing helping the company to gain respect by the public and business partners (Merton, 2005).

Increasing Company's competitiveness was considered a benefit by majority of the respondents. According to Chordia, Sarkar, and Subrahmanyam (2003), the advantages of issuing corporate bonds can be seen in achieving a higher degree of company capital structure flexibility, and a company is thus more able to react promptly to constantly changing conditions, which consequently leads to generating larger financial sources. Liu, Qi, and Wu (2004) assert that corporate bonds can present an instrument of increasing of company competitiveness and can contribute to creation of competitive advantage.

Findings of the study also show that *diversification of risk* was considered a benefit by the respondents. According to Herring and Chatusripitak (2000), the absence of a bond market may render an economy less efficient and significantly more vulnerable to financial crisis. In the same vein, Trigueros (2000) concludes that a proper legal environment and the protection of minority shareholders and bondholders could foster the development of the financial sector and, in turn, contribute more efficiently to the economy's rate of growth. Development of the bond market provides diversification of fund sources and allows to tailor risk reward profile to its preferences concludes Hakansson (2001). Hotchkiss and Ronen (2002) noted that company bond and stock returns positively correlate implying both securities move in response to issuer-specific information (Kwan, 2006). Thus, the bond market is intricately linked to the stock market underscoring the importance of bond market to corporate financing.

5.3.2 Challenges faced in raising corporate finance in the bond market in Kenya

Findings of the study show that *cost of bond life cycle* was considered a challenge. According to Miller and Puthenpurackal (2002), a substantial disadvantage of bonds emissions lies in considerable emission costs created by costs of issue (costs directly connected with issuing corporate bonds) and costs of bonds life cycle (costs connected with the particular emission, arising in course of the life cycle and in connection to paying back the emission).

Findings of the study indicate that *administrative pricing* was considered a challenge. According to Acharya and Lasse (2005), administrative pricing of corporate bonds and price controls failed to reflect risks, thereby preventing effective risk management by issuers and investors

The Current Bankruptcy Law was considered a challenge. The protection given by local governments to bond investors undermined the incentive for them to evaluate the risks involved; the current Bankruptcy Law did not provide investors with effective liquidation as a form of recourse in the event of default. In China for instance, the residual assets - and even the issuer - could often simply disappear without going through legal procedures (Pastor *et al,* 2003). Although we have been working hard on a new bankruptcy law, the current one does not provide adequate protection for creditors; the underwriter's role was not properly defined. Underwriting and redemption typically came under the umbrella of central planning and administrative intervention.

Lengthy approval process was considered a challenge. Regarding the formal procedures for the local issuance of corporate bonds, the approval process in Kenya is a bit lengthier than in other countries in the region with prosperous financial markets. Another restraint on market development is the fact that only 9 corporate bonds are currently listed in the Nairobi Stock Exchange (NSE). Listing more of these bonds in the NSE would accomplish two important goals to promote this market: first, it would provide a valuable safeguard for small investors, and secondly, it would promote the standardization and flow of information through disclosure requirements, which in turn would enhance the price discovery process (Park and Rhee , 2006).

Requirement of bank guarantees was considered a challenge. Since issuance quotas were administratively allocated and prices controlled, and neither information disclosure nor credit ratings were available, bank guarantees seemed to be the natural solution. However, once guaranteed by a bank, the product was no longer a standard corporate debt but, rather, akin to a high-yield deposit at a commercial bank; bond issues were targeted at retail rather than institutional investors, who were capable of risk assessment; effective market discipline was not established. (Acharya and Lasse, 2005).

Credit issuer credibility was considered a challenge. Besides the above, the disadvantage of corporate bonds rests in the fact that investors require a lot from credit issuer credibility, while returns and principal must be always paid in time regardless the company profit (Miller and Puthenpurackal, 2002).

Lack of effective market discipline was considered a challenge. Lack of effective market discipline can lead to recourse to administrative means, which can give rise to a series of problems (Acharya and Lasse (2005). Market forces can discipline both the issuance and trading of corporate bonds as investors exercise their judgment in the choice of products - thereby giving them the final say on issue conditions, prices and consequences of default. In addition, in order for the OTC market to play a dominant role, a proper trading mode should be established to ensure proper assessment of counterparty risks and pricing flexibility; Investor education was not sufficient. To a large extent, many investors used to treat corporate bonds as just another savings deposit product. Whenever a default of corporate bonds occurred, they would turn to government agencies and demand redemption by underwriters. Moreover, the protection given by local governments to bond investors undermined the incentive for them to evaluate the risks involved; the current Bankruptcy Law did not provide investors with effective liquidation as a form of recourse in the event of default. In China for instance, the residual assets - and even the issuer - could often simply disappear without going through legal procedures (Pastor *et al,* 2003).

Underdeveloped financial system was considered a challenge. According to Acharya and Lasse (2005), corporate finance theory suggests that market imperfections such as underdeveloped financial system may constrain firms' ability to fund investments. To this extent, development economics have largely documented the role of financial market development on economic growth. Well developed stock markets provide liquidity, diversification, and information acquisition, resource mobilization for corporate finance, investment and growth. An active and liquid stock market makes it easy and relatively cheaper for firms to finance their operations through equity capital than debt.

The findings of the study also show that *market imperfections* such as underdeveloped financial system may constrain firms' ability to fund investments. According to Acharya and Lasse (2005), corporate finance theory suggests that market imperfections such as underdeveloped financial system may constrain firms' ability to fund investments. To this extent, development economics have largely documented the role of financial market development on economic growth. Well developed stock markets provide liquidity, diversification, and information acquisition, resource mobilization for corporate finance, investment and growth. An active and liquid stock market makes it easy and relatively cheaper for firms to finance their operations through equity capital than debt.

5.3.3 Possible interventions that can be used to address the challenges

Findings of the study indicate that the possible interventions that can be used to address the challenges faced in raising corporate finance in the bond market include: effective information disclosure; policies to strengthen market infrastructure; make regulation favorable to both bond issuance and to the operations of local and foreign investors; development of the money market maybe in terms of the system; diversification of investor base; enhancing taxation policies for both issuers and investors; ensuring a secure and efficient custodial system; and continuously conducting investor education. These findings corroborate the recommendations by World Bank (2001) and Capital Markets Authority (2006).

5.4 Conclusions

This section presents the conclusions.

5.4.1 Benefits derived from raising corporate finance in the bond market

In view of the findings of the study, this section provides the conclusions with respect to the benefits derived from raising corporate finance in the bond market.

The benefits derived from raising corporate finance in the bond market include: raising corporate finance in the bond market provides relatively lower funding cost to the issuer than the traditional banking loans and information disclosure about the firm that helps to access public funds rapidly; provides an option of raising large amounts of money as compared to raising funds using equities; provides a diversification of fund sources and allows to tailor risk reward profile to its preferences; can present an instrument of increasing of company competitiveness and can contribute to creation of competitive advantage; corporate bonds emissions can make up a considerable amount of money provided by a large number of creditors. As a consequence of a risk distribution among a large number of creditors the bond emission is a lower costs alternative in comparison to bank loans under a certain debt level condition; returns of corporate bonds represent a tax base and in case of a company profitability an interest tax shield can be used; and ensures diversification of risk.

5.4.2 Challenges faced in raising corporate finance in the bond market in Kenya

In view of the findings of the study, this section provides the conclusions with respect to the challenges faced in raising corporate finance in the bond market.

The challenges faced in raising corporate finance in the bond market include: market imperfections such as underdeveloped financial system may constrain firms' ability to fund investments; administrative pricing of corporate bonds and price controls fails to reflect risks, thereby preventing effective risk management by issuers and investors; authorities require bank guarantees for corporate bond issuance and still do so today; lack of effective market discipline leads to recourse to administrative means, which can give rise to a series of problem; the current Bankruptcy Law does not provide investors with effective liquidation as a form of recourse in the event of default; regarding the formal procedures for the local issuance of corporate bonds, the approval process in Kenya is a bit lengthier than in other countries in the region with prosperous financial markets; investors require a lot from credit issuer credibility, while returns and principal must be always paid in time regardless of the company profit; considerable emission costs created by costs of issue (costs directly connected with issuing corporate bonds) and costs of bonds life cycle (costs connected with the particular emission, arising in course of the life cycle and in connection to paying back the emission); and illiquidity – A bond may not be fully taken up and this may affect the funds raised by a company.

5.4.3 Possible interventions that can be used to address the challenges

In view of the findings of the study, this section provides the possible interventions that can be used to address the challenges faced in raising corporate finance in the bond market.

The possible interventions include: undertaking corporate sector and banking reforms; ensuring effective information disclosure; formulation and implementation of policies to strengthen market infrastructure; making regulations favorable to both bond issuance and to the operations of local and foreign investors; development of the money market maybe in terms of the system; diversification of investor base; enhancing taxation policies for both issuers and investors; ensuring a secure and efficient custodial system; and undertaking education.

5.5 Recommendations

This section presents the recommendations

5.5.1 Recommendations for Policy and Practice

In view of the findings and conclusions of the study, the following recommendations are made for policy and practice:

For a bonds market to contribute significantly to the development process, it requires that the market caters for a diverse risk preference, is liquid, efficient and has minimal volatility. To achieve this, there must be a sound fiscal and monetary policy, effective legal and regulatory framework, secure and efficient settlement and custodial system, effective information disclosure system, a diversified investor base, and favorable tax policies. For treasury bonds especially, there is need for an effective financial system, a sound and prudent debt management and credible and stable government. In addition, the development of a well-functioning money market is essential in enhancing liquidity of the market. An active money market is the precursor to an active secondary bond market.

The following should be addressed to ensure development of a successful bonds market: Ensuring that there is an active money market in place, that will enhance liquidity in the bonds market:

Ensuring effective policy framework to govern the bonds market, which will help define the path clearly for bonds market development and enhance credibility;

Ensuring a sound legal and regulatory framework that provides necessary oversight of the market and ensures its stability, defines parameters linking fiscal budget with security issuance, showing the ceilings, and legal properties of bonds, ensures fair, efficient and transparent markets, and minimizes systematic risk through clearly defined roles and obligations of market participants;

Develop a secure and efficient trading and settlement systems that will ensure proper surveillance, settlement, trade and dispute resolution, improves market integration, increased liquidity, and reduced operational risk;

Develop and institutionalize quality information disclosure. This will facilitate improvement of market access and transparency; improvement in investor confidence, and improved participation and liquidity;

Ensure a broader investor base for improved competition, improved participation and liquidity and stabilized demand;

Ensure a functional sinking fund and issuer guarantee for reduced investment risk and improved investor confidence;

Address benchmark issues to ensure that pricing of corporate bonds and other instruments is undertaken accurately; and policy makers should give careful consideration to designing a tax regime for pensions and other collective investment vehicles that are conducive to bond market development. . This will ensure improved participation and in turn liquidity through increased transaction volume, provision of checks in excessive speculation, ensure improved savings and investment liquidity, and increased market competitiveness from decreased cost of capital.

5.5.2 Recommended areas of Further Research

The findings of this study, it is hoped, will contribute to the existing body of knowledge and form basis for future researchers. The following areas of further researcher are thus suggested: (i) Whereas the current study focused on responses from the management of the firms listed on the Nairobi Stock Exchange, future studies should focus on responses from the Capital Markets Authority; and (ii) Future studies should seek to establish the nature, extent and implementation profile of firms that have raised corporate finance on the bond market in Kenya.

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