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Dear Dr Jacobs

Thank you for the opportunity to review and amend our article entitled: *Pricing contingent convertible bonds in African banks*. We are grateful to the anonymous referees who provided valuable comments and insightful feedback.

We have now completed our corrections and attach the amended paper. To simplify tracking of our changes, the following represents a summary of our responses to the referees.

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| **Reviewer 1 comments** | **Response** | **Details** |
| I suggest that the methodology be enhanced | We disagree | The methodology is based primarily on the foremost research on CoCo pricing of De Spiegeleer and SchoutensNo methodology currently exists for pricing CoCos in African markets |
| Results are fine, but I am missing specific recommendations | We agree to some extent | While the specific recommendations would prove to be useful to African Banks, as in the comment below, we plan to expand the study in our next paper entitled *Managing African bank capital procyclicality using cocos* |
| I am excited and happy with the study as is, but it goes further than pricing. I know that the study is about pricing only but I believe that the study can contribute much, much more.Basel implementation in Africa is in various stages. CoCos would definitely help, but banks need guidance.Add how CoCos can be implemented and used including an enhanced problem statement, specific recommendations, etc. I would like to see a much clearer contribution to the body of knowledge. We need to “sell” the idea of CoCos to these countries and banks not just the pricing. | We agree but argue that this will be covered in an upcoming paper | Our follow-up article will be entitled *Managing African bank capital procyclicality using cocos* and this will address each of the suggestions made here. We have always had in mind three, linked articles: the first covering pricing, the second, implementation and the third, case studies and future work.We are grateful for the reviewer's enthusiasm and suggestions. |

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| **Reviewer 2 comments** | **Response** | **Details** |
| The abstract reflects the essence of the research. Thus, it fails to outline the research results (within 1-2 phrases). I suggest that a brief presentation of the results should be included at the end of the abstract | We agree | We have now altered the abstract to include the main results and added the sentence: *We find that the African milieu (high interest rates and equity volatility compared with developed markets) makes CoCos particularly attractive instruments for the simultaneous reduction of debt and enhancement of capital.* |
| The introduction is too short. It lacks a brief presentation of what the CoCos are, while they represent the core of the paper | We agree | Mention is now made of the fact that this may be the first study of its kind. A brief definition of CoCos has been added |
| The description of Sections 3 and 4 is far too long | We disagree | Section 3 outlines the history of CoCos and their relevance and this is a crucial part of the introduction, laying the foundation for the reader with Section 4 being the essence of the study |
| While the paper briefly presents its potential contribution to the academic literature, it does not state clearly that it might be the first to investigate the use of CoCos for selected African banks.  | We agree  | We have now elaborated on this crucial aspect of the paper |
| The phrase in page 1 starting with: *The type of Tier 1 capital*...is too long. It should be broken into two shorter and better structured phrases | We agree | The sentence has been amended |
| The paper has to be restructured in order to ensure a better presentation of the core research. Section 2 is irrelevant since the literature included has only a remote connection with the investigated topic. | We disagree | Section 2 explores the history of the financial crises as the primary driver behind Basel II being conceived with emphasis on the effect that the crisis had on South Africa as a proxy for Africa. This section also states the primary measure proposed by Basel III to counteract the procyclical nature of capital and links this to CoCos as an alternative to be discussed in the following Section 3. |
| I failed to see the relevance of the information presented in page 4 at this level of the paper |  | Page 4 references the countercyclical capital buffer suggested by Basel III and links this to CoCos which are posited to be an alternative which Basel may consider |
| My suggestion is to redo the Section 2 by concentrating on the literature investigating CoCos and the related topic of Basel III in order to be relevant for the topic under scrutiny.  | We disagree | In section 2 we provided a brief history of potential crises and the regulatory response thus far. The history of cocos as potential loss absorbing instruments was thus contextualised and introduced in Section 3. We still believe this structure is necessary |
| Section 3 tries to give a description of CoCos and compares them to convertible bonds. However it fails to highlight the similarities and differences | We agree | Although the study is about *pricing* of CoCos and not a comparison of various bonds in the market, we have introduced a few sentences in Section 3 which cover some aspects of the comparison between ordinary convertible bonds and CoCos. |
| It is not clear when CoCos were introduced by Lloyds | We agree | Date of first CoCo issuance added |
| On page 5 I could not understand the reference to callable bonds also; even if Huang (2009) speaks about convertible and callable bonds, the authors should adapt the reference to the announced topic | We disagree | The reason why the callability was referred to relates to the fact that the *issuer* has some control over the trigger of a call on the bond as this is similar to the properties of a CoCo where the trigger mechanism may be discretionary to the issuer of the CoCo.This highlights the fact that the trigger mechanism of CoCos are not necessarily dependent on external events but may be discretionary (also refer to Figure 2 on page 9). |
| I consider that the examples from page 5 and page 9 to be a little bit too much for an academic paper; they might be put in footnote if authors consider necessary, but this paper is not a manual for students.  | We disagree | We feel examples explain in more detail how CoCos function to the “novice” reader. Also, reviewer 1 felt this *was* necessary as CoCos are not well understood in the SA market |
| Section 4 follows too closely the calculations steps of DE SPIEGELEER&SCHOUTENS (2011) and might raise plagiarism discussions. I suggest that author(s) mix Section 4 and Section 5 in just 1 section, showing for every step of the calculations their results for the selected banks/African countries. By doing this, the way the existing pricing methodology was adapted to the African markets can be better highlighted. The author(s) must remember that they announced this adaptation within the introduction, therefore the reader expects to find it presented in a clear manner | We disagree | This methodology is based primarily (although not exclusively) on the De Spiegeleer & Schoutens model – this forms the basis of our discussion, we have referenced their work extensively.Section 4 covers a brief section on the data selection and pricing methodology (the bulk of the relevant mathematical exposition). Section 5 covers the *results* obtained from the application of the mathematics using the relevant data. We believe this is the standard method of presentation in articles of this typeIn certain instances, reference is made to South Africa only because South Africa differs to the similar results represented in the findings of the other countries |
| Section 6, conclusions, dedicated only two paragraphs (last two) to the research results. These should be more boldly presented within these conclusions. The ideas in the first three paragraphs of the conclusions should be shortened since some of these ideas were already presented at the beginning of the paper | We agree | We have shortened the conclusion by omitting one of the paragraphs presented earlier in the article |
| The source is missing for all the figures included in this paper. | We agree | Now added |
| The paper seems to have an original core idea: to investigate the CoCos in African banks. However, due to the inadequate literature review, this originality is difficult to be highlighted. The author(s) must correct this failure in order to make their paper publishable in an ISI indexed journal. | We disagree | An exhaustive search of available literature revealed very little research using CoCos in developing markets and none in African banks |
| The paper demonstrates an adequate understanding of the relevant literature and appropriated sources are cited in relation with the main topic of the paper, the CoCos. However, the following references are not cited into the paper body: Bardoloi (2003); BCBS (2006), Bolton & Samama (2012), McDonald (2010), Pennachi et al.(2010), van Vuuren (2012). Moreover, the same paper is sometime cited with all the authors and after that only as ‘first author et al.’ | Agreed and corrected | Sources have been added as a reference for further study as the ideas depicted in these studies provide context for further reading. Existing citations correctedWe have included sources consulted but not ultimately used in the article. We will remove these if required |

Please contact us if there are any problems.

Yours sincerely

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Dr Gary van Vuuren



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Francois Liebenberg