

INTERIM REPORT OF THE STUDY ON THE STATUS OF SECOND TIER SECURITIES (SSM) COMPANIES IN NIGERIAN CAPITAL MARKET

1.0 INTRODUCTION

The Commission recently participated in the meetings of the Emerging Markets Committee (EMC) of the International Organisation of Securities Commissions (IOSCO) which held in Barbados. One of the main presentations at the meeting by the London Stock Exchange was on Alternative Investment Market (AIM) which is similar to the Second Tier Securities Market (SSM) or Emerging Markets of The Nigerian stock Exchange. The AIM was established in 1995 and consists of smaller growing companies similar to the vision that motivated the establishment of the second tier securities market (SSM) in 1985. While AIM has been growing impressively in the last 10 years, unfortunately same can not be said of the 20 year old SSM in Nigeria, In spite of the following major advantages derived from being Listed.

1. REALISING AND RAISING EQUITY:

Company's shares quotation of the stock exchange enables the existing shareholders to easily convert his holding to liquid cash which otherwise would have be locked up in the equity of the company. In essence, the investors can sell shares when they feel the need be, thereby converting them to cash to address their financial needs. Quotation also makes it easier, and usually cheaper to raise additional equity capital. Institutions are more willing to subscribe to new equity because they know they can, if they wish, dispose of it on the market.

2. ENHANCEMENT OF STATUS:

Quotation enhances status of a company as it creates room for accountability and transparency of the company's' activities as well as improvement of credit rating. It also expose the company to high standards of disclose and monitoring as well as give products or services higher visibility which help to increase sales and attract new business opportunities.

3. EASIER ACQUISITION:

Quotation makes it easier and sometimes cheaper to expand by acquisition. The company with marketable shares may issue new shares as an alternative in whole or part to funding acquisitions from internal resources or external fixed interest borrowings. Acquisitions can therefore be made without necessarily increase gearing and depression of the share prices.

About sixteen companies under the SSM, with majority of them located in Lagos, are operating below half capacity. As a result of this, the Research & Market Development Department of the Commission carried out a study on the way forward.

2.0 OBJECTIVE OF THE STUDY

1. Appraise the growth of SSM market in the last 20 years.
2. To appraise the performance of SSM companies over the yeas.
3. To identify constraints/problems being faced by the companies.
4. To make appropriate recommendations and identify measures/incentives that can accelerates their growth.
5. Make any other recommendation as may be found necessary

3.0 METHODOLOGY

Surveys were carried out through personal administration of questionnaire to sixteen (16) SSM companies most of which are located in Lagos. The survey team also interviewed some of the managing directors of the affected companies. A different questionnaire was sent to The Nigerian Stock Exchange to capture its perspective

4.0 LIMITATIONS OF THE STUDY

Most of the SSM companies did not respond to the questionnaires sent to them as at the period of this analysis despite the deadline of January, 2006 given to them. Of the Sixteen (16) questionnaires administered, only three (3) have been received. This response rate of only 19 per cent considered not sufficient for a final report. the Nigerian Stock Exchange whose perspective was considered very important to the study had responded to the questionnaire sent to it consequently, remainders have been sent to the companies, while follow up visit embarking subject to management approval, Additionally, the responses received is however supplemented in this report by the interview conducted on officials of some of the companies.

5.0 DATA ANALYSIS / FINDINGS

Nigerian second tier securities market (SSM) was introduced in 1985 on the Nigerian stock Exchange with a view to allowing smaller indigenous companies to be quoted on the NSE and given them access to funds from the capital market which hitherto were available only to big and mainly foreign owned companies. According to The Nigerian Exchange, the objective for establishment the second-tier securities market also known as Emerging market includes:

- To empower Nigerian entrepreneurs towards better achievements and to maintain life long enduring enterprises that would out live them.
- To aim of the Emerging market was to provide opportunities for indigenous companies who seek funds for enhancement of operational efficiency, diversifications, and expansion.
- The need for the growth of the small and medium sized companies was recognized by The Nigerian Stock Exchange because The small and medium enterprises are to be seen as important and as necessary tools for the growth of an independent vibrant economy, this is a proven fact because the small and medium sized companies a higher growth rate and up springs, they have a good of employment provision.
- To deepen the market with a wider variation of trouble instruments for investors to generate income.
- To achieve these objectives, Companies on the SSM were to be subjected to less stringent requirements by The NSE unlike the first tier market. Below are the some of the requirements for listing of SSM and the first tier market for clarity purposes.

REQUIREMENTS FOR BOTH FIRST-TIER AND SECOND-TIER (SSM) MARKET IN NIGERIA

REQUIREMENTS	FIRST-TIER	SECOND-TIER
Corporate status	Company must be registered as a public companies and allied matters ACT, 1999.	same
Restrictive clause	All restrictive clauses on transfer of shares in the memorandum and Articles of Association of the company must be expunged.	same
Submission of company's Annual report and Account.	The company must submit to the exchange an audited financial statement and business records of the past five years.	same
Timeliness of data	The data of the last of such statement must not exceed nine month	same
Amount of money to be raised	The amount of money that can be raised is unlimited depending on the borrowing power of the company.	The amount of money that can be raised is limited to twenty million naira (N20million) subject to the borrowing power of the company.
Annual listing fees	The company will be subject to payments of annual listing fees which are based on market capitalisation.	Listing the company will be subject to payment of N50 million annually.
Shares to be offered to public	At least 25 % of the nominal value of the share of the company must be offered to the public	At least 10 % of the nominal value of the share of the company must be offered to the public
No. of share holders	The number of shareholders of the company must not be less than 300.	The number of share holders must not be less than 200
Listings requirements	After listings the company must submit half yearly and annual accounts to the exchange for presentation to the market operators.	Same
Securities to be offered	Securities must be fully paid up at the time of allotment.	Same
Securities allotment	Securities not allotted must be ware house and sold on the floor of the exchange.	same

REQUIREMENTS FOR LISTINGS IN UK FOR USM and FULL LISTING:

In both cases, companies must be registered as UK public limited companies under the companies Act, 1980.

	<i>USM full</i>	<i>Listing</i>
Minimum percentage of equity To be held by external investors	not prescribe but 10 % is the guideline	25%
Trading record	3 years, new ventures under certain Conditions. Latest audited figures not morethan 9 month old	5 year. Latest figure not more than 6 Months old
Minimum market Capitalisation	No lower limit but in excess of &500,000 normally expect	&500,000, but in practice much higher
Annual pre-tax profits	No lower limit but in excess Of &500,000 normally &200,000	No minimum but in practice normally not less than &1mn
S E entry fee	nil	scale from nil to &15,000
S E annual fee	&1,500	Scale from &500 to &3,000
Long-form accounts report	not required but sponsor will Probably need one	Required
Short-form account report	required (except for entry by Introduction)	Required
Adequacy of working capital Report	Directors declaration only	Required from directors and sponsors
Future undertaking	General undertaking	Listing agreement
External services	Card required (Green)	card required (White and yellow)

Details of these companies including,, Date incorporated, and dates listed are as in table below. There are currently sixteen (16) companies listed on the SSM.

Table (1)

COMPANIES	DATE INCORPORATED	DATE LISTED ON THE NSE
West African Aluminum Product PLC.	1976	6/9/1989
Amino International PLC	1981	1/2/1990
Juli PLC	–	2/11/1986
Krabo Nig plc	1977	21/08/1991
Rokana Industries plc	1978	5/11/1991
Smart products Nig plc	1966	26/07/1992

Tropical petroleum product plc	1980	8/2/1990
Capital oil plc	1985	May,1990
Union ventures & petr plc	1976	30/03/1993
Adswitch plc	1982	1991
Afrik pharm plc	1972	26/06/1992
Cutix plc	1982	12/8/1987
New park plc	—	15/08/1989
Rak unity petr.product	—	21/03/1989
Udeofson Garment factory	1986	4/5/1994
Flexible packaging plc	—	1/4/1993

NUMBER OF COMPANIES LISTED

Data gathered from The NSE indicate in the over twenty years of its existence only 30 companies have been listed on the SSM out of which 14 have graduated to the first tier or main board,. Some of the remaining on the SSM has serious organizational problems.

GROWTH IN SSM

It was observed that while there appeared to have been an initial enthusiasm at the inception of the market resulting in slow but steady growth over time the, SSM sector has been declining and had become stagnant in terms of listed companies. Thus, the number of listed companies peaked in 1993 with when there were twenty-three (23) companies listed on the SSM. This however dropped to nine-teen (19) in 1997 and further to sixteen (16) in 1998 where it remained to date. Indeed, there had been no new listings on the SSM for over a decade, after the listing of; Udeofson Garment Factory was listed in April 1994. See table

(TABLE 3)

YEAR	NO OF (SSM) DURING THE PERIOD
1985	1
1986	3
1987	4
1988	6
1989	9
1990	16
1991	19
1992	21
1993	23
1994	21
1995	20
1996	20
1997	19
1998	16

1999	16
2000	16
2001	16
2002	16
2003	16
2004	16
2005	16

Market Capitalisation (2001-2005)

Similarly, the market capitalisation of the second tier securities market has been less than impressive as its fortunes especially as a per centge of total market capitalisation has been fluctuating.

The market capitalisation the of SSM stood at N0.24 billion. Or US\$1,778. This is quite insignificant when compared with N648.5 billion for the first-tier market. The figures represent 0.04 per cent of the total market capitalisation of companies listed on The NSE. In 2005 it rose slightly to N1.30 billion as against N2523.5 billion of the first-tier market thereby accounting for 0.05 per cent of the total equity market capitalizations during the period.

Table 2

YEAR	(SSM) N"B	FIRST-TIER N"B	% OF TOTAL
2001	0.24	648.5	0.04
2002	0.6	748.7	0.08
2003	0.8	1324.8	0.06
2004	0.5	1,925.90	0.03
2005	1.3	2,523.50	0.05

PERFORMANCE OF SSM COMPANIES:

The Poor performance the of SSM companies in terms of market capitalisation is itself a rejection of their corporate performance in terms of networth. Turnover and profit after tax as reflected in table below. As was indicated earlier, many of the companies had not responded to our questionnaires at the time of this report. All efforts to get the audited annual reports of many of them also failed as they seem to have been defaulting on their poss. listing reporting obligations to regulatory authorities. The table below is therefore in respect of only 7 of the 16 listed companies with many of the indicators being incomplete . The pattern of unimpressive corporate performance is however clear a most cases with the possible exemptions of one or two companies such as cutix plc. Even companies which have moved up to the main board have generally not performed well enough to justify their upgrading. It is of course instructive to note that no SSM company has graduated to the main board in the years since 1998 when Aluminum Extrusions Ltd was so upgraded.

SELECTED SSM COMPANIES ON THE NSE

COMPANIES	PRE	POST	% CHANGE
KRABO NIG PLC	6	6057	100,850
CAPITAL OIL PLC	36	13,000	36,011
WAPCO PLC	2	5000	249,900
ADSWITCH PLC	18	3771	20,850

FIVE YEAR PERFORMANCE OF SOME SECOND TEIR SECURITIES MARKET (SSM) COMPANIES (2000 - 2004)

Company	Year								
	2000 (1)	2001 (2)	% Change Btw (2 & 1)	2002 (3)	% Change btw (3 & 2)	2003 (4)	% Change btw (4 & 3)	2004 (5)	% Change btw (5 & 4)
Ad switch Plc	NM	NM		NM		NM		NM	
Networth	32.95	37.95	15.17	25.43	-32.99	25.43	0	28.38	11.6
Turnover	35.31	97.39	175.81	97.39	0	97.39	0	15.26	-84.33
PAT	4.86	11.64	139.51	11.67	0.26	11.67	0	17.39	49.01
Capital Oil Plc									
Networth	24.09	20.62	-14.4	0	-100	0		0	
Turnover	72.48	47.56	-34.38	0	-100	0		0	
PAT	7.46	5.97	-19.97	0	-100	0		0	
Cutix Plc									
Networth	64.15	72.71	13.34	90.52	24.49	67.34	-25.61	122.37	81.72
Turnover	202.05	284.3	40.71	387.2	36.19	376.03	-2.88	432.67	15.06
PAT	23.64	18.37	-22.29	26.7	45.35	27.26	2.1	35.42	29.93
Juli Plc									
Networth	33.32	58.69	76.14	57.29	-2.39	97.1	69.49	111.85	15.19
Turnover	52.47	73.08	39.28	80.92	10.73	92.94	14.85	150.12	61.52
PAT	0.96	1.28	33.33	1.55	21.09	10.3	564.52	0.55	-94.66
New Pack Plc									
Networth	0	30.47		0	-100	0		0	
Turnover	0	120.3		0	-100	0		0	
PAT	0	2.7		0	-100	0		0	
Smart Products Nigeria Plc									
Networth	59.15	65.6	10.9	110.24	68.05	64.25	-41.72	0	-100
Turnover	9.21	0.38	-95.87	8.74	2,200.00	8.78	0.46	0	-100
PAT	-13.19	5.64	-142.76	-7.1	-225.89	0.24	-103.38	0	-100
Union Ventures Petroleum Plc									
Networth	26.94	18.37	-31.81	17.41	-5.23	11.43	-34.35	0	-100
Turnover	62.21	62.01	-0.32	66.65	7.48	77.63	16.47	0	-100
PAT	0.8	0.8	0	0.89	11.25	1.8	102.25	0	-100

PRE AND POST PERFORMANCE OF (IPO) SHAREHOLDING PATTERN OF SOME SELECTED SSM COMPANIES ON THE NSE

COMPANIES	PRE	POST	% CHANGE
KRABO NIG PLC	6	6057	100,850
CAPITAL OIL PLC	36	13,000	36,011
WAPCO PLC	2	5000	249,900
ADSWITCH PLC	18	3771	20,850

6.0 PROBLEMS FACING THE SSM SECTORS

The following major problems were identified by respondent as militating against the growth of companies listed on the SSM.

1. Low patronage by government
2. Dumping of substandard goods
3. Preference for imported goods
4. Exposure to unnecessary harassment and taxes
5. Fear of Dilution of ownership
6. Lack of education and enlightenment
7. Low capacity utilization, due to unreliable infrastructure i.e. electricity, water and inaccessibility to finance because of stringent conditions
8. Cost of raising funds and servicing the funds is too high
9. Political and economic instability
10. Channeling resources to other sectors other than the second tier securities market (SSM)
11. Lack of raw materials incase of manufacturing companies
12. Lack of capital
13. Most companies could not raise money through the capital market due to poor performance

THE NSE'S PERSPECTIVE

However, The NSE in its submission on the SSM listed five major causes of the unimpressive growth of the SSM as follows:

1. Management of these companies have failed over the years to update their records with The Exchange as investors don't know about their operations and are scared to further involved themselves in investing in them, this is one of the listing requirements they fail to abide to.
2. Stockbrokers don't try to promote them any more as they feel that the rates of returns on investments in The Emerging Market are not profitable. The Emerging Market.
3. Majority of the companies are still being run like it's a one man business as most of them are still in control of over 75% of the company shares.
4. The economic policies, political instability and ideologies under which the SME'S operate have not been recognizes as part and parcel of the national economic development, coupled with poor economic

records of most developing countries which can be regarded as a lead to their inefficiencies, lack of motivation and promotions.

5. They lack professional and managerial skills and limitations in handling policies and operational problems and sourcing for funds.

LESSONS FROM OTHER JURISDICTION

The phenomenon growth of some securities market which originally target small companies in other jurisdictions suggest that given the right policy and operational environment, the SSM has the potential for growth. The example will tend to support this view.

AIM

Nasdaq Stock Market Inc: Although not a regular stock exchange being an over the counter market the phenomenon growth of the NASDAQ stock market has been of interest to many market watchers according to Ioll and bulk (1981), the OTC has historically been the providing ground for an unseasoned company to prepare itself for eventual listing on an organised exchange, but the NASDAQ as an over the counter market has over the years growth beyond initial expectations. It is therefore not surprising that many newspapers including the comet (p.40) reported on April 12, 2006 that Nasdaq has become the biggest shareholder in the London stock exchange having bought a 15 per cent stock in LSE, repoted to be Europe's largest stock market. In effect what was conceived as an alternative market for smaller companies was taking over the LSE.

In the area of listing requirements for the SSM, those of Nigeria and United Kingdom (UK) are similar. However the UK demands three (3) year trading record for the SSM while in the case of Nigeria, 5 years is required. The United Kingdom SSM has considerably performed better than the Nigerian SSM. The figures available to us showed that the market capitalisation for UK SSM grew consistency from \$mn 2,361 in 1983 to & mn 2,863 in 1984. It rose further to \$3,132 in 1985. This indicated a percentage increase of 32.7 between 1983 and 1985. In the case of Nigeria, the growth rate is low as compared to the UK market, though there were no figures for the corresponding periods for comparison but the percentage growth was used as a yard stick.

For instance, the market value for the Nigerian SSM which stood at NO.60 billion in 2002 rose to NO.80 billion in 2003 but fell to NO.50 billion in 2004. This represented a drop of 16.7 per cent in three years (between 2002 and 2004). The market capitalisation however rose to N1.30 billion in 2005. This growth during the period was attributed to rise in prices of Cutix Plc and Ads witch Plc listed under the SSM. Cutix Plc also declared bonus issues which added to the number of its outstanding shares.

The fact is that the Nigerian SSM had not witnessed a consistent growth over the years as in the case of UK SSM. Similarly, the number of listings on the UK SSM grow rapidly from 97 in 1981 to 158 in 1982, reaching 268 in 1984 and 300 in 1985. This showed a growth of 209.3 per cent between 1981 and 1985. Whilst the Nigerian market had remained static at 16 in the last 8 years (1998-2005). though the figure was 16 in 1990, it rose to 19 in 1991 and 23 in 1993. The number of listed companies however dropped to 21 in 1994 and further down to 19 in 1997. Some companies however graduated to the first tier market during the period. The fact is that new listings on the Nigerian SSM have been very low as compare to other jurisdictions.

7.0 RECOMMENDATIONS

1. The listing cost and conditions of SSM companies should be lowered further
2. Visible campaign for government patronage of products of quoted indigenous companies
3. Render assistance in debt recoveries
4. Indigenous companies should be encouraged by way of various incentives including waivers / reduction in some of the listing requirements
5. Concerted effort should be made to help indigenous companies that are quoted to attract quality investment by taking advantage of the opportunities in SMIE.
6. Tax incentive should be introduced to encourage indigenous companies to get quoted.
7. Structural support from SEC, CBN etc.
8. Creation of a forum where by the Commission and the companies on the second tier market can meet on a regular basis to discuss their problems.
9. The SEC and NSE should as a matter of urgency meet to fashion out specific, short, medium and long term measures to move the SSM forward.

8.0 CONCLUSION

Based on the above findings, there is need for regular meetings with the representatives of SEC, NSE and members of the affected companies, as a matter of urgency in order to overcome the problems, There is need also, for the Commission, to make presentation during the next FSRCC Meeting on ways of reviving issues concerning SSM companies so as to have first hand information and recommend to government.

Also the issue of giving tax incentives to companies would assist in reviving the SSM and also encourage those that are not quoted to be quoted on the Nigerian stock exchange. Similarly, the average Dividend yield (DY) for UK market recorded a percentage change point of 1.78 in 5 year ended 1984. It stood at .35 per cent and 2.13 per cent in 1980 and 1984 respectively. The Nigerian market had recorded marginal increase of 0.06 in percentage change point the average DY was 8.69 per cent in 2001 and 8.75 per cent (2005). The fact is that been dormant. A lot need to be done to encourage more listings on the Nigerian SSM and those ready listed to be given insensive to enable them perform better.

