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Capital Market Operations and SMEs' Financing in a Developing Economy: A Conceptual Evaluation of the Nigerian Stock Market

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Abstract
This study evaluated the capital market operations vis-a-vis SMEs' financing in Nigeria. The fundamental objective of this study was to assess how the capital market enables organisations, particularly the small and medium scale enterprises (SMEs), raise medium to long-term finance. It was observed that the financial accessibility has been a key challenge to SMEs' growth in many developing economies. The issue of SMEs' funding need to be addressed with swiftness, given the importance of SMEs to Nigeria and the global economy in general. This study will stimulate increased interests in the trading of SMEs' stocks at the floors of the stock markets in many developing countries. The study therefore evaluated the reforms agenda of the Securities and Exchange Commission (SEC) and the Nigerian Stock Exchange (NSE) which were targeted at mitigating the challenges of SMEs' financing. The study concluded that there is need to develop a culture of venture capital and private equity in Nigeria. The study recommended that using the capital market to finance the SMEs in the developing economy should not be a matter of choice but a part of the operating environment in the country's financial system, especially in this contemporary regime of fairer trade in goods and services. The Nigerian stock market needed to be built up with mass participation of SMEs to attain a meaningful sustainable growth and development. There are also needs to formulate investment friendly regulations; keep low inflationary rate; provide favourable government policies and provide stable macroeconomic framework for the sustainability of informal and SMEs sector in the developing countries.
Keywords: capital market operations, Nigerian financial system, small and medium enterprises (SMEs) financing, stock market.

1. Introduction

The capital market, according to Akadiri (1996), is a vehicle for mobilization and redistribution of surplus fund (savings in small units) to the capital deficient units through specifically designed instruments (securities). It is a mechanism for monetisation of securities that would have otherwise remain illiquid. Therefore, the capital market is a source of domestic finance which provide equality and loan capital for more than one fiscal year. However, the capital market is a segment of the financial supermarket for raising long-term funds to finance productive investments. Anyafo (2002) refers to the capital market as a securities market for transacting in debt and equity instruments of long term or perpetual maturities. It is a meeting point for buying and selling of securities (shares, loan stock, and other securities) issued by listed companies, governments and other statutory bodies on the basis of wide distribution of ownership, adequate and full disclosure of information which must be provided regularly (Meier and Ranch, 2005).

The role of the Nigeria capital market as a source for long term funds for small and medium enterprises (SMEs) cannot be undermined, most especially in this contemporary regime of fairer trade in goods and services. There is no gainsaying that every business starts off as an SME. Nevertheless, SMEs provide most of the jobs. According to Nnanna (2004), over 90 per cent of businesses in Africa, and Nigeria in particular, are small and medium scale enterprises (SMEs) and these SMEs are the biggest employers of labour. Employment generation develops a nation and it enhances dignity of labour especially in a developing country like Nigeria that has a very strong entrepreneurial culture. The significance of the capital market as a segment of the financial supermarket for raising long term funds to finance productive investments cannot be overemphasized. For the avoidance of doubt, the capital market, which is also referred to as the securities market or the stock market, is a market for sale and procurement of medium and long term securities in form of equity participation (Alile and Anao, 1986). It is against the backdrop that Onigbinde (2005) remarks that the capital market enables a business entity to raise medium to long term finance, particularly for a small and medium scale enterprise. The capital market enables one to invest at individual, corporate and institutional levels. However, to what extent has the Nigeria capital market realized the mandate for the mobilization and redistribution of surplus fund to the capital deficient SMEs' sector through specially designed instruments or securities? This is the identified gap that informed the concept behind this study.

2. Review of Literature

A number of studies have been conducted on various segments of the capital market operations vis-a-vis many performance indicators in the economy (Anyafo, 2002). Steiner (1985) refers to the capital market as a specialized machinery to facilitate indirect investments by bringing together the sources and the users of funds in order to perform the financial function that will enable the placement of corporate and government securities in the hand of those who have funds to invest. Olalusi (1986), however, refers to the capital market as a market for the sale and purchase of medium and long-term securities in the form of equity participation, and as a tool to enhance co-existence of deficit and surplus institutions in the same economy of interest. Gardner (1991) states that a capital market is an avenue whereby owners of surplus funds can invest such funds by lending to borrowers who need them. According to him, the participants include governments, banks, multinational companies and SMEs among others, which can borrow or invest large sum of money from medium to long-term periods.

One of the distinguishing features of the capital market is that borrowing and investment are generally carried out using financial instruments, such as shares, bonds, development stock, and other securities which are all negotiable (Alile, 1994). Negotiability implies that the holder of an instrument need not wait for its maturity before he can dispose it off. Another feature of the market is that a borrower need not going directly to the bank as non-bank funding is entrenched in the capital market operations (Alile, 1993).

Furthermore, the market is organized into primary market, where new securities are sold; and secondary market, where outstanding securities are bought and sold (Alile and Anao, 1986). This has informed the remarks by Anyafo (2002) that the capital market is not really a market in the African sense. It is rather a network of institutions that arrange for long-term financial assets, such as shares, debenture stocks and mortgages. Within this network of institutions are primary market institutions such as issuing houses and secondary market institutions such as stock exchanges.

In some advanced economies, such as the United States, the secondary security market is further decomposed into: the stock market (or the stock exchange), the over-the-counter market (or the third market), and the fourth market. In this regard, the secondary market, according to Anyafo (2002), is the market in which outstanding securities are bought and sold by owners other than the issuers; while the third market refers to the over- the-counter trading of securities listed on an exchange; and the fourth market is the direct trading of securities between owners, usually institution, without any broker intermediation.

The promotion of the capital market in Nigeria is tied up with the objective of accelerated economic growth and development. Ekiran (1999) identified the following as the main objectives behind the establishment of the Nigerian capital market: mobilization of long term funds from surplus units for on-lending to deficit units to ensure efficient allocation of scarce financial resources; reduction of over- reliance on the money market for industrial and SMEs' financing; promotion of a solvent, efficient and competitive financial sector; and provision for long-term finance as well as promotion of a healthy stock market culture. The Securities and Exchange Commission (SEC) is the apex institution in the capital market. However, it is only in operation due to the existence of the stock exchange. The stock exchange, which is the cornerstone of the capital market operations can be segmented into two sectors: The First-Tier Securities Market and the Second-Tier Securities Market (Anyafo, 2002).

The first-tier securities market (Equity Market) is the original and principal market dealings. According to Alile (1994) and Anyafo (2002), the following conditions have to be met before a company can be quoted on the stock exchange:

- A minimum nominal value share capital of #500,000, being at least 25% of the total issues, must be held by the general public.
- Unless by prescribed council authority, minimum number of shareholders shall be 500.
- There must be total payment for securities before registration.
- Application for quotation will only be made possible through sponsorship by an existing member of the stock exchange

Furthermore, such a company must possess records of, at least, five years of trading with the latest audited financial statements not exceeding nine months. The company is also required to pay an annual quotation fee based on its share capital.

On the other hand, the first-tier securities market (Bond Market) is the alternative market dealings. Applications for state and local government bonds must meet the requirements above in addition to four (4) proof prints of the prospectus to be provided at least 30 days before publication. The prospectus must include the following among others;

- The full name of the issuing company
- The amount and the title of issue
- Price of the issue, and other information regarding the issue.

The second-tier securities market, however, was established in 1985 for the benefit of companies that found the listing requirements of the first-tier market too stringent. The market is generally aimed at the small and medium scale enterprises (SMEs) as well as private-owned firms that wish to go public. The following are the basic requirements into the market;

- The company must be registered according to the Companies and Allied Matters Decree (CAMD) of 1990;
- 10 per cent (unlike 25 percent of the first-tier market) of minimum nominal value share capital of #150,000 should be in the possession of the general public;
- Shareholding is restricted to a maximum of 75 per cent by an individual;
- Financial statements of, at least, three (3) years must be tendered;
- The number of shareholders must not be less than 100;
- A flat fee of (#3,000) is payable for listing;
- A maximum amount to be raised is #10 million.

The number of companies or SMEs that are listed on the second-tier securities market changes from time to time as new companies are listed whilst some older ones are upgraded from the side-stream market to the main-stream market and get listed on the stock exchange big board. In June 1987, the Nigerian Stock exchange (NSE) introduced an electronic system which beams the Nigerian capital market operations to the international financial system via the Reuters International Information Network. With the introduction of this service, foreign investors may automatically access relevant, information on quoted companies on the stock exchange: share prices, dividend payments, earnings per share, price-earnings ratio, among other stock market indices may be accessed by using the code NSXA-B. According to NSE Fact book (2009), these are growing investment interests in Nigeria's stock market by the international business community. Meanwhile by the virtue of the Non-Voting Shares Decree No. 34 of 1987, quoted companies are permitted to issue, through the stock exchange, non-voting shares for subscription to persons whether citizens of Nigeria or not; whether residents of Nigeria or not.

The shares, according to Alile (1993), are to be paid for in foreign convertible currency. Major features of these non-voting shares include:

- Eighty per cent (80%) of proceeds of sale goes to the selling companies in foreign currency for raw material and machinery importation needs.
- Twenty per cent (20%) of the proceeds will be held in an interest-yielding escrow account at the Central Bank of Nigeria (CBN) for the purpose of paying dividends to shareholders of non-voting shares whose ever resident.

The position above was the policy stance prior to 1995 when the Nigerian Investment Promotion Commission (NIPC) Decree No. 16 came into effects. According to NSE Fact book (2009), the share holding structure of the Nigerian stock market shows that foreign holding represents about 43 per cent of the equity market capitalization in the country.

3. Capital Market and SMEs' Growth in Nigeria

The capital market enables organizations to raise medium to long-term finance, particularly for the small and medium scale enterprises (SMEs). Similarly, the market enables the individuals, corporate organizations and institutions to invest their surplus funds (Oteh, 2014). One important segment of the capital market is, of course, the equities market. The market gives individuals and corporate organizations the opportunity to participate in the creation of wealth (Mobolurin, 2001) via a particular company by investing in such a company.

Furthermore, the capital market provides risk management instruments to the investors; this enables them to manage their investments for better returns. In leverage the success of the Nigerian capital market in building wealth for investors, Nigeria has a stock market that is in total of $121 billion, as at the end of the first quarter in 2014, which is about #18 trillion in terms of market capitalization. The equities market is about #12.9 trillion, while the rest of the investments actually belong the bonds market.

According to NSE Fact book (2012), bonds market in Nigeria have been highly impressive in the recent years primarily because of the mechanisms for sustaining macroeconomic stability that had been put in place by the governments of the Federal Republic of Nigeria. This has also gone a long way in addressing the structural imbalance between the bonds and equities market segments of the Nigerian capital market operations.

4. Capital Market Operations and SMEs' Financing in Nigeria

First and foremost, it becomes imperative to state that access to finance has been a key challenge to SMEs' growth in many developing economies (Oteh, 2014). According to Thoughton (1989), analyzing the global index that focuses very specifically on what entrepreneurs face as their biggest challenges in terms of their businesses; the financial accessibility was rated number one. Therefore, the issue of SMEs' funding is something that must be tackled with swiftness, given the importance of SMEs to the global economy in general, and Nigeria in particular.

There is no gainsaying that SMEs rely on bank lending, loans from co-operative societies, and personal savings for funding in many developing economies such as Nigeria. Unlike the United States and other developed economies, where SMEs focus on the capital market to raise medium and long-term funds via equities and bond markets. To attain this status, the regulatory and supervisory body for the capital market operations in Nigeria: the Securities and Exchange Commission (SEC) has embarked on a number of reform agenda since the beginning of the year 2010. The key aspect of the agenda is the revamping of the second-tier and the third-tier securities markets of the Nigerian Stock Exchange (NSE). According to Oteh (2014), the first-tier is the main bond market, while the second and third tiers are what are being referred to as the alternative securities markets.

One of the reasoning behind the reform agenda embarked upon by the SEC in collaboration with the NSE to revamp the Nigerian capital market is really to address the inadequacy of the market at mitigating the challenges of SMEs' funding. However, one of the things that constitute a key characteristic of the alternative securities market is what is being referred to as Designated Advisers who hand-hold the enterprise through the listing processes; and after listing, they help make sure that the enterprise is meeting the requirements of listing. This goes a long way in enhancing the corporate status and the financial strength of the SMEs and other companies that operate in the emerging sectors.

Meanwhile, if a company wants to be listed on the main board- the daily official list of the stock exchange, which is not where the SMEs would normally seek listing, the company does not need to have a designated adviser. All that is required for such an enterprise to meet the requirements for listing is to have an issuing house, lawyers, accountants and other professionals who can package the enterprise for the listing specifically. A key characteristic that is new for the Alternative Securities Market is that there is need to have a designated adviser that works with the enterprise so as to get the enterprise listed. However, after the enterprise has listed on the Nigerian Stock Exchange, the designated adviser remains with such an enterprise to ensure that it is able to meet the listing requirements on sustainable bases.

The role of designated advisers is greatly important because the number of SMEs that were listed in the past ended up being delisted because they were not able to cope with the sustainability of the listing requirements. Meanwhile, it should be noted that entrepreneurs have very specific characteristics; they are highly focused on their businesses and they nurture their passions for growth. According to Onigbinde and Sodipo (2013), however, entrepreneurs are not as focused on building a team or the building blocks that enable a company to be successful. So, a designated adviser helps in doing that. The designated advisers are pre-qualified by the Nigerian Stock Exchange and they are on the Nigerian Stock Exchange's website.

Therefore, an entrepreneur or a promoter of an SME can actually go on the website and look for the designated adviser (Oteh, 2014). These designated advisers are experienced accountants, experienced issuing houses and experienced business consultants who can work with budding enterprises and support them through the alternative securities market process. In addition, the alternative securities market scheme has worked successfully in South Africa, United Kingdom and in other parts of the world (Du Toit and Moolman, 2004).

4.1 Developing a Culture of Venture Capital and Private Equity in Nigeria

The Securities and Exchange Commission (SEC) had recently put together a package of reforms. According to Oteh (2014), one of them, of course, is working with the Nigerian Stock Exchange (NSE) to revamp the second and third-tier securities markets .The second, which is particularly critical, is to start to develop a culture of venture capital and private equity in Nigeria. According to Alfines (2005), the culture of having venture capital and private equity has been very critical in countries likes Israel and the United States, where SMEs have been nurtured as the engine of economic growth and sustainable development. The nurturing of SMEs from the beginning in an emerging economy like ours in Nigeria therefore becomes more imperative. The reason Google becomes one of the biggest companies in the world is the early foundation that was laid by the venture capital firm that supported it from the very beginning .There is certainly a need to have a culture of venture capital and private equity in Nigeria since there are opportunities to enjoy the full benefits' of such a culture. There are a number of state governments that are developing export processing zones in the country. However, the venture capital and private equity believe in an emerging enterprise ahead of a bank. The other aspect is that the venture capital and private equity scheme being champions by the Securities and Exchange Commission (SEC) presently can rely on the corporate business plan and the support that an enterprise is getting from a technical partner or somebody who is already well known (Oteh, 2014). This was not a case as a way to consider an enterprise coming to the market hitherto. Today, there are green field projects and new projects that do come on the market. There are accesses for brown field projects to also come on the market, which were not available in the past

5. Evaluation and Conclusion

Building an SME is like having a child and nurturing that child till he/she becomes an adult. The capital market, however, offers an avenue for growing the business enterprise, and creating value for it; while the ability to realize some of those values is strictly the prerogative of the entrepreneur. To list an enterprise, the venture need to have some form of a track record. The track record may not necessarily be a record of profitability as it was required in the past but the organization needs to have good corporate governance practices. Nevertheless, there is also a need to present a business plan that can guarantee good returns on investment.

However, documentation for SMEs to access the capital market is sine qua non for listing on the market. One of what the Securities and Exchange Commission and the Nigerian Stock Exchange do is to create greater awareness of what the processes are so that an entrepreneur can start as early as possible in preparing for the processing. The second is to make the process very fast. If an enterprise meets all the requirements for listing, then the council of the stock exchange can provide approval very quickly, while the SEC, as the supervisory and regulatory body for the capital market operations, can also do the same.

Therefore, there is no gain saying that there is clarity of what the processes are. The entrepreneurs can find it on the SEC's website, while they can also find the listing processes on the website of the Nigerian Stock Exchange. These procedures are clear; it is streamlined and the requirements are simple. Most importantly, it is also paramount that an enterprise get an expert, at least, a professional who can give reasonable financial advice. Meanwhile, there is a list of designated experts on the website of the Securities and Exchange Commission as well.

In conclusion, there are so many benefits in going to the capital market for the SMEs. One of them is building corporate brand image. What the stock market does is to create greater awareness for the enterprise, because on a daily basis people can buy or sell its stock. This helps the business enterprises because they will have a wider range of customers who can feel empathy, and participate in the creation of wealth. The second one is to build a lasting legacy; who would have known that the little funds that were invested in Facebook and Google would list them among the largest companies in the world? Therefore, going to the capital market also gives access to other sources of funding. Moreover, the NSE and SEC promote good corporate governance practice; so when a company is listed on the stock market, investors believe that such a company is well managed and they obliged to invest there-in.

5.1 Recommendations

From the evaluation done and conclusion drawn from the conceptual analysis above, the following recommendations therefore become imperative:

- Using the capital market to finance SMEs in a developing economy like ours in Nigeria should not be a matter of choice, but rather a part of the operating environment in the nation's financial system, especially in this contemporary regime of fairer trade in goods and services.
- The world is now a global village and Nigeria cannot pretend to be an island. Therefore, the Nigeria stock market should be build up with mass participation of SMEs to attain a meaningful sustainable growth and development.
- The Securities and Exchange Commission (SEC) and the Nigeria Stock Exchange (NSE) should continue to avail any micro, small and medium enterprise (MSME) showing desire to raise capital from the stock market of needed information and assistance upon contact.
- Nigeria, as a country, must appreciate the message of new theory of growth centred-around capital market's financial intermediation, and be willing to undertake significant and relevant financial reforms where necessary.
- Nigeria, as a country, needs to further re-define and domesticate the stock market in her economy as a way of overcoming the dichotomy between the formal and informal sectors vis-a-vis her capital market.
- There are needs to formulate investment friendly regulations; keep low inflationary rate; provide favourable government policies; and provide stable macroeconomic framework for the sustainability of informal and SMEs sector in Nigeria.

5.2 Suggestions for Future Research

The forgoing recommendations, however, contain grave lessons for all stakeholders in SMEs financing in the developing economies as Nigeria imbibe the lessons of new forms of the possible roles of stock market in funding micro, small and medium enterprises in the country. Nevertheless, the future researchers may extend the frontiers of knowledge by making a comparative analysis between money and capital market operations vis-à-vis SMEs' financing in a developing economy. Future researchers are also encouraged to embark on the appraisal of capital market operations in financing other vital sectors of any developing economy. Further research efforts are also needed to evaluate the possible role of capital market operations in public projects' financing in both developed and developing economies. This suggestions would certainly mitigate the developmental deficits that exist in the macroeconomic frameworks of many developing countries and as well provide further opportunities for SMEs' growth in those countries.

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