The Nigerian Capital Market

Submission by the Securities and Exchange Commission

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Committee on Capital Market and other Institutions,
House of Representatives of the Federal Republic of Nigeria

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INTRODUCTION

1. I am deeply honoured to present a report on the capital market's recent performance to this Honourable Committee. This interaction is both timely and auspicious given that it provides an opportunity for the house to examine the significance of the Nigerian capital market within the context of the nation's overall economic transformation agenda and arrive at a common understanding of necessary steps to advance the market. Nigeria is indeed fortunate to have passionate visionaries in the House of Representatives who canvass the course of an orderly growth and development of the country's capital market.

2. As you all know, the capital market is a common feature of every modern economy and is reputed, amongst other things, to perform critical capital allocation functions which promote growth and stimulate orderly economic development. In many advanced countries where capital markets correlate directly with the economy, the capital market is viewed as the primary gauge for the economy's performance. More so, capital markets with adequate depth play an essential role in economic development since they are the principal platform through which low cost funds to finance medium to long term projects on infrastructure and other important projects that transform economies are mobilized. Such markets are characterized by high investor confidence, market integrity, efficient processes, adequate product offerings,

sound regulatory framework, strong and transparent disclosure and accountability regime and good corporate governance. Markets with these attributes are classified as world class capital markets.

3. We believe Nigeria has the capacity to evolve into such a market. It is our strong conviction that a world class capital market is a necessity if indeed we aspire to better leverage our national wealth in terms of natural and human resources. In essence, the capital market can foster diversification of the country's economic base which is largely oil dependent and assist economic agents to pool, price and exchange risk thereby encouraging savings and investments and ultimately creating wealth. This conviction informed our vision "to build a world class capital market" as a catalyst for the realization of the country's full potential even as our leaders strive to address our socio-economic challenges.

4. As the apex regulator of the capital market therefore, this singular vision, the vision to evolve a world class capital market, a market that is complemented by necessary structures to attract world class institutions, one that is an efficient enabler of socio-economic development; which fosters meritocracy, good corporate governance, innovation and entrepreneurship and harnesses the entrepreneurial zeal of many hard working Nigerians, has been the thrust of all our activities.

5. Today, I shall present an overview of the state of the market, analyze developments which defined the market within the last decade and informed the underlining strategies for our reform agenda. Recognizing that the world has become a global village, attention will be drawn to some of the external factors which influenced developments in the Nigerian capital market highlighting the measures employed by SEC to mitigate the downside risk while optimizing positive prospects of these factors. I shall also outline the impact of our reforms on the market to date, our plans for the future. Given the importance of the House Committee's oversight role, we will make a case for the aspects of the ongoing market reforms for which the Committee's intervention is required.

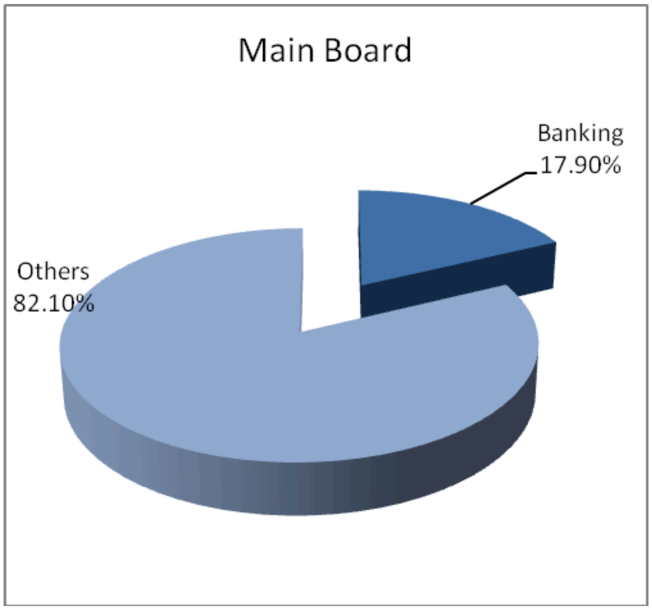
THE NIGERIAN STOCK MARKET'S EVOLUTION (1999 – 2009)

6. Ample understanding of the current state of the Nigerian capital market cannot be gained without a thorough understanding of the events which led to the un-usual growth which characterized the market prior to the downturn of 2008.

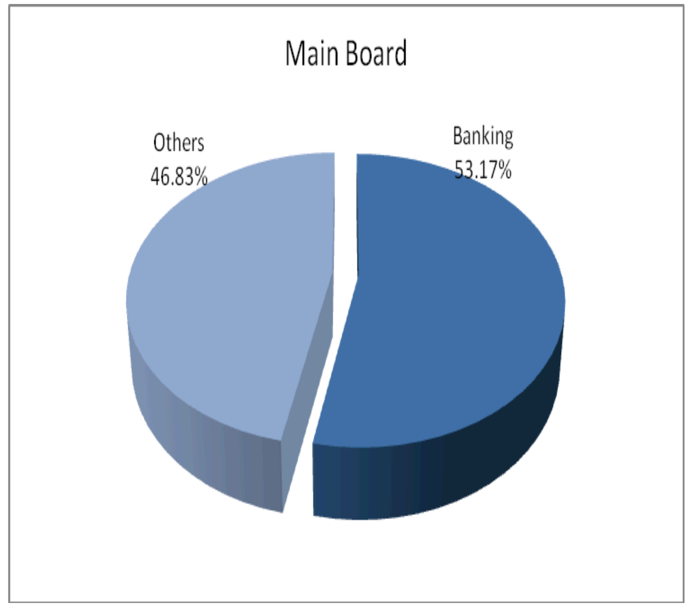
As you may know, the market was and is still predominantly driven by equities with the banking sector making up a significant proportion of total market capitalization.

Figure 1: Sectoral Composition

Sectoral Mix as at Year End 2011

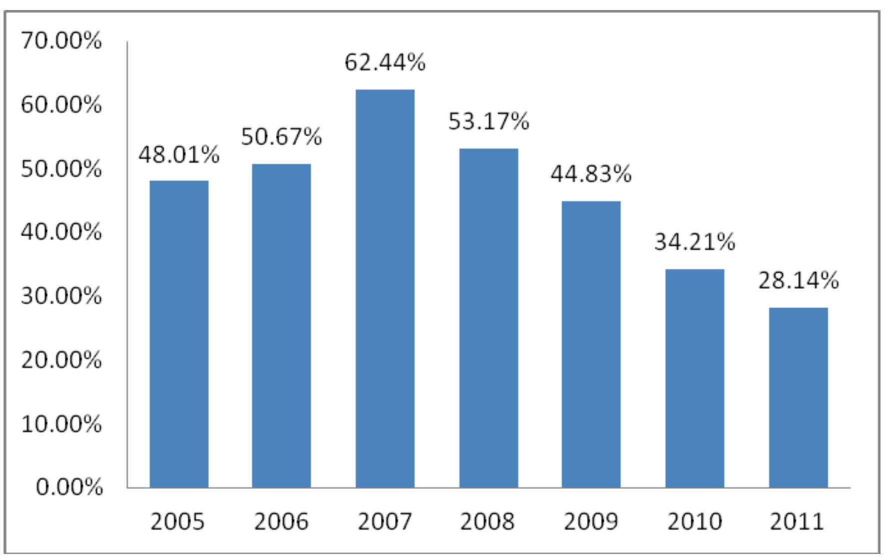


Sectoral Mix as at Year End 2008



Source: Nigerian Stock Exchange

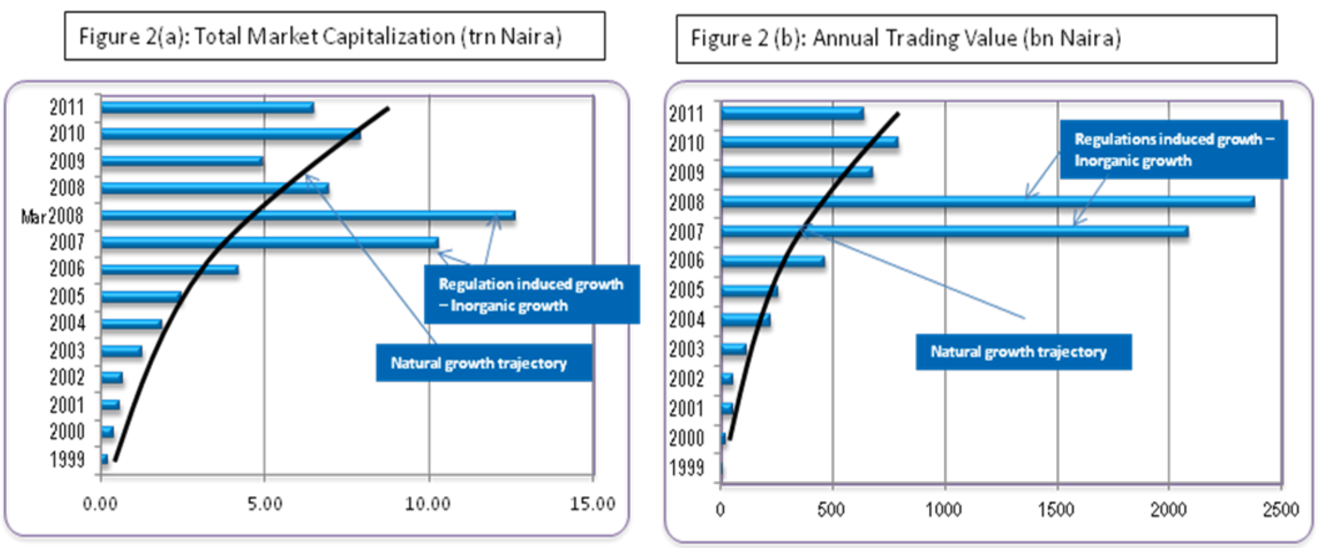
Figure 2: Bank market capitalization as a % of total market capitalization



Source: Nigerian Stock Exchange

7. Until the corrections of 2008, the stock market enjoyed a decade of high activity in both trading value and volume which grew at 176% and 153% respectively over the period. However, the in-organic growth recorded in the market was induced by the regulation which mandated the recapitalization of Banks and was a clear deviation from the markets natural growth pattern. As seen in the chart below, the 2007 and 2008 radical spikes in total market capitalization and trading volume were clear departures from the trend line of the market's natural growth.

Figure 3: Trend line for Market capitalization & trading volume



Source: Nigerian Stock Exchange

8. In 2004, Banks were mandated to shore up their capital base from N2 billion to N25 billion by December of 2005. This was in a move by the sector regulator, the Central Bank of Nigeria, to strength the institutions for global competitiveness. The exercise triggered a string of public offers, mergers and new listings. At the end of the first exercise, the increase in Banks' capital base

catapulted equities capitalization attributable to the sector from N400 billion to approximately N1.12 trillion, and led to the reduction in the number of banks from 89 to 25 by the end of 2005.

9. Since equities dominated the market, banking stocks by extension, became the major determinant of the fortunes of the equities market. Nonetheless, the positive market sentiments set off by the wave of bank driven public offers aroused corporate interest with record breaking new issuance activities. Aggregate new issues by corporate organization, which stood at N412.7 billion in 2005 increased to N1.34 trillion in 2007; a growth of 224.6%. Several real sector entities equally accessed the capital market for funds with strong public participation in the offers. The euphoria of the offers led to a surge in the average number of subscribers which rose to 99,000 subscribers in 2007 from 4200 in 2002. Many companies from different industrial sectors became first time issuers in the market during this period. During this period, the Nigerian Stock Exchange All-Share Index (NSE ASI) gained 161.64% while equity market capitalization increased by 384% from N2.5 trillion ($22.73 billion) in 2005 to N12.1 trillion ($110bn) in March 2008.

10. That period also saw a significant increase in the number of brokers, asset managers, and issuing houses that were established. Consolidation efforts and the ensuing capitalization opened up the Nigerian financial landscape to the international space.

11. Regrettably, emphasis on risk management and corporate governance did not evolve commensurately to support the fast growth. Invariably, the additional capital raised by the banks went into speculative lending to the oil and gas sector, and unregulated margin finance to brokers, and individual investors which fuelled an asset bubble. Banks engineered over-valuation of their stocks on the stock exchange prior to accessing the market for capital. This was in addition to the instances of financing the purchase of own stock in the primary market to create a semblance of huge investor appetite for such stock through shell companies.

12. There were also instances of "Pump and Dump", a market manipulation method wherein own stocks are purchased to push up price and public appetite. The own stocks are subsequently sold at premium when its valuation peaks. Since such pricing is not based on fundamentals, natural corrections would follow and the stock price would plummet.

13. The SEC's forensic investigations also uncovered evidence that there were manipulative transactions in the stock of listed companies outside the floor of the exchange. At the time, Regulators were neither sufficiently prepared nor well-positioned to monitor and sustain the explosive growth in the capital markets thus these illegalities largely occurred unhindered.

14. When therefore the global financial crisis triggered large portfolio outflows, international investors exited the Nigerian capital markets to address challenges in their home countries. Stock prices started to decline, prompting margin calls and local investors who were unaccustomed to huge and persistent declines started to panic, fueling more sell orders, further depressing prices and eroding investor confidence. The situation was exacerbated by the huge borrowing and margin finance exposure of individual investors, brokers and banks.

15. Between 2007 and 2009, the market lost over 70% of its value. Obviously, investors were traumatized by the occurrence. Naturally, confidence was lost and domestic investors have since then not fully returned to the market. By 2009, new issues had dropped by 93.5% to only N85.9 billion from the peak of N1.3 trillion in 2007.

NIGERIAN STOCK MARKET (2010 – 2011)

16. The SEC's strategic interventions to strengthen the market, restore investor confidence, engender market integrity and stimulate interest in the market began to yield positive results in 2010. The market rebound as the All-Share Price Index gained 18.9%, closing at 24,770.52, Equity market capitalization increased by 58.5% (from N4.99 trillion in 2009 to N7.91 trillion in 2010, driven mainly by the listing of Dangote Cement which made up about 25% of the market capitalization) and trading value increased by

17.0% (from N681.6 billion in 2009 to N797.55bn in 2010). The improvement in the market after two very turbulent years was a welcome relief to market participants and fueled hopes of early recovery of the market.

17. The improvement in the market was also witnessed in primary issuance as the number grew from 9 issues in 2009 to 23 issues in 2010 as issuers evidently saw a window of opportunity as the market showed signs of recovery. Twenty three (23) new issues which comprised 12 equities, 6 corporate bonds and 5 sub-national bonds were issued. The 12 equities issued were mainly rights issues to existing shareholders. It is worthy of mention that given the fragile equity market, issuers were increasingly shifting to bonds. This perhaps had been further encouraged by a number of reforms in the bond market.

18. The hope of a quick recovery in 2011 given the trends in 2010 was not realized owing to developments during the year. At the end of 2011, equities market capitalization declined to N6.5 trillion ($43.06 billion) and the NSE ASI fell to 20,730.63, representing a 17.42% and 17.07% dip respectively from the closing figures of 2010. Similarly, the total trading value dropped to N634.92 billion ($4.18 billion) representing a 20.39% decrease from N797.5 billion ($5.38 billion) recorded in 2010. Average daily transaction also declined to N2.68 billion in 2011, a drop from the 2010's daily average of N3.32billion. At year-end 2011, the market

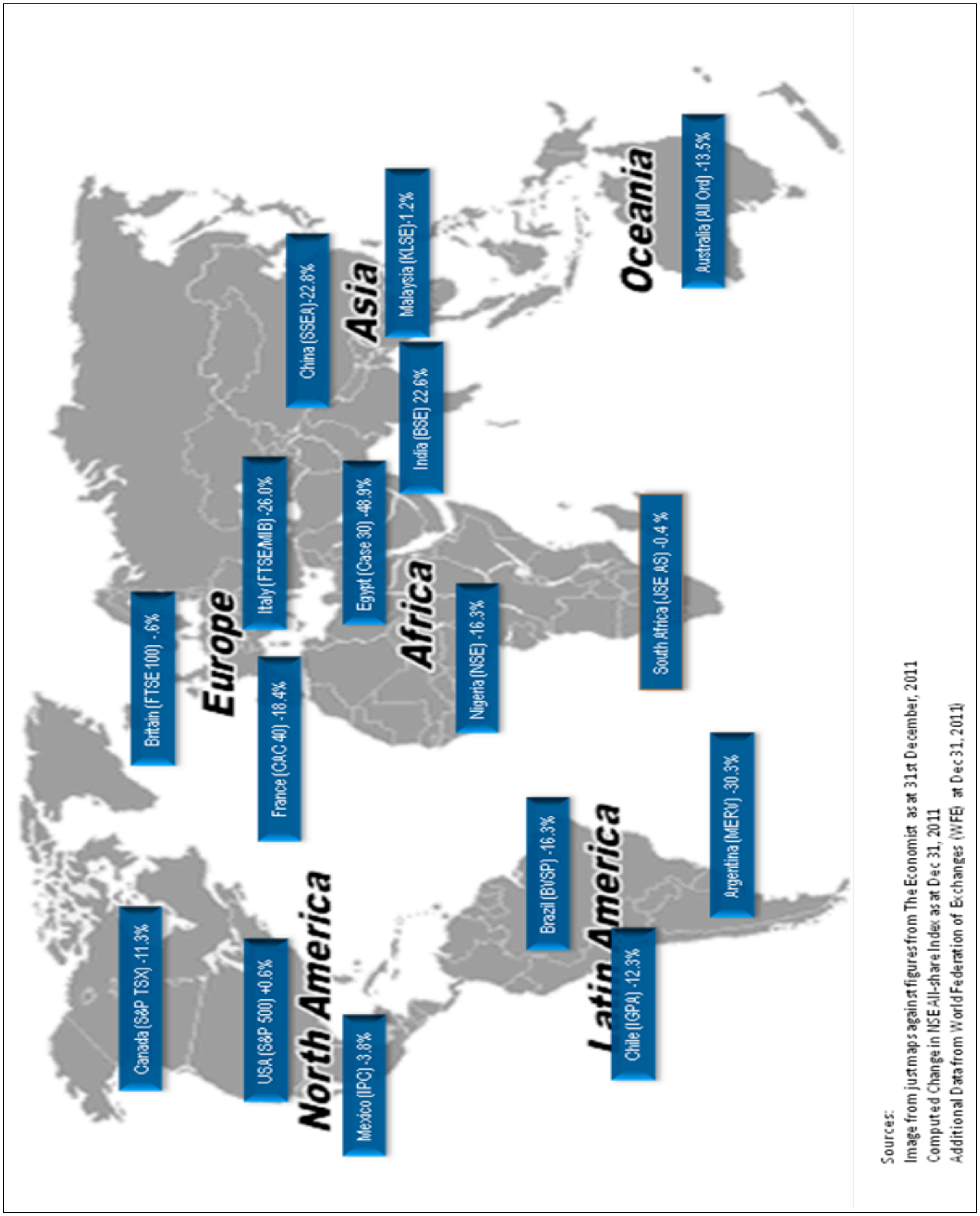
capitalization of all 201 listed equities – 198 stocks and 3 preference stocks – accounted for 63.62% of total market capitalization, while in 2010, 217 listed equities accounted for 76.67% of the total market capitalization.

Figure 4: Snap shot of the Nigerian capital market (2010 – 2011)

	2010	2011	% Change
Total Market Capitalization	N10.33 trillion	N10.28 trillion	(0.48)
Market Cap. (Equities)	N7.92 trillion	N6.54 trillion	(17.42)
NSE All Share Index	24,770.52	20,730.63	(17.07)
Total Volume (units)	93.34 billion	89.58 billion	(4.03)
Total Value	N797.55 billion	N634.92billion	(20.39)
Avg. Daily Vol.(units)	377.87 million	364.15 million	(3.63)
Avg. Daily Value	N3.23 billion	N2.58 billion	(20.12)
Turnover Ratio	12.51	8.36	(33.17)
No. of New Issues (Approved)	31	34	12.90
Value of New Issues (Approved)	N2.44 trillion	N2.03 trillion	(16.80)
No. of Listed Companies	217	198	(8.76)
No. of Listed Equities	220	201	(8.64)
No. of Listed Bonds	44	48	9.09
No. of Listed ETFs	0	1	
No. of Listed Securities	264	250	(5.30)
No. of Trading Days	247	246	
Avg. Exchange Rate (Naira: USD)	148.31	151.82	

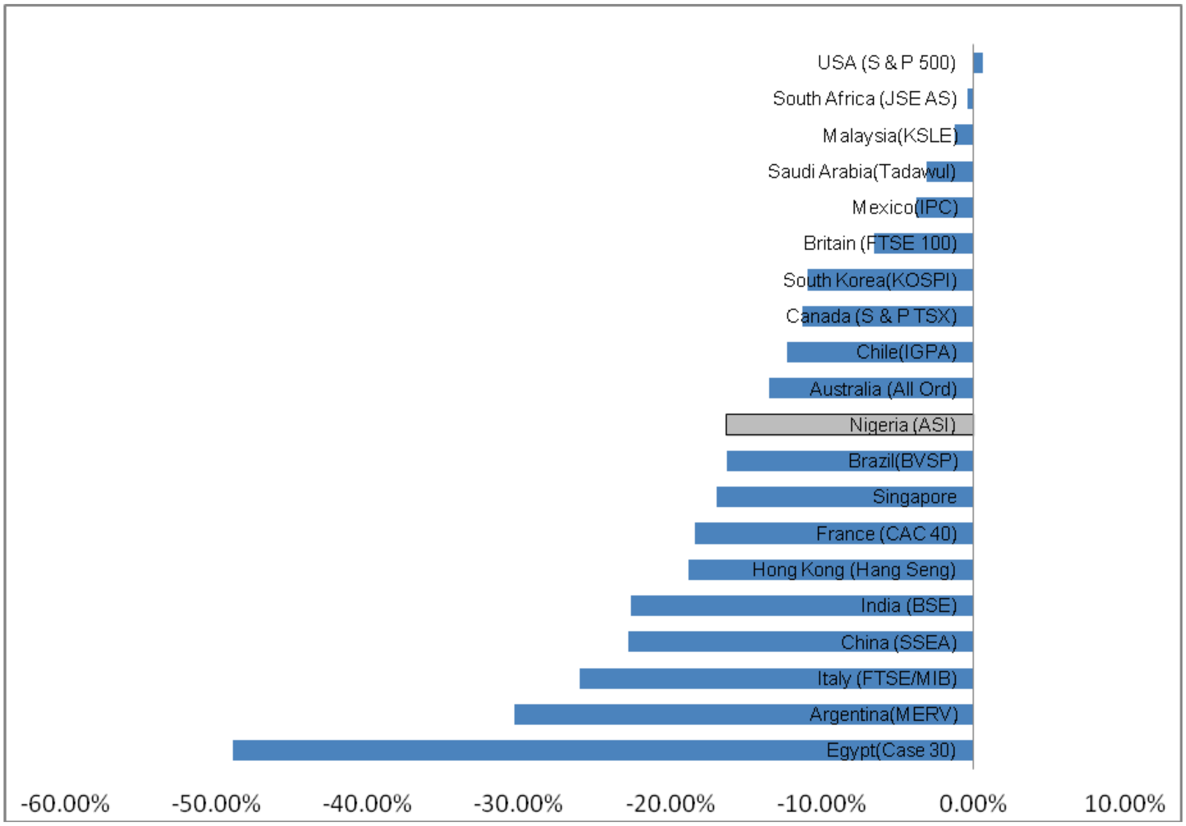
Source: Nigerian Stock Exchange

Figure 5: Comparison of Market Index across various regions in 2011



19. As you would note from Figures 5 and 6, the decline in the Nigerian market notwithstanding, the Nigerian market outperformed a number of global markets.

Figure 6: Closing index for major markets across regions



Source: World Federation of Exchanges, Country Exchange Data

20. Therefore, Nigeria's decline of 16% in market capitalization should be viewed in the context of a 22.8% stock market decline in China (SSEA), 16.3% in Brazil, 22.6% in India, 48.9% in Egypt, 26% in Italy, 30.3% in Argentina, 18.4% in France.

21. Despite the general downturn in the capital market, the number of new equities issued increased in 2011 compared to 2010 as shown below:

Figure 7: Number & Value Of Sub-National & Corporate Bonds 2008-2011

	Number Of Issues				Value (billion Naira)			
	2008	2009	2010	2011	2008	2009	2010	2011
Equities*	49	5	12	16	939.06	31.24	120.34	224.26
Corporate Bonds	2	1	6	8	5.17	13.17	77.29	70.26
AMCON Bond**	-	-	-	1	-	-	-	17.62
Sub-National Bonds	1	3	5	5	50.00	41.50	157.50	119.00
Total Debt	3	4	11	14	55.17	54.67	234.79	206.88
Overall	**52**	**9**	**23**	**32**	**994.23**	**85.91**	**355.13**	**431.14**

Source: SEC

**Excluding equity placement of N854 billion to AMCON by Intercontinental Bank Plc (N548.35 billion) and Union Bank Nigeria Plc (N305.70 billion)*

***Cash portion of AMCON bonds issued to Institutional Investors*

22. In 2011, a total of 16 new issues (6 Rights Issues, 9 Private Placements & 1 Preference Shares Issue) worth N141.78bn were concluded in the year, representing an increase of 18% in value over the 2010 figure of N120.34bn through 12 issues.

FIXED INCOME MARKET

23. Given the importance of the fixed income market in providing long term funds for the economy and in the quest to deepen the capital market, the Commission embarked on measures to develop this sector of the market through introduction of rules such as those on book building and shelf registration

among others. These initiatives have shortened the average issuance period and improved the price discovery process for bond issues and other issuance. To facilitate the development of the bond market, a bond resident adviser was engaged for a period of 18 months through an IFC/ESMID programme. As a result of these efforts by the SEC, bond issuance by sub-national and corporates has increased. In the last 2 years the market witnessed the flotation of 14 corporate bonds and 10 sub-national bonds compared to just 4 corporate and sub-national bonds in 2009 as shown on the table below:

Figure 8: Sub-National and Corporate Bonds 2010 And 2011

	2010		2011	
	Corporate Bonds	N'bn	Corporate Bonds	N'bn
1	UACN Property Dev. Co. Plc	15.0	Sterling Bank Plc	7.50
2	United Bank for Africa Plc – S1*	20.0	Dana Group of Company Plc	9.00
3	Flour Mills Nigeria Plc –S1	37.5	Lafarge WAPCO Plc	20.00
4	Chellarams Plc –S1	1.50	NAHCO Plc	2.15
5	Tantalizers Plc (Loan stock of US$7.0 million)	1.05	United Bank for Africa Plc –S2	35.00
6	C & I Leasing Plc	2.24	Tower Funding - S1*	4.63
7			Chellarams Plc –S2	0.54
8			Vital Products Plc	0.55
	Sub-national Bonds		Sub-national Bonds	
1	Lagos State Government –S2	57.50	Benue State Government	13.00
2	Bayelsa State Government	50.0	Niger State Government –S1	9.00
3	Kaduna State Government	8.50	Delta State Government	50.00
4	Ebonyi State Government	16.50	Ekiti State Government	25.00
5	Edo State Government	25.00	Ondo State Government	27.00
	Total	234.78	Total	203.37

Source: SEC
**S1 Represents Series 1*
***S2 Represents Series 2*

COLLECTIVE INVESTMENT SCHEMES

24. The Commission has taken a number of steps to strengthen Collective Investment Schemes through more regular on-site and off-site inspections of the schemes as well as transfer of fund assets to custodians to better safeguard the assets. It has also strengthened trustees' oversight of the schemes and initiated the formation of an Association of Fund Managers, as a trade group. In addition, the Commission holds periodic meetings with the association and has made extensive overhaul of rules on Collective Investment Schemes which have improved the operation of such schemes.

25. Furthermore, the Commission took a number of actions against erring fund managers and trustees. The various actions of the Commission have improved confidence in CIS schemes resulting in the flotation of more schemes in number and variety.

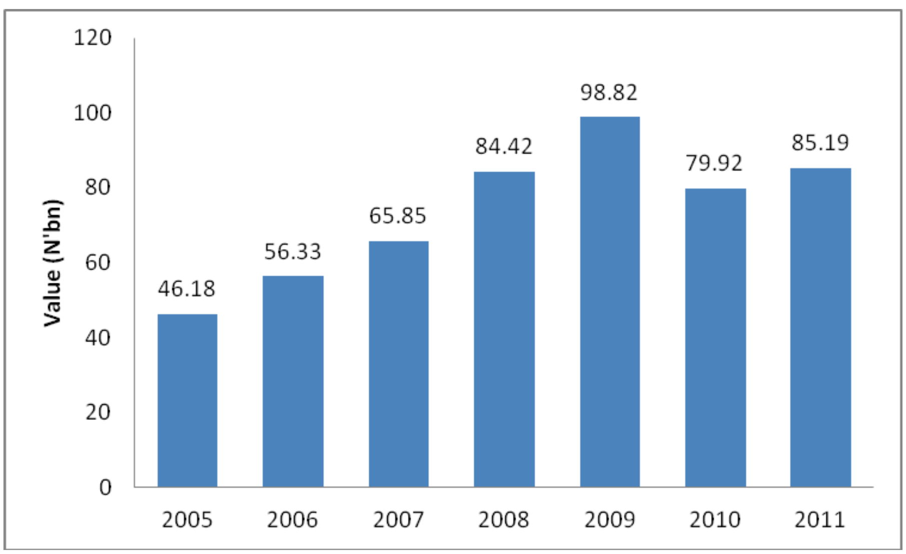
26. There were 43 registered Collective Investment Schemes with a net asset value of N85.3 billion as of February 2012. The schemes included bond funds, equity funds, balanced funds, ethical and Islamic funds, Real Estate Investment Trusts (REITs), Exchange Traded Fund (ETF) as well as Private Equity Funds. These provided investors the opportunity to diversify their portfolio. There is great potential to expand this segment of the market particularly given the recent experience of retail investors in direct investing. One of

the market development strategies of the Commission is to focus on collective investment schemes in order to bring in more Nigerians into the capital market.

Figure 9: Unit Trust Schemes By Types Of Fund As At February 2012

Type of Fund	Number	Net Asset Value (N)
Equity	20	41,548,512,984.61
Money Market	2	3,293,859,522.40
Bond	4	6,053,697,550.94
REIT	2	16,632,953,335.61
Balanced	11	12,019,664,503.76
Ethical	4	5,701,223,181.22
Sector	1	64,271,075.74
Total	43	85,314,182,154.28

Figure 10: Net Asset Value (N'bn) of Unit Trust 2005 – 2011



27. Nonetheless, the gains which characterized the first half of 2011 were reversed in the second half of 2011. Consequently, the equities market returned all the gains of 2010. Events which adversely affected the market included:

28. <u>Weak Global Economy</u>: Concerns over the fragile global economy intensified with the Euro zone debt crisis, United States credit rating downgrade and general economic uncertainties. This fuelled cautious international investor sentiments by international investors and flight to fixed income, money market instruments and gold. Also, the political impasse in Cote d'Ivoire early in the 2011 had some contagious impact on the Nigeria Market. The Crisis in the Middle East and North Africa (MENA) region may have also had some contagion effect on the Nigerian and other African Markets.

29. <u>Resolution of the Banking Crisis:</u> In 2009 the CBN had released an audit report which indicated that ten banks were in distress. Following the injection of N620bn, the CBN established a timeframe within which the Banks would be recapitalized to ensure that their distress would not lead to a systemic risk. At the time, the CBN took the proactive steps to prevent further deterioration instead of revoking licenses or handing the banks over to the Nigerian Deposit Insurance Corporation (NDIC).

30. At the expiration of the recapitalization timeline, 3 banks - Afribank, Bank PHB and Spring Bank - had yet to complete the recapitalization exercise and appeared to lack capacity to do so. In a pre-emptive step by regulators to save the financial service industry from the impact of failure of these institutions, the CBN and NDIC intervened. Consequently, the Banking licenses of the

institution were withdrawn and three bridge banks were formed under a purchase by assumption agreement. The interventions preserved all the deposits and some of the assets of the institutions but induced further fragility in investor sentiment as shareholders in those institutions lost their holdings.

31. Monetary Policy Decision: The Central Bank of Nigeria (CBN) revised the Monetary Policy Rate (MPR) upward six times during the year, driving it from 6.25% in January to 12% in November 2011 in its bid to fight inflation. The CBN also increased the Cash Reserve Ratio (CRR) of banks to reduce pressure on the Naira while the measures were effective in preserving the purchasing power of consumers, it led to the portfolio rebalancing in favour of bonds and money market to the disadvantage of equities.

32. Local Investor Apathy: Given the losses suffered by shareholders from the market crisis in 2008, many local investors are thus hesitant to return to the market. The losses heightened risk aversion by investors and flight to money market instruments, bonds and real estate investment. Investors' aversion to equities dampened corporate interest in equity issuance.

33. Debt Overhang: High margin loan exposures continue to distract stockbrokers from focusing on their core businesses. As brokers continue to bear the brunt of the debt overhang given the over significant levels of margin loans arising from the exposure to

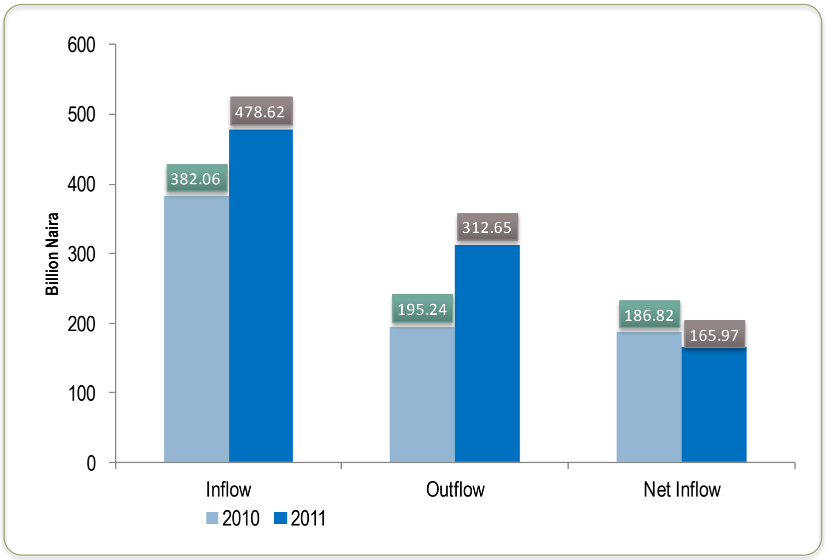
banks, their ability to provide liquidity to the market has been significantly impeded.

34. Security Challenges: The spate of bombings by the Boko Haram sect has led to an increase in the perception of insecurity in some parts of Nigeria with consequent negative impact on the market.

35. Foreign Participation: On a positive note, foreign interest in the market grew with over 60% of trades driven by foreign institutional investors. Total foreign portfolio investment inflow according to the Nigerian Stock Exchange was N478.62 billion in 2011 as against an outflow of N312.65 billion. This resulted in a net positive inflow of N165.97 billion during the year. In 2010 there was a net inflow N186.82 billion.

36. Estimated assets of foreign investors under custody with the four (4) main Custodians were over N730 billion as at September 2011. Perhaps foreign investors are being encouraged by the reforms in the capital market to invest in Nigeria and taking advantage of the undervaluation of Nigerian Stocks.

Figure 11: Foreign Portfolio inflow 2010/2011



Source: Nigerian Stock Exchange

37. <u>The Bond Market:</u> The Bond market witnessed significant activities in 2011. While the Federal Government issued a total of 28 new tranches of outstanding bonds valued at N791.27billion, a total of N183.79billion worth of new fixed income securities was issued by states and corporates. State government issued bonds totaling N97 billion which were variously applied to infrastructural projects across the individual states. Also noteworthy is the increase in the tenor profile of these bonds - Seven (7) years for three (3) out of the four (4) sub-national bonds from the 3 – 4 year tenor of previous issues. Invariably, State Governments have realized the potential of the market to enable actualization of their developmental agenda and are willing to leverage the market for longer periods.

38. In the secondary market segment, a total of 8.95billion units of FGN Bonds valued at N7.99 billion were traded, a drop from N15.8 billion in value of FG bonds traded in the preceding year. Most of these transactions were conducted on the Over the Counter (OTC) market.

THE NIGERIAN STOCK MARKET IN 2012

39. The Nigeria Stock Exchange opened in 2011 with an All Share Index (ASI) of 20,730.63 and a total market capitalization of N6.53 trillion, down by 17.1% and 18.6% relative to the January 4, 2010 figures of 25,102.93 and market capitalization of N8.02 trillion respectively. As of March 9, 2012, marginal improvements were recorded as total equities market capitalization grew to N6.61trillion with the market closing at ASI of 20,950.01. This rise was driven by the increased demand for some banking stocks following the successful merger and acquisition of some banks in the country. We expect this trend to continue as short term investors take positions in order to profit from the share price appreciation in coming weeks.

40. On a positive note, the shares of Austin Laz and Company Plc were listed on the floor of the Exchange on 29th February 2012. We are optimistic that this is the first of many listings which will be recorded in 2012.

MEASURES TO STRENGTHEN THE NIGERIA CAPITAL MARKET

41. The impact of the global financial crisis and the subsequent stock market crash while devastating for the Nigerian capital markets, has given the Commission an opportunity to reposition the Nigerian Capital Market to play a pivotal role in capital formation and the development of the Nigerian economy. As a first step towards reforming the market, the Commission constituted a Committee of experts to undertake a diagnostic review of the Nigerian Capital Market. In addition, Accenture, a reputable global management consulting firm, was engaged to assist the Commission with a review of the organization's systems and processes with a view to enhancing operational efficiency. The US SEC was also invited to conduct a peer review of the Commission. The recommendations made by these assessments on the vital building blocks of a world class market have been taken into account in the Commission's reform agenda. Some of the areas of focus for the Commission's reform program are outlined below:

42. Strengthening the SEC: The report mentioned above highlighted the importance of capacity within the SEC. Areas that will facilitate the upgrading of the SEC include human capital, technology and process. The SEC has begun implementing these recommendations.

43. *Technology:* Significant investments have been made to enhance our technology platform. Since it began the retooling exercise, the Commission has increased its cost efficiency, minimized its turn-around-time, automated a number of its process, and enhanced its communication channels. Specific investments include:

- Networks & Communications: The Commission has succeeded in building a shared technology system for common services and capacities. By this, all Zonal offices and Head office are connected over a secure Wide Area Network (WAN). This singular achievement enabled the Commission to transition from an analogue organization to a fully digital institution.
- Procurement of productivity tools: To complement the network inter-phase, the Commission procured work tools such as workstations, laptops and operating software for staff across all zonal offices. Handheld work tools have also been issued to eligible staff with full access to official emails to enable staff function from offsite locations.
- Commissioned a Data Centre: The Commission now boasts of a fully equipped Network Operations Centre from where all the Commission's networks are monitored.
- Implemented business applications such as the margin listing software which will be launched during the year.
- Data Storage: The gross inadequacy of storage and memory for corporate mail services has been upgraded with the acquisition of a network file server.

- Development of tailor-made application software: The SEC commenced the development of application software for electronic registration and returns analysis. As an interim measure while completing the e-filing process, the Commission introduced e-offer application to facilitate the filing process by market intermediaries.

44. *Human Capital:* In a review of the operations of SEC Nigeria conducted by the US SEC, the point was made clear that significant capacity issues burdened our Commission. There is no doubt that poor capacity on the part of SEC Nigeria contributed to the heavy impact of the downturn of 2007 – 2009. Low capacity meant that the Commission was poorly positioned to check market abuse, and to swiftly punish parties at fault.

45. According to the US SEC, our Commission "appears to be over-weighted with administrative personnel and has a shortage of professional staff." Thus the report noted the need to "attract well trained, aggressive professional talent," in fact "the best talent in the financial industry." The report deplored the prevalent hiring by patronage that might have denied the best-qualified candidates an opportunity to work for the Commission.

46. The US SEC report confirms an earlier (December 2008) independent report by Accenture, which found that staff in support roles constituted 48% of the SEC workforce, as against only 24% in roles critical to the Commission's core mandate. "It is unlikely that current staffing in terms of skills, competence and abilities, deployment and utilization can deliver a world class market regulator," Accenture noted. All of this was is in consonance with my own observations upon assumption of office in January 2010, that we had a significant gap in capacity at the level of the regulator. To address this gap, it was needful therefore that the Commission injected a crop of fresh and technically competent professionals into the organization. After a thorough and rigorous recruitment exercise named "Young Professionals' Programme", the SEC in December 2011, engaged 52 young professionals comprising lawyers, economists, accountants. This is intended to fortify the personnel strength, and add vigour to the activities of the Commission.

47. The recruitment exercise was the result of a transparent process which ensured the engagement of only the best and the brightest of 34,292 applicants. The new hires have undergone a bootcamp akin to that of fortune 500 companies and are currently undergoing internship with capital market operators and law firms. They are expected to assume full duties within a few weeks.

48. The Commission has continued to leverage our strategic relationships within IOSCO as well as with the US SEC and others to deliver relevant training in the critical mandate areas and grow the capability of staff to enhance market efficiency, oversight and professionalism. Furthermore, discussions are at advanced stages with institutions such as Oxford University, Guarantco, Financial Services Volunteer Corps, etc to take advantage of capacity building opportunities being offered by the institutions.

49. The Commission is also currently reviewing the business model and operational framework of the Nigerian Capital Market Institute to be able to effectively deliver on its mandate of providing training and other capacity building services to Nigeria and by extension the West African sub - region.

50. In addition, the Commission hopes to partner more effectively, with capital market trade and professional groups to design and implement focused training programmes to further develop the requisite skills for the market.

51. *Governance and Internal Control:* The Commission must hold itself to highest standards if it is to demand same from the market it regulates. The Commission invested in an Enterprise Resource Planning System to automate its administrative and financial management processes. This will ultimately enhance our internal control, reduced overhead and improved efficiency.

52. <u>Strengthening the NSE</u>: To strengthen and improve the governance of the NSE, the SEC as is well known intervened in the Nigerian Stock Exchange in 2010. A new CEO and Executive Director have since been appointed and assumed duties. The new management team is currently introducing positive changes to the process, technology, regulation and more importantly the governance of the Exchange. Recognizing the potential of the market, the management of the NSE has set a target market capitalization of $1trllion by 2016 along with the introduction of 5 new products in 5 years commencing in 2011, a target which the SEC fully endorsed. The new management met its 2011 target with the introduction of the Newgold Exchange Trade Fund (ETF) in December 2011.

53. <u>Demutualization of the Nigerian Stock Exchange:</u> Given the importance of demutualization to the global competitiveness of the Nigerian Stock Exchange, the Commission is taking steps to prepare the framework and guidelines. Specifically, on 22 September 2011, the Board of the SEC set up an industry-wide committee to examine issues around demutualization of the Exchange and make appropriate recommendations to the

Commission. The Committee submitted its report to the Commission on 29th February 2012.

54. It is expect that demutualization will reposition the NSE to provide a fairer, more efficient and more transparent system of operation that will enhance liquidity, improve price discovery and institute good corporate governance which are essential features of an effective Self Regulatory Organization (SRO). It will bolster investor confidence and enhanced international competitiveness of our exchange and invariably the market. The increased operational efficiency, enhance profile and the heightened competitiveness which will accrue to the exchange by this exercise will significantly augment our overall capital market reforms and development agenda in particular and the economy in general.

55. In addition to setting up an industry-wide committee to offer guidance on the road map for demutualizing the NSE, the Commission had also obtained technical assistance from FIRST, a multi-door grant facility that provides technical assistance to promote financial sector strengthening, hosted by the World Bank. The Consultant was engaged to provide advisory and capacity building services to the Commission in particular and the market as a whole. Indeed a national workshop on demutualization was facilitated by the Consultant on 9th March 2012 to deepen our knowledge and understanding of demutualization.

56. Privatization of Abuja Securities and Commodity Exchange (ASCE): Given its importance to the growth of the national economy, the Ministries of Finance, Trade and Investment and Agriculture, Central Bank of Nigeria (CBN), ASCE and the SEC are collaborating in efforts to reform the ASCE. An inter-ministerial meeting led by the Coordinating Minister of the Economy was held with the World Bank in the third quarter of 2011. This was with a view to aligning the structure and operations of the Exchange with the Agricultural Transformation Agenda of the federal government. The World Bank's final report will form the basis for further action in this regard.

57. Strengthening Public Companies: To ensure that corporate governance practices in Nigerian public companies align with international best practices, a new corporate governance code was issued by the SEC and became effective in April 2011. The code is quite extensive and covers all aspects of corporate governance. The Commission has had a number of enlightenment sessions with publicly listed companies to enable them understand and effectively comply with the code. Companies are expected to periodically file their level of compliance with the code with the SEC. Currently, over 135 of the 198 listed companies have signed up for full compliance with the new code which will no doubt promote transparency and accountability in public companies.

58. Strengthening the Market Operators: In collaboration with the US Securities and Exchange Commission and the USAID, the SEC organized a week long training workshop in July 2011 which attracted three hundred and forty six (346) market operators and financial sector regulators. The week long workshop served as a forum for exchange of ideas on global best practice in the development and regulation of capital markets. The workshop also provided participants with up-to-date tools to professionally handle enforcement and contemporary market development and oversight duties particularly in light of the recent global economic and financial challenges.

59. In addition to bridging competency gaps and enhancing technical capacity, the SEC is also working with the Brokers to determine appropriate minimum capital requirement, human capacity and technology that will ensure they become more competitive.

60. Improved Financial Disclosure: Periodic disclosure of financial information and the quality of such information have improved in recent years as a result of enhanced monitoring, enforcement and the requirements for higher quality information disclosure from public listed companies by the SEC and NSE. In the last 3 years, the SEC sanctioned 187 companies for non-compliance with financial disclosure requirements, while the NSE also delisted about 10 companies in 2011 for non-compliance with its listing rules. To

improve disclosure in prospectuses, the SEC in the last few years has also introduced a number of new rules and rules changes.

61. Adoption of International Financial Reporting Standard (IFRS): Given that 2012 is the migration year stipulated by government for IFRS in Nigeria, the SEC in 2011 continued to invest enormous resources to ensure seamless transition by public companies. For example the SEC has approved for the Financial Reporting Council of Nigeria (FRC) to use Nigerian Capital Market Institute (NCMI) to commence an IFRS academy launched by FRC to address the dearth in IFRS skills. In a similar development, the SEC is working with the World Bank to organize IFRS Clinics for the purpose of providing technical support to public companies. A series of workshops and seminars were held to acquaint Chief Executive Officers, Finance Directors and Compliance Officers of targeted companies with the new regime in financial reporting.

62. Improving Liquidity: The Commission is working with various stakeholders to improve liquidity in the market. Apart from new listings, we believe that the formal take-off of market making, security lending and short selling will improve liquidity in the market. The Commission recently approved the NSE's rules on market making, short selling and securities lending.

63. Other measures being taken by the SEC to improve liquidity include:

- Encouraging more institutional investors such as PFAs and insurance companies to participate in the capital market
- Lowering transaction cost
- Encouraging improvements in trading infrastructure which the NSE is vigorously pursuing
- Encouraging Introduction of more products in the market
- Continued improvement in corporate governance practice
- Planned dematerialization of certificates
- Introduction of e-offers
- Promoting the take off of an over the counter market

64. New Products: The SEC endorsed the NSE's product introduction strategy. Under a 5 year plan, the NSE introduced Exchange Traded Funds (ETF) in 2011 following SECs approval. The roll out plan will see the introduction of financial options in 2013 and financial futures in 2015. On our part, the SEC is designing a framework for the introduction of Sukuk (Islamic bonds) in the Nigerian capital market to provide issuance variety.

65. The Commission is also working closely with the Ministerial Steering Committee to improve bond market liquidity through the establishment of a virile secondary bond market. This is notwithstanding recent efforts by the Commission to license inter-dealer brokers with the intent of establishing electronic trading platforms for bonds. We are also working to expand Collective

Investment Schemes (CIS) such as Ethical and Islamic Funds, and Real Estate Investment Trusts (REITs) among others.

66. New Listing: The Commission believes that that new listings are critical to the development of the Nigerian Stock Market given that it is one of the two ways companies can raise long term capital. Indeed, new listings are even more critical in restoring investor confidence as they are clear signals that the stock market is recovering.

67. Having identified the constraints to listing and deployed some measure to attract eligible companies, the Commission approved the NSE's new listing rules which cover oil and gas and solid minerals companies as well as SMEs amongst others. It is our belief that the new listing rules would attract companies in these sectors to list.

68. The Commission is determined to ensure that sectors of the Nigerian economy which are under-represented on the exchange are encouraged to participate. This measure will transform the Exchange into the primary barometer for measuring the economy as exemplified in more advanced economies.

69. Currently, Agriculture constitutes over 40% of the country's GDP yet only 0.04% of the market capitalization of the NSE is accounted for by Agriculture. Another sector under consideration

is the oil and gas sector which accounts for 90% of Nigeria's export revenue, more than 70% of fiscal revenues and 14% of GDP. Despite the sector's importance to the economy, no upstream oil and gas company is listed on the Nigerian exchange. Global brands such as the Anglo-Dutch multinational Royal Dutch Shell have had presence in the country long before independence, yet have never listed on the Exchange.

70. Perhaps the most notable sector of the economy yet to be appropriately represented on the Exchange is the telecoms sector which is considered the fastest growing sector of the economy and contributes about 5.5% of GDP. Despite Nigeria's booming telecoms market, with over 80 million subscribers, there is but one Telecommunications Company traded on the NSE. With the recent revisions to the listing requirements, the Commission is set to upturn this trend.

71. In addition to the market deepening potential of new listings, the companies will reap the benefits of higher corporate governance standards required of listed companies. Listing will also engender brand extension and democratize their successes. It will also enhance the participation of Nigerians in the economy and elicit necessary empathy on the safety of company assets. Finally, listing on the Exchange will enable appropriate valuation of the entities. The Commission will continue in its efforts to encourage more companies to list. Following the lead by Austin

Laz, we understand that some other public companies that had already registered their securities with the SEC are preparing to list.

72. Besides encouraging private companies to list on the Exchange, the Commission has also engaged the Bureau of Public Enterprises and the Federal Ministry of Power, on the listing of state owned enterprises scheduled for privatization under the federal government privatization agenda. Ultimately, privatization of Nigeria's power sector could see as many as 17 power generation and distribution companies filing for Initial Public Offers (IPO) in due course.

73. As efforts are made to attract new listings, genuine concerns of listed companies would continue to be addressed without undermining disclosure standards and market integrity.

STRENGTHENING REGULATORY OVERSIGHT AND ENFORCEMENT:

74. We believe that we cannot have a strong market or command investor confidence and public trust if our enforcement machineries are weak. Our greatest strength is in our ability to take enforcement actions without fear or favor and without regard for whose ox is gored. The Commission therefore has zero tolerance for market infractions and indeed any act which could undermine the integrity of the market. Recently, the Commission took various enforcement actions against operators and issuers with respect to inadequate filing of periodic returns and other market infractions.

75. Risk Management: The market crisis of 2008 exposed the weaknesses of companies and regulated entities in the area of risk management as many companies paid little attention to the identification and management of risk. The Commission therefore now requires regulated entities in particular, to employ efficient and effective risk management framework that will enable them identify and manage risk effectively. This is also emphasized in the 2011 corporate governance code.

76. The Commission has also adopted a risk-based approach to supervision of regulated entities which is now the best practice in regulation of financial intermediaries. The framework for its implementation has been put in place and will become operational in due course. The SEC in collaboration with the CBN formulated guidelines on Margin transaction to forestall excessive margin lending which contributed to the financial crisis in Nigeria.

77. Rule Making and Enforcement Actions: Seventy (70) new rules and rule amendments have been released since 2010 to further strengthen the capital market. The SEC also took various enforcement actions against operators and some publicly quoted companies. For instance, between 2010 and 2011, 52 companies were suspended for various capital market violations, while 30 companies were referred to law enforcement agencies for further action. This excluded the 260 entities and individuals whose cases

were taken to the Investment and Securities Tribunal for various violations. The zero tolerance stance of the Commission against market infractions saw the sealing up of the premises of many illegal market operators (Wonder Banks) across the country.

78. The NSE in pursuing market integrity with the same vigor as the SEC suspended 60 stockbroking firms for failing to comply with the directives of the Commission to maintain a N70 million minimum capital base. We also facilitated the refund of about N200 million by market operators in cases of breach of contractual agreements and non-refund of money to investors during the year. We penalized 14 fund managers for non-rendition of returns while one (1) case involving mismanagement of funds was earmarked for enforcement action.

79. The Commission has strengthened its working relation with law enforcement agencies especially the Federal Ministry of Justice, Economic and Financial Crimes Commission (EFCC) and the Nigeria Police Force (NPF). It had resident legal teams from both the Federal Ministry of Justice and established a police desk in 2010 in the Commission. This assisted in investigation and enforcement activities.

80. <u>Complaints Management:</u> In 2011, the Commission received 729 complaints and resolved 709. 156 cases were referred to the enforcement and compliance department of SEC for necessary

action. Over the past three years (2009 to 2011), an average of 882 new complaints were received each year; while an average 848 complaints were resolved each year. However, 2010 had the highest number of complaints both received and resolved, owing largely to the sanitization embarked upon when the present leadership of the SEC took office in January of that year. In 2010 alone, 1,223 complaints were received as against 695 of the previous year and 1,169 complaints were resolved while 316 were referred for enforcement action, as against 666 resolved and 102 complaints referred for enforcement action in 2009. The drop in 2011 indicates a drastic reduction in number of infractions committed as a result of increased regulatory vigilance.

Figure 12: Schedule of Complaints

Description	2009	2010	2011
Complaints brought forward	999	926	664
New complaints	695	1.223	729
Resolved complaints	666	1,169	709
Referred for enforcement	102	316	156
Outstanding complaints	926	664	528

Source: Securities and Exchange Commission

81. In total, 3646 complaints were treated in the period 2009 to 2011, out of which 2544 were resolved and 574 were recommended for enforcement action. As testimony to the diligence of the Commission, the number of outstanding complaints reduced drastically from 926 in 2009 to 664 and 528 in

2010 and 2011 respectively. This shows a reduction of 28.3% in 2010 and a further reduction of 20.5% in 2011.

82. A breakdown of the complaints shows that most of the complaints received against stockbrokers relate to non-remittance of share sales proceeds and non-purchase of shares. In 2010, 305 (or 45.9%) out of a total 665 complaints received that year against brokers alleged non-remittance of share sale proceeds. The increase from 120 of similar complaints of the previous year was largely as a result of the incidence of margin lending involving banks and brokers. As of 2011, following actions by the SEC, the NSE and AMCON, the complaints reduced to 107 or 20% out of 532 similar complaints received in the three years.

83. The Commission has recently developed an enhanced complaints management programme, which is expected to be fully launched at the end of April 2012.

84. Our breakdown also shows that complaints against registrars mostly bordered on failure to return money for un-allotted shares, as well as non-receipt of dividend warrants. In 2009, 350 complaints were received alleging unreturned money for un-allotted shares, while 230 complaints related to non-receipt of dividend warrants. The Commission's rigorous engagement with registrars (by way of a reconciliation exercise) and active enforcement led to a significant reduction in these cases, such that in 2011 only 45

(allotment) and 90 (dividend warrant) complaints were received. In 2011 alone, the Commission resolved 300 registrar-related complaints which were more than 251 of such complaints received that year.

85. Monitoring and Inspection: Pursuant to the mandate to ensure compliance with the Anti-Money Laundering Prohibition Act (2011) and relevant Rules and Regulations, the Commission conducted ninety (90) inspections on Capital Market Operators. We also reviewed a total of 1,594 returns from 337 market operators in 2011.

86. Investor Protection Fund: The Commission is at an advanced stage in the establishment of an Investor Protection Trust Fund as required under Part XIV of the Investments and Securities Act (ISA). The Corporate Affairs Commission is poised to approve the registration of the Fund upon receipt of approval from the office of the Attorney General of the Federation (AGF). The Fund is intended to provide compensation for investors who suffer loss in the market as a result of the insolvency, bankruptcy, negligence or misappropriation committed by a market operator.

INVESTOR EDUCATION AND OUT REACH

87. <u>Investor Education:</u> The Commission believes that an educated investor is a protected investor as he is better able to take informed investment decisions. The Commission has thus, outlined various investor education strategies and outreach programmes to improve the understanding of the retail investor and restore investor confidence. For Example, in July 2011, the Commission collaborated with the Rivers State Government and successfully hosted an investor/issuer education outreach for the government and people of Rivers State. Over 1000 participants were offered critical insights into the market as an ensemble of capital market experts participated over the interactive sessions presided over by the SEC. This was done to educate the citizenry and government of the state on the benefits of investing in and sourcing funds from the capital market.

88. To commemorate 50 years of capital market regulation in Nigeria, the Commission on October 31 2011, organized an international investor forum in Abuja under the theme "Nigeria, the preferred investment destination." The event was well attended by leading international and local investors, as well CEOs and financial sector leaders. It showcased the wealth of investment opportunities in Nigeria. At the October 31, 2011 event, the Commission unveiled a Nollywood movie, titled "Breeze". The goal of the Commission, amongst others, was to leverage the following enjoyed by Nollywood as a platform to reach a wider spectrum of people. "Project 50," as the series of events marking the Golden

Jubilee is called, will culminate in a bigger investment forum in October 2012.

89. The Commission also believes that it is important to inculcate a culture of saving and investing in the younger generation. The Commission's investor education strategy is therefore designed to appeal to various target groups including students, given the need to catch them young. The strategies have included out-reach and town hall meetings with the public, establishment of capital market clubs in secondary schools, quiz programmes, introduction of capital market studies in universities and publications of various types.

90. Given the centrality of social media to stakeholder management in the 21st century, the Commission has incorporated the use of Facebook and Twitter into the stakeholder management matrix. The deployment of this neo-media has enhanced public awareness on the market and also created a platform for an increased number of Nigerian and foreigners alike to interface with the Commission directly.

91. <u>Promoting OTC Platform:</u> We are promoting and supporting the creation of an over-the-counter market which hopefully would attract more companies to the capital market and also provide additional platform for bond trading. To this end, the National

Association of Securities Dealers (NASD) and FMDA OTC Plc have forwarded applications to the SEC to set up Over- the- Counter (OTC) trading platforms in Nigeria. The Commission recently approved the registration of ICAP Brokers Limited as an inter-dealer broker in the Nigerian Capital Market. Their role is to provide price discovery mechanism for bond dealers.

92. Whistle blowing: Keeping up with international best practices, the SEC Nigeria has remarkably improved its regulatory and market development processes. One such enhancement is in the use of whistle blowers for market surveillance. The SEC encourages individual employees of firms to report infractions committed by either their employers or by other capital market operators (CMOs). As you may know, Section 306 of the Investments and Securities Act (ISA) 2007 gives an employee the right to disclose information suggesting that a crime has been committed or is likely to be committed, to their employer, or the Commission. Whistle blowers are protected under the law: an employee who suffers any form of victimization as a result of making disclosures is entitled to reinstatement or compensation. And the Commission is under a duty to investigate complaints received from whistle blowers.

93. We have set up whistle blowing hotlines. Professionals are currently undergoing training and before the end of April, we shall

fully launch the whistle-blowing platform. A code of conduct will be released as part of this initiative.

CONCLUSION:

94. Although, the Nigeria capital market has gone through and indeed is still going through some difficult period, the potentials of the market are enormous. Perhaps foreign investors see these potentials more than local investors given the increasing involvement of the former in the capital market. The Commission will continue to work aggressively to bring back local investors. One of the priorities is to strengthen the stock broking community through risk-based capital requirement and strong corporate governance while expanding instruments in the market as earlier mentioned.

95. The Commission is an Appendix "A" signatory of IOSCO and chairs the Africa and Middle East Regional Committee of the organization and subscribes to the 38 principles of securities regulation which are critical to our becoming a world class capital market. Capital market are very important to the development of any economy, we are hopeful that the various reforms will enhance the capacity of the market to become a critical source of funds for infrastructure and industrial development and contribute meaningfully to the actualization of vision 2020.

96. In conclusion, the Commission seeks the support of the National Assembly particularly the Committee on Capital Market in its drive to actualizing its vision to build a world class capital market through the initiatives highlighted in this paper among others.