CAPITAL MARKET AS A CATALYST FOR ECONOMIC GROWTH AND DEVELOPMENT

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ABSTRACT

This paper investigated the nature of the capital market as a catalyst for economic growth and development in Nigeria. The paper enumerated the common products in the sector and detailed how they are linked to public and private sectors of the economy. The critical role of the capital market in channeling investor's funds to public and private projects were also discussed. Further, the paper identified the major investors in the capital market and described the policies, which have improved the participation of both local and foreign investors. It showed that an increase in capital market activities and efforts to mainstream the Capital Market Master Plan (2015-2025) initiatives into the national development agenda would go a long way to addressing many of the challenges of the economy.

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1. INTRODUCTION

Economic growth is an increase in the production of goods and services in a country, often measured by changes in real Gross Domestic Product (GDP). However, the concept of economic development is larger as it includes improvement in the quality of life and living standards of the citizens. These include improvements in literacy, health and life expectancy, better savings-investment culture as well as improved wealth distribution, housing and environment.

There are many capital market products and mechanisms that can be used to stimulate economic development. This piece considers products such as bonds, equities and commodities as well as the activities of domestic retail, institutional and foreign investors that may contribute to the process of economic growth and development.

2. CAPITAL MARKET PRODUCTS

Bonds are issued by corporate, sub-national, national and supranational institutions to raise funds for their expenditures and investments. At the end of second quarter of 2018, the bond market capitalisation of the Nigerian Stock Exchange (NSE) stood at N10.11trn. The FMDQ also provides a platform through which these bonds and other instruments are traded.

Recently, the Nigerian government issued N100bn Sukuk to finance 25 road projects and issued N10.791bn Green bonds to finance afforestation, renewable energy and provision of clean energy. Similar opportunities also exist to issue revenue bonds to finance revenue-generating projects, which will exert less pressure on government budget and allocation.

The Nigerian bond market therefore has the potential to close the country's huge infrastructure deficit. An AfDB (2013) report shows that Nigeria's annual GDP growth can increase by 4 percentage points if the country's infrastructure is scaled up to the level of African middle income countries. It is estimated that Nigeria needs to invest US$350 billion in its infrastructure sector between 2011 and 2020. A total sum of $131.2b is expected to be mobilised from the private sector.

In addition to the general purpose bonds often issued, infrastructure project bonds can be issued to finance debt obligations of a single-asset infrastructure project. It is designed such that the expected income from the executed infrastructure is securitized to ensure payment of the bond's interest and principal.

All these will be supported by the credit enhancement offered by institutions like InfraCredit and GuarantCo as well as the operations of the infrastructure funds registered by the Commission.

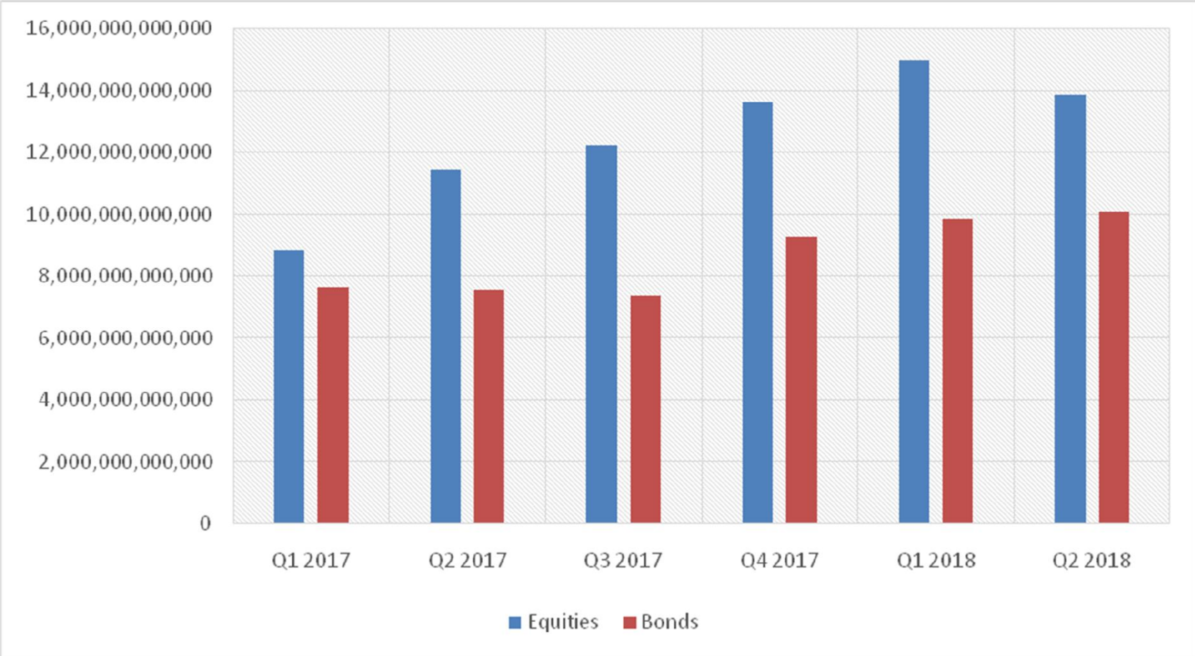

Figure 1: Equities and Bond Market Capitalisation the NSE

Equities have also been issued by many public companies to raise funds and expand their operations. This has engendered improved productivity, employment and governance. Equally, government has utilized the platform of the capital market to privatize some of its enterprises in order to make them profitable, less bureaucratic and less dependent on government's lean resources. Through these equity issuances and privatization, citizens are able to invest, own and partake in the wealth of companies, thereby aiding financial inclusion and wealth creation.

The capitalisation of the equities market on the NSE stood at N13.88trn at the end the second quarter of 2018. In addition, public companies that are not listed on the NSE have their shares traded on the NASD platform.

Commodities value chain and trading are other areas where the capital market makes significant contribution to economic growth and development. Nigeria is endowed with agricultural resources but pricing, storage and transportation mechanisms have continued to pose problems. Most of these problems can be addressed by a vibrant commodity exchange system, which the SEC is working towards achieving. AFEX commodity exchange is currently operational in the country while the Nigerian Commodity Exchange (NCX) is undergoing some restructuring to further deepen the commodities market.

3. CAPITAL MARKET INVESTORS

In addition to the above instruments, the activities of various capital market participants contribute to economic growth and development. Examples include activities of domestic retail and institutional investors and foreign capital inflow. For instance, domestic retail investors are able to earn income on their investments in capital market securities. This has the potential of reducing household poverty and inequality levels, which are key measures of economic development. By the first half of 2018, domestic retail investors accounted for 20.2% of the transactions on the NSE.

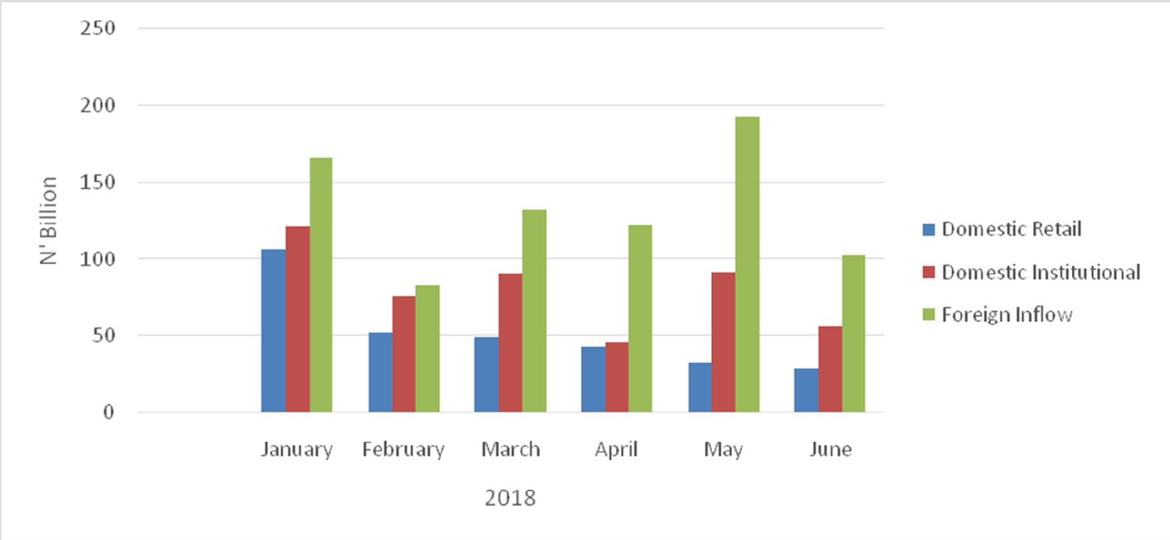

Figure 2: Investors' Participation in the Nigeria's Equities Market

The Federal Government also commenced issuing savings bonds in March, 2017 which allows retail investors to participate in the bond market. So far, 31 savings bonds have been issued with the total amount allotted standing at N8.52bn. Further, opportunities exist for retail investors to reduce their risk exposure by investing in collective investment schemes (CIS) comprising diversified baskets of securities. The volatility of these types of investments is less and they can be safer. The net asset value of CIS in Nigeria currently stands at about N610bn and is growing.

Domestic institutional investors equally invest in capital market instruments to generate value for their clients and their institutions. Examples in Nigeria include the Pension Funds, Insurance companies and Banks. At the end of April, 2018, Nigeria's pension fund assets stood at N8.1trn and the bulk of the funds are invested in capital market instruments. Investment in FGN bonds stood at 49.34%; ordinary shares at about 10%; corporate debt at 4.4% and CIS at 0.23%.

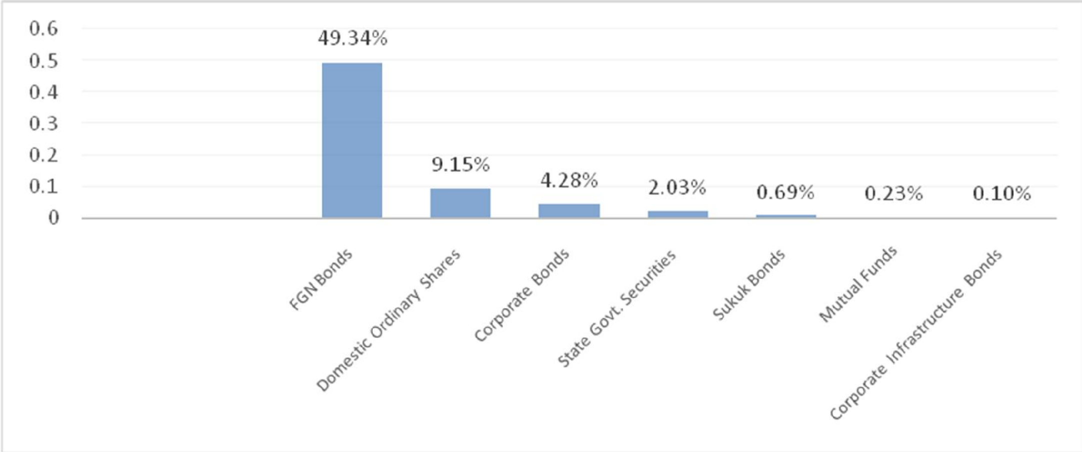

Figure 3: Allocation of Nigeria's Pension Asset

Foreign capital inflow improves a country's profile in terms of exchange rate, external reserves, balance of payments and economic growth. A vibrant capital market is a major attraction to capital inflows. In the first quarter of 2018, out of the $6.3bn capital importation into Nigeria, portfolio investments into the capital market accounted for 16.5%. Further, foreign investors have accounted for about 50% of the transactions on the NSE this year with the attendant positive impact on market efficiency and liquidity.

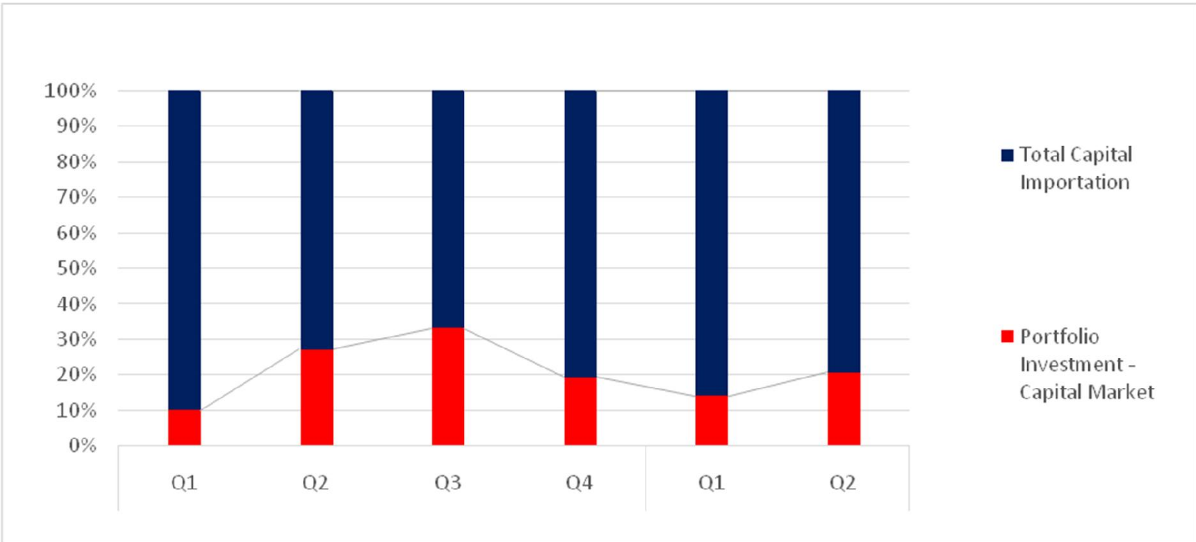

Figure 4: Foreign Portfolio Investments in Nigerian capital markets

Nevertheless, there is still a need to encourage more retail investor participation, so that the market can be less vulnerable to the behaviour of foreign investors as often seen. Various efforts have therefore been made in this direction, especially industry-wide policies and initiatives to further deepen the Nigerian capital market in terms of products and participation.

4. INDUSTRY POLICIES AND INITIATIVES

One major initiative to tap the potential of the Nigerian capital market was the development of a ten-year Capital Market Master Plan (CMMP) launched by the Commission in 2014. The Plan has over 100 initiatives to spring–board the Nigerian capital market as one of the world's deepest and most liquidas well as the largest in Africa by 2025.

It is also aimed at ensuring that the market contributes much more to the socio-economic development of the nation particularly in facilitating capital-raising for sustainable development and transformation of key sectors.

Some of these initiatives include the e-Divi dend payment, Direct Cash Settlement, Dematerialization, Financial Literacy, Non-interest Capital Market, Complaints Management Framework, Liquidity Enhancement and Equity Listing Enhancement. Each of these initiatives is contributing to the growth and development of the Nigerian capital market, and by extension, the economy.

The E-dividend Management System campaign is meant to tackle the growing number unpaid dividends due to investors in the market. This initiative is complemented by the dematerialization of share certificateswhich resolved the long-standing issue of carrying and posting paper dividend warrants. The initiative also addressed issues of irregular signatures of shareholders. Numerous investors have testified to receiving dividends accrued and have newfound belief in the efficiency of the capital market. As such, over 2.5 million account holders have registered for the e-dividend while more are expected to come forward.

Direct Cash Settlement initiative provides investors with the means to settle trade directly into their accounts instead of their brokers, thereby improving transparency and confidence in the system. This is an important initiative, which gives more confidence to the public to invest funds in the market without having to worry on whether a broker can make away with the proceeds of their investment.

Financial literacy initiatives are aimed at improving financial inclusion, which is an integral component of economic development. The Capital Market Committee established a Financial Literacy Committee, which engages investors on multiple platforms including social media to educate them on the capital market. Furthermore, successful efforts have been made to inculcate capital market studies into the curriculum of secondary schools to improve awareness of the industry. It has been ensured that all capital market stakeholders contribute to these initiatives towards ensuring their success and ownership.

Following the financial crisis of 2008, many complaints were tabled before the Commission. The decision to efficiently handle these cases led to the creation of the Complaints Management Framework. The framework seeks to organize market operators into SROs registered with the Commission to facilitate complaints management in the market.In order for the implementation of the framework to be effective, it has been made mandatory for all Trade Groups to register with the Commission while capital market operators must also register with their relevant Trade Groups.

Further, the Listings Committee was set up to encourage new listings in a bid to further develop the market. The committee engages with both public and private unlisted companies and presents the benefits of listing. It has also met numerously with the Bureau of Public Enterprise (BPE) on the benefits of increased transparency and improved corporate governance that characterizes listed companies.

In addition to the foregoing, there are various committees working on and proffering solutions to different issues concerning the market. Some of these include: enhancement market liquidity, introduction of electronic Initial Public Offering (e-IPO), establishment of minimum operating standard, enhancement of commodities trading ecosystem and development of non-interest capital market.

5. CONCLUSION

The capital market has a critical role to play in economic growth and development of a country, and the Nigerian capital market has not been left behind in performing this role. The Nigerian capital market has funded critical public and private projects from both local and international issuers and investors. Specifically, governments at various levels in the country have, at different times, resorted to issuing bonds in the capital market to fund key development and infrastructural projects. Equally, the equities segment of the capital market has provided funding for companies to expand operations and for the government to privatize/divest ownership of its enterprises.

In addition, both domestic institutional and retail investors have participated in the capital market to earn income and generate employment. Through the activities of foreign investors, the market is increasingly becoming more efficient and the foreign capital inflows have been used to augment the country's external reserves with attendant benefits on exchange rate. All these are geared towards the development of Nigeria.

Therefore, the current initiatives by the Nigerian capital market regulator, in conjunction with other stakeholder, to further develop the market are laudable and ultimately beneficial to the country. It therefore crucial that more supports are given towards increasing the number and depth of capital market instruments, raising the level of investors' participation and properly mainstreaming the capital market into the national development plan and agenda.