RESTORING INVESTOR CONFIDENCE AND VALUE CREATION IN THE NIGERIAN CAPITAL MARKET

Presented by

Adeolu Bajomo

Executive Director, Market Operations & Technology
for

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Outline

• About the NSE
• Understanding the Boom Years: 2004 - 2008
• Understanding the Burst Years: 2008 - 2011
• Enter The Future
  – NSE Vision and Goal
  – Objective and Outcome
  – NSE Key Initiatives
  – Outlook: 5-Year and 2012
  – Restoring Investor Confidence
• Creating Value in a Bear Market
Established in 1960; Company limited by guarantee

Approx. 5 million investors:
Foreign – 81% of market activity
Local – 19% of market activity

234 active Broker-Dealer firms
28 member Issuing Houses

Equities – 199 listed cos. N6.35t ($40.56b) mkt cap
Bonds – 52 bonds N5.23t ($33.40b) mkt cap
ETFs – 1 ETF N1.09b ($6.96m) AUM

14 electronic trading floors around Nigeria
3rd largest stock exchange in Africa by capitalization
Services the 2nd largest financial center in sub-Saharan Africa

Figures as at 29-Feb-2012
A ₦1,000 investment in 1996 would have been worth ₦13,029.26.

Peak: March 5, 2008
ASI 66,371.20

-17.07
-20.39
Enter the Bull – 2004 to 2008
Understanding the Boom Years: 2004 - 2008

1. Consequences of the steady rise in Liquid Gold Price - 2004 to 2008
   - From $25/barrel to $110.20/barrel on 12-Mar-08
   - Banking system flooded by oil revenues, driving up deposits and lending, and accelerating credit creation
     • Banking assets grew 76% avg. post-consolidation
   - Real sector unable to absorb excess liquidity from oil revenues and foreign investments in productive sectors, driving flows to non-priority sectors and the capital market
     • Increases in margin loans and proprietary trading
   - Lacking regulatory framework enabled surge in market capitalization
     • Market cap of banking stocks grew by a factor of 9
     • Lacking evidence supporting commensurate improvements in companies’ fundamentals
     • Stage set for a “bubble”
Understanding the Boom Years: 2004 - 2008

2. Low financial literacy, market discipline and consumer sophistication
   - Spike in retail participation with first-time investors pouring into the market
   - ASI surged 225.37%; market cap of listed equities grew 841.46%
   - Investment decisions based on speculation (herd mentality)
   - Easy access to loan facilities usurped the need for proper financial planning
   - Risk management processes were overlooked in anticipation of higher return on investments and loans by banks
     - Unprecedented level of bank over-exposure and high rates of margin lending

3. Inadequate regulatory framework failed to enforce rules of the capital market
   - Inadequate disclosure by listed companies and broker-dealer firms
   - Lack of enforcement by the Regulators
4. Amorphous management processes and poor governance
   – Lenient approach to overseeing the capital market
     • Known lack of will to enforce the rules of the markets, including sanctions for market infractions
     • Requisite analytic data for management purposes not available
   – Priorities skewed by market performance
     • No Council Committee structures and no performance management framework
   – Inability to adequately manage systemic risks
   – Cultural nuances, professed status and perceived success of the market impinged on good leadership
   – Deficient communication by the Exchange; fell short of addressing investor fears (both locally and internationally)

The four triggers of the market CRASH.
But the Boom was Now Meant to Last Forever…

"Mr Deputy Speaker, we will not return to boom and bust."
Budget Statement, 7 March, 2001

"As I have said before Mr Deputy Speaker: No return to boom and bust."
Budget Statement, 22 March, 2006

Gordon Brown, Former PM of the UK on Burst and Boom Cycles
Enter the Bear – 2008 - 2011
• Global Financial Crisis
  – Triggered by the sub-prime mortgage crash
  – The Myth of “Too Big to Fail Banks” was broken

• Nigerian banking crisis
  – N30b ($119.13m) market cap erased in one day; Banking Index down 34.69%

• Low broker-dealer participation rates
  – Margin loan debt overhang and lack of access to financing (CBN prudential guidelines)

• Unfavorable interest rates

• Eroded investor confidence
  – Preference for government paper

Understanding The Burst Years 2008 - 2010

Flight To Safety Is Prime

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The Nigerian Stock Exchange
2011 Equity Market Drivers

• Sovereign Debt Crisis
  – The Myth of “Governments don’t go broke” was broken

• Soft global economy and cautious foreign investors
  – Eurozone contraction (Aug-Dec) with half of 17 zone economies forecast to shrink in 2012
  – 17-year unemployment high in UK and record high of 10.7% in 17-member zone; credit ratings for 9 Euro nations cut by S&P (Jan 2012)
  – US economy recovering – 3.0% growth in Q411; Inflation at 2.9%; Unemployment down to 8.30% (Jan 2012) from 8.50%

• Unfavorable interest rates
  – MPR Rate at 12%

• Lack of liquidity and depth
  – Low equity issuance, no IPO in 2011
  – PFAs and Institutionals on the sidelines; Inordinate ratio of foreign-to-local participation
## 2011: A Tough Year All-Around

<table>
<thead>
<tr>
<th>Global Indices Performance</th>
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<tbody>
<tr>
<td><strong>ASI -17.42%</strong> (NSE Nigeria)</td>
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<tr>
<td><strong>IBOVESPA -18.88%</strong> (BM&amp;F Bovespa)</td>
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<tr>
<td><strong>FTSE/JSE ASI -0.99%</strong> (JSE)</td>
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<tr>
<td><strong>FTSE 100 -5.55%</strong> (LSE)</td>
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<tr>
<td><strong>MASI -12.37%</strong> (Casablanca SE)</td>
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<td><strong>WIG -21.68%</strong> (Warsaw SE)</td>
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<tr>
<td><strong>EGX 100 -46.08%</strong> (Egyptian Exchange)</td>
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<tr>
<td><strong>NASDAQ Composite -2.67%</strong> (NASDAQ OMX US)</td>
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<td><strong>NASI -31.11%</strong> (NSE Nairobi)</td>
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<tr>
<td><strong>S&amp;P 500 -1.12%</strong> (US – NYSE Euronext &amp; NASDAQ)</td>
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<td><strong>SEMDEX -4.67%</strong> (SE Mauritius)</td>
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<td><strong>S&amp;P CNX Nifty -25.14%</strong> (NSE India)</td>
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<tr>
<td><strong>Ghana Composite -2.34%</strong> (GSE)</td>
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<td><strong>HANG SENG -20.32%</strong> (Hong Kong Exchanges)</td>
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State of the Global Economy

• Debt Crisis in Western Economies
  – Sovereign debt threatening survival of Euro
  – Importation of Euro crisis into capital markets (Greek bond yields > 30%)
  – Downgrading of credit rating (European equities down)
  – Impact on FDI for Nigeria and other emerging economies

• Global Markets In Bear Territory
  – Most now pre-2009 levels (bear market territory)
  – More than $10 trillion eroded from US Equities during height of 2011 downturn
  – MSCI All-Country World Index of 45 nations down by 20% in 2011

• Global Economic Growth Easing
  – Recession a stark reality for most European economies
  – Slow down in growth for commodities, with impact on emerging economies
  – Global economic slow down in the horizon (downward revision of GDP growth)
State of the Nigerian Economy

• Banking Crisis Over but Impact High
  – We now have best capitalised (and stable) banks on the universe
  – Nationalisation and delisting of 3 banks wiped min of N170bn from equity prices
  – Confidence of equity holders impacted

• GDP and Employment
  – Relatively strong and sustainable GDP growth
  – Worsening trend in youth employment and overall job creation
  – Unemployment rate estimated at 22%

• Tightening Monetary Policies
  – Pressure on Naira (easing in 2011)
  – MPR at 12% with direct impact to bond and equity prices (flight to safety)

• Global Competitiveness
  – Difficult place to do business (index ranking remains low)
  – Not in top 10 economies most likely to transform radically in short term
2012 Outlook - Global

- Global recovery underway, surrounded by risks
- Eurozone debt crisis remains a key risk to the world economy
- Concerns surrounding sovereign debt sustainability
- Volatility in certain regions (and sectors) driven by prolonged unrest
- Slower growth projected in OECD countries*
  - 2.1% (2011), 2.6% (2012), 2.5% (2013)
    - US 2.9%, Eurozone 1.8%, Japan 2.6%
- Non-OECD countries to sustain world growth*
  - East Asia & Pacific 8.1%, South Asia 7.7%; Sub-Saharan Africa 5.7%
    - Nigeria 7.5%

* Figures reported by World Bank
2012 Outlook – Nigeria’s Comparative Advantage

- Economy growing at 7.5%+
- Large population (largely under 30)
- Strong profitable growth businesses (Food & Beverages, Manufacturing)
- Relaxed labour and investment laws
- Short term outlook in oil prices positive
- Huge mineral reserves
- Under-exploited manufacturing base
- Entrepreneurship “Can do, Will do” Attitude
- Possibly strongest banking sector in the world in terms of capital ratio

Nigeria must seize the opportunity!

* Figures reported by World Bank
The Nigerian Bull Re-Emerges? 2012 to ?
The NSE’s Vision

“To be the leading Stock Exchange in the African region for capital formation, driven by transparency, innovation, efficiency and liquidity.”

To become the gateway to African Markets.

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The Nigerian Stock Exchange

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Current Position

- NSE services the 2nd largest financial centre in sub-Saharan Africa
- NSE is the 3rd largest stock exchange in Africa by capitalization
- NSE is the largest market in West Africa by company capitalization
Drivers of Success

Integrity
- Accountability
- Effective Corporate Governance
- Transparency and Strong Regulation

Durable Wealth Creation
- Operational Efficiency
- Technology and Supporting Infrastructure
- Capacity Building
- Demutualisation

Market Leadership
- Listings Development
- Market Development
- Product Development
- Strategic Alliances

Transformational Capital Market Customer Experience
Key Initiatives

The Organization
- Reconstitution of the Board
- Fully Operational Board Committees
- Board Committee on Demutualization Formed

Corporate Reorganization
- Reorganization for Effectiveness and Efficiency
- Transformation Programs Underway
- Four Divisions to Better Position the Exchange as a Commercial Entity

Business Development
- Listings Sales/Retention Focus on Growing from $75B to $1T in 5 Years
- “5 Products in 5 Years” (Equities, Bonds, ETFs, Options, Financial Futures)
- National Reach via Branch Network of 13 Trading Floors and Offices

Technology
- Upgrade of Trading and Market Management System to NASDAQ OMX X-stream
- Build Business Technology Baselines and Process Automation
- Advocating Full Dematerialization

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Key Initiatives contd.

**Regulation**
- Tailored Best-in-Class Service for Issuers and Broker-Dealers
- Attention to Rules and Interpretations for Market Participants
- Surveillance Automation (Conduct, Controls, Systems, etc.) e.g., SMARTS

**Regulatory Program**
- Better Coordination with Other Regulators
- Compliance via Enforcement (Disclosures, Financial Reporting, Forecasts)
- Eradication of Insider Trading, Market Manipulation and Issuing of False Statements

**Investor Protection**
- Reconstitution of Board of Trustees of Investor Protection Fund (N597m)
- Trade Guarantee Fund
- Additional Support by the SEC’s Establishment of a Similar Fund

**Market Structure**
- Market Making and Securities Lending, and Development of a Short Selling Program
- Consideration of an Increase in the 5% Band to 10% with an Intraday Auction at the 5% Mark
- Longer Trading Day, Sponsored Access, Opening/Closing Auctions, etc.

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Restoring Investor Confidence Through New Products and Services

- **Technology infrastructure**
  - X-Net (virtual private network) for brokers
  - Development of NASDAQ OMX X-stream trading platform
  - New corporate database

- **Market data services**
  - New data policy
  - Feeds, subscriptions and reports for market participants

- **NSE Web site**
  - Access and market information for investors and all stakeholders

- **Value-added services**
  - Corporate Governance, Investor Relations, Institutional Services, Equity Research Coverage, and Corporate Access for listed companies
## Restoring the Market: Key Initiatives

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<tr>
<th>Key Initiatives</th>
<th>Term</th>
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<tr>
<td></td>
<td><strong>Short (2011)</strong></td>
<td><strong>Medium (2012)</strong></td>
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<tr>
<td><strong>Within NSE Control</strong></td>
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<tr>
<td>- Market Segmentation ✓</td>
<td>- Develop Product Liquidity and Depth</td>
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<td>- Company Share Buy-Back ✓</td>
<td>- Attract and Retain More Listings</td>
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<td>- Introduction of ETFs ✓</td>
<td>- E2E Trading Automation</td>
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<td>- Investor Clinics ✓</td>
<td>- Continued Enhancement of Regulatory Programs</td>
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<tr>
<td>- New Web Site ✓</td>
<td>- Financial Literacy Program</td>
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<tr>
<td>- Revised Listing Rules ✓</td>
<td>- IFRS Compliance</td>
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<tr>
<td>- Market Making <em>(rules approved)</em></td>
<td>- Demutualization</td>
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<td>- Securities Lending <em>(rules approved)</em></td>
<td>- Market Data Services</td>
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<td>- Short Selling <em>(rules approved)</em></td>
<td>- Advocacy</td>
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<td></td>
<td>- Financial Literacy Program</td>
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<tr>
<td><strong>Outside NSE Control</strong></td>
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<tr>
<td>- AMCON Debt Resolution</td>
<td>- Review PFA Investment Guidelines</td>
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<td>- Advocacy</td>
<td>- Tax Breaks on Transaction Fees</td>
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<td>- Policy on Large Cap Firms to Deepen Market</td>
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<td>- Access to SWF Funds</td>
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<td>- Exit Strategy for Privatized Entities</td>
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<td></td>
<td>- Reduce Focus on Dividends</td>
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<td>- Capacity of Local Institutional Investors</td>
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<td>- Broker Margin Debt Resolution</td>
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<td></td>
<td>- Broker Access to Funding</td>
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The Eagle Needs to Intervene

• Investment of Sovereign Wealth Fund In the Nigerian Capital Market – **Ministry of Finance**
• Alignment of Short Term Monetary Policy to Support Low Cost Long Term Funding of Businesses – **CBN**
• Implementation of Proper Margin Lending Facilities – **CBN**
• Broker Access to Funding - **CBN**
• Investment of Pension Funds in Equities - **PENCON**
• Targeted Tax Breaks for listed companies – **FIRS**
• Listing of National Companies in the Capital Market - **BPE**
• Nigerian Participation in Growth and Success of Multi Nationals through “minimum ownership requirement” initiative – **Ministry of Trade and Industry**
Achieving The Transformation – Critical Role of The Legislative and Executive Arms of The Government

• Developing a market that is representative of the economy
  – **Agriculture**: 40% of GDP → 0% of market cap
  – **Oil & Gas**: 16% of GDP → 5% of market cap
    *(Majority of national revenue, no upstream listed)*
  – **Power**: 8% of GDP → 0% of market cap
    *(13 companies recently created)*
  – **Telecoms**: 4.5% of GDP → 0% of market cap
    *(> 80m subscribers)*

• Advocacy for Listings
  – Passionately promoting companies and appropriate government institutions to list on the stock market through appropriate incentives

• Educating the public on the benefits of long term investment in a well run capital market

• Facilitating joined up development of capital market
  – Government, regulators and industry participants
Creating Value in a Bear Market

Asset Diversification

Valuations at Lowest Levels

Strong fundamentals in many companies

The time to invest is now!
“We simply attempt to be fearful when others are greedy and to be greedy only when others are fearful.”

Warren Buffet
Thank You

The Nigerian Stock Exchange

Stock Exchange House
2-4 Customs Street
P.O. Box 2457, Marina
Lagos Island
Lagos, Nigeria

abajomo@nigerianstockexchange.com
www.nse.com.ng