



Capital Market Literacy in Nigeria:
Issues, Challenges, and Way Forward.



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This notes distills thoughts using data and market intelligence to appraise the issues and challenges of capital market literacy in Nigeria and offer reasoned points to aid a discussion on the way forward to a fit-for-purpose market.

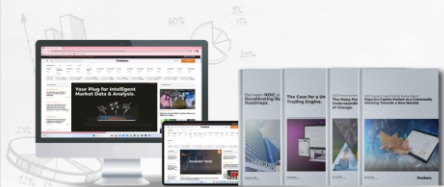
Nigeria's Capital Market Then and Now.

The Nigerian 'Capital Market' has evolved from a market of a few primary equity listings in the 1970s to 155 instruments and seven Mutual Fund categories with 143 funds and 101 federal and 9 state debt instruments listed on the NGX as of November 08, 2023. The market has grown in depth and breadth over the last five decades. While the market's growth is not in doubt, with a new historical Index high of slightly over 70,000, what has become a compelling interrogation issue is whether the market could have grown broader and deeper. If the market can do better, what needs to be done to achieve a more prominent, liquid, and flexible market should anchor ongoing conversations. For example, conversations need to be advanced around:

- Ⓟ Establishing a base literacy level around the 6 key stakeholders in the market ecosystem – Regulators,

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- Ⓟ Operators, Analysts/Financial Journalists, Corporate entities (securities), legislators/judiciary; and investors.
- Ⓟ Improving the trading experience of domestic Retail Investors (31.1% of the market in 2023), Institutional Investors (59.18% of the market) and Foreign Investors (9.51% of the market).
- Ⓟ Resolving the issues around unclaimed dividends (establishing equitable rules in favour of domestic retail investors, considering the N190bn in unclaimed dividends as of October 2023).
- Ⓟ Revisiting margin trading rules and guidelines (learning from past errors). Creating equity and debt market derivative products (to enhance market attractiveness).
- Ⓟ Addressing a growing list of companies opting out of the listed securities market (delistings).
- Ⓟ The lower number of public offers (IPOs) over the last half-decade (most new offers have been by introduction rather than public offers).
- Ⓟ Deepening and broadening market literacy by promoting and supporting investment clubs across secondary and tertiary institutions nationwide.
- Ⓟ Accelerating technology adoptions through horizontal linkages with the financial information and news service providers.

New Realities

The shifts in the retail equity market reflect both a misalignment between the broad economy and the Nigeria Exchange Limited (NGX) and a disconnect between the Nigerian economy and changing *geopolitical dislocations* and *geo-economic fragmentation*. Global wars and African coups have increased risk factors that impact investors' decision-making. Nigeria has seen the impacts of these developments in the reclassification of *Nigeria in global Indices*, a phenomenon reported by Proshare recently. In addition, the fragmentation of the world into global economic blocs has restricted investment flows and limited foreign portfolio investment (FPI) to frontier markets like Nigeria.

For the NGX, NASD and other financial markets to serve as sources of mobilising investment capital

for the country during rising global uncertainty, the Exchange must attract new listings that reflect the relative sizes of sectors in Nigeria's gross domestic product (GDP). The banking sector, for example, has a disproportionate influence over the equity market. The misalignment is reflected in the NGX All Shares Index (ASI), providing a year-to-date (YTD) return of 34.34% and the Banking Sector Index, which is 67%, or almost twice the broad market yield. The Agricultural sector is almost non-existent (0.64% of the NGX market capitalisation) despite its 21.07% contribution to nominal GDP in Q2 2023.

For the NGX to be relevant to the average Nigerian, it must align with their daily existence, but this is not the case now. Investor literacy will result from people with savings seeing the economy from the eyes of the growth (or decline) of the NGX ASI and its sub Indices. If the ASI does not reflect the economy, it would be challenging to improve literacy about the market since such knowledge would not translate into intelligent investment decisions and improvement in individual or collective investor well-being.

Finding the Missing Bridge Between Economy and Market.

Market literacy is an adjunct to economic literacy. People who would invest in the Nigerian capital market are taking a bet on the Nigerian economy. As in any bet, probabilities of economic/market outcomes depend on market/economic experience, economic intelligence, and luck. Data plays a vital role in teasing insights about market conditions and potentials. Still, suppose the economy and the capital market are not in alignment. In that case, a depressed economy (Nigeria's GDP growth has fallen from 3.52% in Q4 2022 to 2.31% in Q2 2023) may see strong market growth (the ASI has risen to a 15-year high with a YTD return of 34.34%).

Nigeria's market capitalisation to GDP ratio was about 75% as of June 2023, compared to less than 50% as of December 2021. This suggests an improvement in market size, albeit more on price appreciation of selected stocks than new entry into the market. Analysts have also argued that the growth in transactions has little impact on the

market functionality of capital formation and wealth creation.

Although the local market is rising in market cap-to-GDP ratio, it is still lower than the ratios of some developed markets such as the United States (156.66%), Canada (143.84%), Japan (124.14%), and the United Kingdom (100.2%) as of December 2022, according to Sibilis Research. Proshare Analysts note that the low market capitalization-to-GDP ratio reflects that the capital market does not represent the Nigerian economy. To build the bridge between the market and the economy, urgent steps may be required, which would include, but not limited to, the following:

- ❶ The listing of large public enterprises, such as the Nigerian National Petroleum Company Limited (NNPCL) on the NGX (the Saudi Aramco Model).
- ❷ The financialisation of idle federal assets and their listing on the NGX. The listing of idle assets would mean establishing market values for assets such as the National Stadium, Lagos, the National Arts Theatre, Lagos, the Abuja National Stadium, all Federal Airports, and even the relocation of army, customs, and police barracks and the building of securitizable real estate assets.
- ❸ Encouraging large indigenous corporate organisations to list on the NGX or NASD to take advantage of the potential (proposed) tax benefit of listing and the possible concession to local companies that meet employment cut-off metrics and export earnings targets or thresholds and,
- ❹ Making market assets more liquid by creating a derivatives market based on equities, commodities, and currencies.

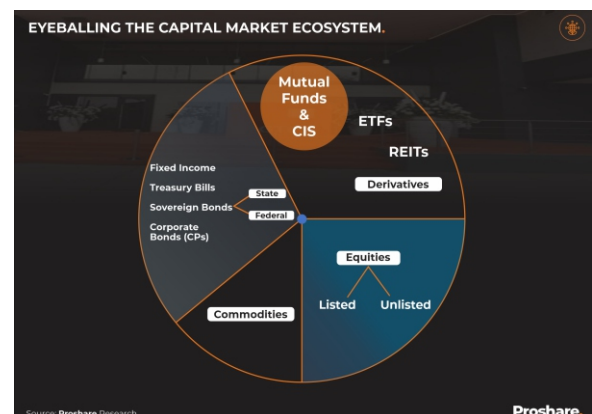
Issues and Challenges of Nigeria's Capital Market Literacy.

Capital market literacy, or understanding how financial markets and investments work, is crucial to retail investor mobilisation. The key issues include but are not limited to the following:

- ❶ The dearth of initial public offerings (IPOs) is a matter of concern to stakeholders. The prevalence of companies entering the market

by Introduction limits the free float available for regular trading and price discovery.

- ❷ The get-rich-quick-or-die-trying mindset of younger Gen-X and Gen-Z Nigerians has created a fertile landscape for Ponzi schemes and other advance fee fraud or pyramiding adventures. The lack of diverse investment opportunities in the market has created a vacuum that Ponzi schemes have exploited. As a result, young and old investors fall prey to fraudulent schemes due to the allure of quick and "guaranteed" returns.
- ❸ The market has evolved into a "caveat emptor" investment park, leaving investors to fend for themselves. The evolution of the market into a high-risk showground undermines market credibility and limits investor confidence.
- ❹ Another challenge is the lukewarm methods of engaging investors and stakeholders. The interaction process has been unfocused and clumsy. The existing channels for disseminating information and educating prospective investors are inadequate (the NGX could support school investor clubs nationwide), rather than leaving young and impressionable minds to schemes of Ponzi merchants.
- ❺ The Nigerian capital market is evolving rapidly, but the regulatory framework still struggles to keep up. This misalignment between market realities and regulatory requirements creates a lively ground for market participants' high-risk ventures and scammers' fraudulent activities.



The Road to Nigerian Financial Market Maturity.

To address the previous issues, managers of Nigeria's capital market institutions may consider the following actions:

1. Adoption of Invest-tech Platforms

The global financial market has evolved with technology, and the Nigerian capital market needs to embrace innovation fully to bridge the gap in market literacy and attract a new generation of investors. The Nigerian market may need to create platforms like America's *Robinhood*, which could make investing more accessible, user-friendly, and attractive, especially to tech-savvy millennials and Gen Z market patrons.

Platforms like Robinhood feature mobile trading apps, robo-advisors, and educational resources that simplify the investment process and provide valuable market insights and data, promoting capital market literacy among diverse users. Partnerships between market stakeholders and tech companies, fintech startups, or mobile network operators can extend the reach of these technologies to ensure that even individuals in remote areas access the capital market using their smartphones.

2. Encouraging Listing by IPOs

Another way to improve market functionality is to encourage listing through IPOs. Hitherto companies have preferred listing by way of Introduction for two reasons: (1) listing by Introduction means limited free float, and (2) listing by Introduction means avoiding the challenges and financial burden of book building, underwriting agreements, and public offerings, among others, which are associated with IPOs.

But by listing through IPOs, companies raise new capital and generate considerable market excitement and interest, particularly companies with strong fundamentals. IPOs also create room for a considerable level of free float, which is critical for market stability, as it ensures sufficient trading activity, price discovery, and overall market efficiency.

Fostering a culture of listing by IPOs requires

collaboration between market regulators, brokerage firms, and the companies of interest seeking to go public. Nigeria's Securities and Exchange Commission (SEC) must streamline the IPO approval process and incentivise companies to list on Exchanges. SEC and institutions like the CIS can put checks in place to curb the excesses of brokerage firms on commission charges and fitness-for-purpose. Brokerage firms should also provide high-level support services to companies considering IPOs, helping to meet listing requirements and navigating the complexities of going public.

3. Supporting Risk Management and Product Innovation

Key capital market operators must invest in risk management and innovative product offerings that resonate with the younger generation for the Nigerian capital market to regain its role in capital formation. Aside from the need for continuous education of investors about the fundamental principles of investing, risk management, and market dynamics, stakeholders, particularly the regulators and Associations of Stockbrokers (e.g. CIS), should, in *principle* and *practice*, guide against transactions that paint the market as random gambling stores. For instance, a high rate of insider and related parties transactions, gaining an unfair advantage or profit from the market with non-public information heightens market risks and discourages willing issuers and investors.

These efforts could be augmented with the development of new investment products that cater to the preferences of millennials and Gen Z investors, leveraging the **distributed ledger technology (DLT)** and creating tradeable assets on smartphones to attract the tech-savvy demography. Proshare analysts in a **2022 Online Trading Report**, argued that DLT could aid the current payment and settlement process's acceleration, speed, and accuracy and lead the charge toward a network of African Exchanges. Adopting innovative products and channels aligns with the evolving financial landscape and provides investment avenues that suit their fast-paced thinking.



Closing Thoughts.

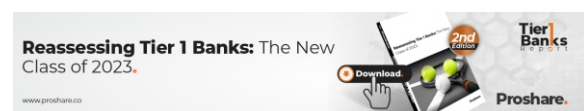
The Nigerian capital market has seen significant growth in retail investors since the banking sector's recapitalisation exercise in 2005. However, despite the growth, the number of retail investors in the country remains under 4m (active retail investors are less than 1m), indicative of the challenges associated with achieving financial inclusion in the capital market. It also indicates the gaps that need to be filled to ensure that the benefits of the capital market are accessible to a broader range of citizens who have been depending on alternative schemes.

Financial inclusion is not just about providing access; it also involves providing the **knowledge** and **tools** necessary for investors to make informed investment decisions, as retail investor participation is crucial for market growth and the development of a more inclusive financial ecosystem.

Additionally, the capital market's role as a source of funding for companies appears to be diminishing. The changing preference suggests the need for the capital market to adapt and offer more competitive and attractive opportunities for companies to raise capital. First, by streamlining market regulations through harmonising registration and listing processes and enforcing ethical standards.

Also, promoting market incentives such as proper risk management, lowering transaction costs, developing new products, and facilitating the cross-border issuance and trading of securities. In doing so, the market is better structured to serve the needs of businesses while encouraging more retail investors to participate, thus contributing to a more robust and inclusive capital market in Nigeria.

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Related News.

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3. Q1 2023 Nigerian Capital Market Service Report.
4. The Nigerian Capital Market report 2022 and 2023 Outlook.
5. Full Report: Q1 2023 Nigerian Capital Market Service Report.
6. Q3 2022 Nigerian Capital Market Service Report.
7. NGX RegCo Empowers Retail Investors with Capacity Building Workshop.
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9. NGX to Mobilize Capital for FG's Agenda.
10. NGX, CIS, ASHON to Work with MOFI on Market Development, Listings.
11. Nigeria's Ponzi Finance: The Looming Debt Crisis.
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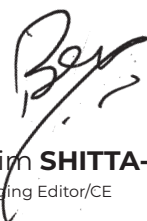
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