Graduating from a Junior Stock Market in the UK

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Author: Rhiannon Price, rhiannon.price@barclays.com

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Summary

There has been considerable commentary on the difficulties being faced by public markets in the UK as well as in other jurisdictions. The UK represented only 3.5% of the world's market capitalisation in 2023, a decline from 10% in 2000, a larger decline than observed in the EU from 18% in 2000 to 13% in 2023.[1] It is important continually to examine the entire capital market ecosystem with a view to addressing any weaknesses because of the important connection between capital market strength in the UK and overall economic growth.

"The UK needs strong public markets. Not merely because they are a way of companies funding growth and investment which in turn creates jobs and pays wages across the countries and regions of the UK. But because increasing the opportunities for investors to share in that growth helps spread wealth. Strong and deep capital markets drive the economy, spread risk, and they help people to build up their savings and plan for old age."[2]
Lord Hill, UK Listing Review, 2021

This report examines one part of the capital markets ecosystem; the transition between junior stock markets and main markets in the UK. At the moment few companies make this step, often seeing no advantage to graduating to a main market even when they have grown to considerable size. We find evidence that companies engaged in a multi-stage divestiture plan for their growth would currently be
unlikely to benefit from using a junior market as one step of enacting that plan.

If a smoother glidepath between junior and main markets were created, it could increase the attractiveness of UK capital markets, particularly for a small group of companies seeking fast, high growth. This could reduce the risk that they would otherwise choose to be admitted to public markets for the first time in another jurisdiction, at a later growth stage. While many companies will still choose to go public directly on the market that suits them and helps them achieve their preferred corporate strategy, the policy recommendations in this report could provide an incentive for a small number of companies to consider using the UK's junior stock markets as a steppingstone to a main market, thereby incentivising them to stay in the UK.

In order to be effective, this glidepath would need to be created alongside a concerted effort by the junior stock markets, supported by regulators, to evolve their profile. Junior markets should be viewed as platforms where early stage companies are supported by various policies, to access public markets easily and then eventually, at a later stage in their maturity follow a streamlined process that allows them to migrate to a main market with minimum disruption when they have reached the relevant size or revenue.

The Scale-up Institute, that advocates for the 28,410 UK scale-up companies, in their 2023 review noted the heavy use of growth capital by UK scale-ups with 5 in 10 being of the view that they do not have sufficient capital to meet their current growth trajectory.[3] This signifies an opportunity to support those companies. Easing the transition between the junior markets and main market could help provide a pipeline of younger, more diverse and innovative companies coming from junior markets, also addressing the current imbalance on main markets towards more traditional sectors. This would make the system as a whole more attractive, boosting the overall competitiveness of UK capital markets.

[1] AFME, Capital Markets in the UK, Key Performance Indicators, April 2024
[2] HM Treasury Independent Review, UK Listings Review , March 2021
[3] Scale Up Institute, ScaleUp Annual Review 2023

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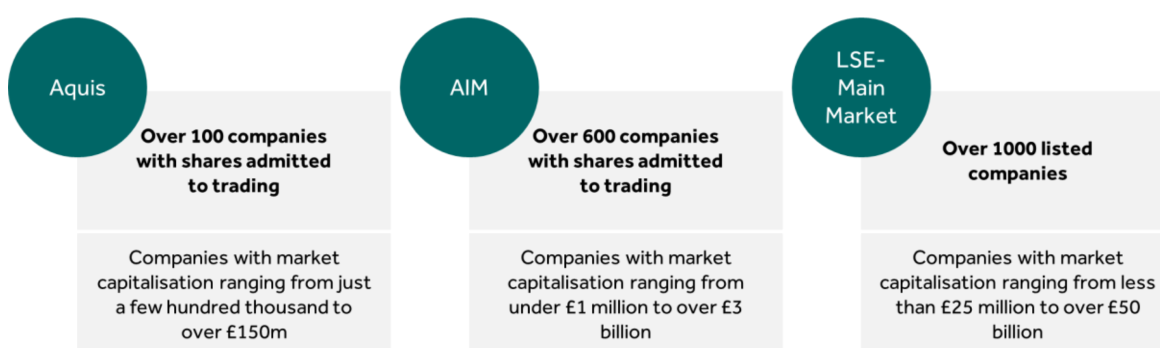
Gap analysis & research question

The political and regulatory focus on improving capital markets in the UK has, thus far, been on reforming the FCA's Listing regime. This applies to companies admitted to Recognised Investment Exchanges – for example the London Stock Exchange's Main Market. The recent reforms aim to attract companies to a main market as their first step onto the public markets. This is the most common way that a company joins a main market in the UK at the moment and, given there are 43 active unicorns, being companies with valuations over $1 billion, headquartered in the UK that are likely to seek admission directly to a senior stock market, [4] and who have the most choice over which jurisdiction to go public in, it is a natural focus for policy makers.



However, there is another entry point for companies onto a main market. In other jurisdictions, most notably Japan and Sweden,[5] it is more common for companies to graduate from a junior stock market onto their respective main markets, with the junior market having a modified regulatory environment, calibrated to be less burdensome for smaller companies but still providing adequate information to investors. Since it was established in 2006, First North Growth Market in Sweden has seen 130 transfers to the Main Market.[6] Rather than a junior market being the destination for a company it can be a brief stop off point on the journey to a listing on a senior market. In contrast, as shown in table 1 below, although historically there have been many more companies admitted to UK junior markets than to Nordic junior markets, fewer have graduated to a main market both in absolute terms and as a proportion of the total.

Table 1: Number of companies transitioning from AIM to the LSE Main Market in UK, compared to those transitioning from Nasdaq First North to Nasdaq Main Markets[7]

Year	Number of companies admitted – AIM	Number of companies admitted – Nasdaq First North	Number of graduations from AIM	Number of graduations from First North
2023	753	531	2	3
2022	816	558	4	12
2021	852	544	3	7
2020	819	404	2	12
2019	863	369	3	7

[4] Beauhurst, UK Unicorn companies, March 2024
[5] Caroline Granier, Valérie Revest, Alessandro Sapio, SMEs and Junior Stock Markets: A Comparison between European and Japanese Markets, 2019, Journal of Innovation Economics & Management 2019/2 (n° 29)
[6] Nasdaq celebrates 130 switches from First North Growth Market to Nordic Main Markets, 2023
[7] London Stock Exchange, AIM factsheet, April 2024, Nasdaq Annual Trading Statistics 2019, 2020, 2021, 2022, 2023

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In 2021 AIM was responsible for 53% of all funds raised on European junior stock markets,[8] however it has been facing competition for this title from First North in Sweden more recently.[9] As with the LSE's Main Market, the number of companies admitted to junior markets in the UK has fallen in recent years. At the end of 2023 there were 859 companies admitted to UK junior markets in contrast to 1,087 a decade earlier, a decrease of just over 25%.[10]

While the two junior markets in the UK, AIM and Aquis Growth Market , serve many functions for companies and investors, and have been copied by other jurisdictions worldwide, very few companies have used the junior markets as a steppingstone to a main market. In some years the reverse has been true, with more companies moving to a junior market from a main market than the other way around. Typically, private equity houses looking to exit an investment via the UK public markets will look to a main market to list, likely due to the size of the assets involved, whilst the junior markets are more seen as a place for companies that are seeking to raise cash quickly, and which wish to take advantage of the lighter regulatory and less costly regime. Rather than graduating on to a main market once they have reached significant size, companies tend to stay on the junior market.

Graduations from junior stock markets

It is not necessarily a problem for companies to stay on a junior stock market and never graduate onto a main market. However, graduation can represent an additional strategic option for entrepreneurs that wish to enact a multi-stage divestiture strategy.[11] For example, a founder-led company may be admitted to a junior market when it is seeking additional capital for a growth stage such as financing for early-stage research following a proof of concept. However, once it has matured and reached the stage of a proven product with a predictable revenue stream, early-stage investors may want to exit, to be replaced by an institutional investor base looking for a more stable pattern of returns.

There is not a lot of academic work studying companies that do graduate from a junior market to a main market, likely due to the low number of graduations on the most prominent junior markets. However, one study of companies graduating from the junior to senior markets in Japan concluded that "ultimately graduates to the Tokyo Stock Exchange (TSE) main markets exhibit better performance…. Our findings suggest that IPO firms should aim higher—specifically, they should quickly seek to climb to main stock markets—to raise their performance."[12]

The absence of a significant number of companies graduating from junior markets to a main market suggests that moving may be being inhibited in the UK in some way. Alternatively, it may be that companies see no need to graduate from the junior market if their needs are being met sufficiently on the junior market.

Barclays' experience in this area is as an advisor to companies when they seek admission to the LSE's Main Market, either as they go public for the first time or when they graduate from a junior market. It is for this reason that we have primarily focussed on this inflexion point in the capital markets ecosystem.

[8] Hacker Young, UK AIM dominated European junior markets in 2021 but is its lead unassailable?, Mar 2022, Junior Accountants
[9] First North Growth Market
[10] LSEG AIM factsheet link and AQSE Market statistics and Trading data link
[11] Caroline Granier, Valérie Revest, Alessandro Sapio, SMEs and Junior Stock Markets: A Comparison between European and Japanese Markets, 2019, Journal of Innovation Economics & Management 2019/2 (n° 29)
[12] Honjo, Y., Kurihara, K. Graduation of initial public offering firms from junior stock markets: evidence from the Tokyo Stock Exchange. February 2023, Small Bus Econ 60, 813–841 (2023)

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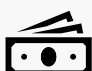
***Research question*: Are junior markets in the UK working effectively, or are there any ways in which companies and/or investors could be better served by graduating onto a main market?**

Box 1: What does a stock exchange do?

5 Core functions of Stock Exchanges[13]

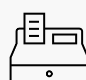


Cash: a source of corporate finance through new share issuance, at IPO or subsequently in a follow-on issue, and the distribution of corporate cash to shareholders in the form of dividends and repurchases.

Creation: the ability of the stock market to encourage the flow of financial resources into new firm formation by providing a promise of liquidity at a later point in time. **Specific to junior markets, one way this creation function is carried out is when companies graduate to a main market, representing a multi-stage divestiture strategy for entrepreneurs.**[14]

Control: affects the relationship between the ownership of shares of the company and managerial control over the allocation of resources.

Combination: A stock market listing makes the company's shares a currency that can be used as payment, partially or wholly, for another company's shares in mergers and acquisitions (M&A).



Compensation: A stock market listing makes the company's shares a currency that can be issued to employees as a form of remuneration, with stock options and stock awards as prime examples.

Its normal for stock markets to perform these five functions in different ways, and regulation can act to limit or maximise a particular function that is deemed more important for various reasons. For example, allowing public companies to have dual-class share structures would limit the control function, potentially giving managers or founders continued control over allocation of resources even though the company now has public shareholders. A market or regulator may be willing to accept this because they see wider economic benefits. An example of this is the recent changes to the UK Listing Rules to allow dual-class share structures under certain conditions. These were motivated by a wish to "bolster the accessibility of our listed markets to innovative technology companies….and broaden the listed investment landscape for both institutional and retail investors in the UK".[15]

[13] William Lazonick, The Functions of the Stock Market and the Fallacies of Shareholder Value, June 2017, Working Paper no.58 Institute for New Economic Thinking, June 2017

[14] Caroline Granier, Valérie Revest, Alessandro Sapio, SMEs and Junior Stock Markets: A Comparison between European and Japanese Markets, 2019, Journal of Innovation Economics & Management 2019/2 (n° 29)

[15] FCA CP21/21 Primary Markets Effectiveness Review July 2021

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Box 2: What is a junior stock market and how does it differ from a main market?

Junior stock markets can be characterized by simplified listing processes and customised information standards in comparison with the rules in force on the senior markets.[16] They are intended to suit the needs of smaller companies, that would struggle to meet the requirements on the senior market.

In contrast to the London Stock Exchange (LSE), whose history goes back more than 300 years,[17] the two junior markets in London were founded more recently. The Alternative Investment Market (AIM) was established by LSE in 1995 – although some trace its genesis back to the report of the Macmillan Committee in 1931.[18] More recently, Aquis Exchange, which operates both a main market and a junior market,[19] began with the establishment of Plus Markets in 2007.[20]

Both AIM and Aquis Growth Market are regulated by the FCA as Multilateral Trading Facilities (MTFs) and then registered as SME Growth Markets. They are subject to bespoke regulatory requirements tailored to meet the needs of smaller companies. For example, in contrast to a main market, under most circumstances no FCA approved prospectus is required at admission, and the FCA does not approve each admission. Importantly the FCA Listing Rules do not apply to these unlisted public markets. However, rules governing conduct and market abuse are broadly the same although primarily monitored by the market operator rather than the FCA.[21] There is also an enhanced role for advisers, known as Nominated Advisers (NOMADs) and Corporate Advisers in assessing the suitability of companies for admission to the market.[22,23]

A number of tax incentives apply to what are referred to as 'unquoted' or 'unlisted' markets. Most importantly transactions are exempt from the Stamp Duty Reserve Tax levelled at 0.5% on the purchase of shares on senior markets. However there are also specific alleviations in the following areas:[24]

- Enterprise Investment Scheme (EIS)
- Venture Capital Trusts (VCTs)
- The Seed Enterprise Investment Scheme (SEIS)
- Capital Gains Tax – Gift Relief/Business Asset Disposal Relief
- Inheritance Tax – Business Property Relief
- Investors Relief

[16] Caroline Granier, Valérie Revest, Alessandro Sapio, SMEs and Junior Stock Markets: A Comparison between European and Japanese Markets, 2019, Journal of Innovation Economics & Management 2019/2 (n° 29)
[17] London Stock Exchange Group, The history of LSEG
[18] Sridhar Arcot, Julia Black and Geoffrey Owen, From local to global: The rise of AIM as a stock market for growing companies, September 2007, London School of Economics
[19] Aquis acquires NEX Exchange, press release, July 2019
[20] FCA register
[21] FCA handbook MAR 5.10 Operation of an SME growth market
[22] AIM NOMAD link
[23] Aquis Corporate Advisers link
[24] Aquis, Investing in Aquis Stock Exchange Growth Market: A tax guide, 2023 and London Stock Exchange Group, LSEG A guide to AIM tax benefits, 2015

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Methodology

In order to consider how companies are being served on the junior markets we took a sample of 20 of the largest companies admitted to a junior stock market and found a comparator company admitted to a main market for each.[25]

In order to provide a good basis for comparison:

- We focussed on companies on the junior market that would likely be eligible for admission to a main market.
- We looked for main market comparators of a similar size market capitalisation, in a similar industry to each junior market company.
- Where a reasonable comparator could not be found, we excluded the company from the sample.

This resulted in 15 companies being used to make comparisons.

We then established a number of metrics to compare each pair against one another with a conscious focus on metrics that measure how easily a shareholder would be able to exit:

1. **Liquidity**: on UK markets as well as across all EU markets, measured by both volume and value over 3 month periods, then compared using the percentage difference between the liquidity level on the two markets.
2. **Volatility**: measured via the percentage move on a daily basis over 90 days, then compared in absolute terms.
3. **Shareholder make-up**: proportion of shareholders across different investment styles- index, yield and growth.
4. **Number of Investment Research analysts** covering the company
5. **Capital raised:** both at IPO and post-admission in primary follow-ons (a direct sale of a company's shares from the company that are newly issued), considering number of times capital was raised as well as value, and how much was raised per year admitted to the market.
6. **Secondary market offers** (a public resale of existing shares from current shareholders) – by number, aggregate value, average size as a percentage of market capitalisation and aggregate size as a percentage of market capitalisation.

The data was compiled using Bloomberg, FactSet, Dealogic as of the 17th April 2024.

[25] Companies admitted to the Aquis Growth Market tend to be considerably smaller than those admitted to AIM and therefore very few would be eligible for a main market. There are also only a very small number of companies admitted to the Aquis Main Market. For this reason our analysis focussed on companies admitted to AIM and the LSE Main Market.

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Results

As one would expect from a broad sample of public companies there was considerable variation in the observed behaviour of the comparator pairs. Although no company admitted to a junior market was superior on all metrics to its senior market comparator, six performed worse on over half of the indicators.

Table 2: Results of comparison of junior market companies with main market comparators

The below heat map shows the comparison of an individual company admitted to a junior market with a main market comparator company. Red signifies where the result of the comparison showed that the junior market company was worse off than its main market comparator, yellow where the results were similar, green where the junior market company was better off. For example, a junior market company that had higher volatility than its main market comparator would register red.

No of Analysts Covering	Index investors	Liquidity metric (3M ADTVolume) (% difference)	Liquidity metric (3M ADTVolume EU) (% difference)	Liquidity metric (3M ADTValue) (% difference)	Liquidity metric (3M EU ADTValue) (% difference)	Volatility metric (90d) (%)	IPO Value (£m)	No of Primary Follow-ons	Aggregate Value of Primary Follow-ons (£m)	Total capital raised (£m)	Total capital raised per year admitted (£m)	# of Secondary Market officers

Most significantly, over half of the companies included in the comparison had raised more capital in absolute terms on the junior market than their comparator on the main market, although primarily at IPO. Interestingly the most similarity across the metrics was in primary follow-on capital raises where 5 of the comparator pairs had conducted both a similar number and size of follow-on capital raises. This suggests that capital raising, or the 'cash' function of stock markets as described in Box 1, is being performed adequately on the junior market, where companies seek to use it for this purpose.

We expected to find higher volatility and less liquidity across the junior market companies. However, the results show a much more mixed picture, suggesting both may be more related to the small market capitalisation of the companies chosen regardless of market admitted to.

There were three areas where we did find that the junior market comparators would have been better served on a main market:

- Investment Research Analyst coverage
- Shareholder make-up: proportion of index investors
- Number of secondary market offers

The difference in **Investment Research analyst coverage** was in line with our expectations, and that of other academic work, that an increase in analyst coverage can be expected for companies that graduate to a main

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market. This is thought to reduce information asymmetries and can result in an improved market in a companies' shares.[26]

The indicator where it was most clear that all except 3 junior market companies were significantly worse off on the junior market was in the **investor base.** 12 of the main market companies had significantly more index investors as a proportion of their investor base when compared to their junior market counterparts. The difference was significant in each case, ranging from 6.2 percentage points at its narrowest (junior company 4.2%, main market comparator 10.4%) to 11.5 percentage points at its widest (junior company 3.2%, main market comparator 14.7%). On average the difference was 9 percentage points.

Of particular interest was a junior market company that outpaced its main market comparator on almost all of our metrics and yet nevertheless still only had just 3.6% of its investor base consisting of index investors in contrast to its comparator that had 15%. **This is a strong indicator that there is an investor base on the main market that is not available to a similar company admitted to a junior market.** Although there are index investors on junior markets they are much more significant on the main market. While this is to be expected for companies in the most well-known indices for the largest companies on the main market, it is notable when considering the companies we have used as comparators as they are of much smaller market capitalisation.

A **secondary market offer** happens when a large shareholder is seeking to exit their position in the company. It typically involves an overnight placement of shares with institutional investors following an accelerated book build. There are various ways this can be structured, for example, where the seller takes full market risk or it can be underwritten, where a bank takes on some or all of the market risk.

If this were actively happening on the junior market this would be an indicator that investors were able to exit positions effectively (referred to as the incentive for the creation function as described in box 1). It would suggest that there was no need for this function to be fulfilled by graduating onto a main market. For this reason, we looked in more detail beyond the number of secondary market offers that were occurring to establish both the average size of secondary market offers as a percentage of market capitalisation and the aggregate of all secondary market offers as a percentage of market capitalisation. This shows the extent to which a company has changed hands since admission to the relevant market.

Table 3: Examination of secondary market offers

# of Secondary Market offers	Aggregate Value of Secondary Market Offers (£m)	Average Secondary Market Offers as a % of Market Cap	Agg. Secondary Markets offers as a % of Market Cap

[26] Omaima A.G. Hassan and Frank S. Skinner, Analyst Coverage, Financial Reporting Credibility, Investor Base and Listing Location, June 2014, Economic and Finance Working Paper series, Working paper No 14-11

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Our comparator pairs show that over half of junior market companies had carried out fewer secondary market offers and the average value of those offers as a percentage of market capitalisation and in aggregate was often significantly less than that of their main market comparator.

Of these, the three junior market companies that had the most significant differences with their main market comparator in terms of secondary market offers had been admitted to the market for significantly longer than their main market comparator suggesting duration of time on the market (and therefore number of times there would be an opportunity for investors to sell shares) was not a contributing factor to the difference.

Table 4: Secondary market offers and time since admission

Difference in time since admission (years)	# of Secondary Market offers	Aggregate Value of Secondary Market Offers (£m)	Average Secondary Market Offers as a % of Market Cap	Agg. Secondary Markets offers as a % of Market Cap
10				
30				
26				

It is worth noting the types of profile of companies that are currently admitted to junior markets to provide further context to the lack of secondary market offers. Many do so for the express purpose of raising significant amounts of capital, therefore dilution of early shareholders positions can happen via this process rather than just via secondary market offers. Others are founder-led rather than backed by private equity who typically stay invested for a longer period than private equity backed companies that are more common on main markets.

Key Takeaways

There are always going to be considerable differences between companies based on their corporate strategies and individual circumstances, and we note the limitations of only looking at a small subset of companies admitted to junior markets.

However, while we have found that junior markets are serving companies as well main markets in terms of capital raising, and provide comparable trading conditions in terms of liquidity and volatility, we have found evidence that there are areas where junior markets in the UK are not serving companies effectively and they could potentially be better off on these metrics if they graduated onto a main market.

- The lower number and value as a percentage of market capitalisation of secondary market offers shows that investors are not exiting large positions post-IPO, while admitted to the junior market.
- The lower proportion of index investors in junior market companies shows that their investor base is not changing/maturing significantly while admitted to the junior market.

This suggests that were an easier path created between the junior markets and main markets it could improve the attractiveness of the UK's junior markets for some companies that are not currently public but could be if the UK's capital markets were more conducive to operating a multi-stage divestiture strategy. This could be twinned with incentives for these companies to stay in the UK as they grow, creating a pipeline of companies who would join the UK's main markets in due course.

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Policy recommendations

Vibrant capital markets are necessary to support a growing economy. The reduction in the number of companies admitted to UK capital markets over the past 10 years means we need to examine every element of the market ecosystem to understand where additional levers can be pulled. Rather than just looking at barriers to companies coming to the market in a traditional way, we should also look at ways of encouraging more companies with different growth strategies and corporate plans, and consider how the UK's markets can be expanded to include them. While there is no silver bullet to improving UK capital markets, the recommendations that follow could help increase the attractiveness of UK markets for a particular type of fast-growing company.

If these companies can be attracted to accessing public markets via the junior markets in the UK, the transition between a junior market and the senior market will be an important moment in their life cycle. Policy incentives could be introduced at that point that biases them towards graduating to a UK main market over one in another jurisdiction. Thriving UK junior markets with a good reputation as well as reduced regulatory requirements that act as a conduit to a senior market could then encourage more companies to use them as a steppingstone to the senior market rather than considering a main market listing (which may not be in the UK) as their first foray into the public markets.

We set out to explore whether junior markets in the UK were working effectively, or whether there were any specific ways in which companies and/or investors would be better served by graduating onto a main market.

Our findings show that there are two specific areas where junior markets in the UK are not working effectively:

- The lower number and value as a percentage of market capitalisation of secondary market offers shows that investors are not exiting large positions post-IPO, while admitted to the junior market.
- The lower proportion of index investors in junior market companies shows that their investor base is not changing/maturing significantly while admitted to the junior market.

The recent reforms to the UK Listing Rules, moving to a disclosure-based approach, have, to some extent, removed the hard requirements that acted as a barrier for some companies moving from a junior market to a senior market.[27] These have the potential to significantly tip the balance when companies are considering whether moving to a main market is of benefit for them. However, more could be done to make a positive glidepath that is more accessible and clear for companies that are not currently public. Alongside improving the profile and reputation of the UK's junior markets, the Government and FCA should:

- Make it easier for companies to transition from a junior market to a senior market, creating a clear road map that can be planned for over multiple years. (Recommendation 1,2 and 3)
- Improve the profile of junior markets in the UK, by ensuing a suitably calibrated approach to the regulation of junior markets, aimed at meeting the needs of smaller companies seeking to grow. (Recommendation 4 and 5)

[27] FCA CP23/10: Primary Markets Effectiveness Review – Feedback to DP22/2 and proposed equity listing rule reforms, March 2023

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Policy recommendation 1: Remove the requirement for a prospectus for admission to a UK regulated market for companies that have been admitted to a junior market for 18 months.

Currently, admission to a junior market requires an admission document in line with the junior market's rulebook rather than a FCA approved prospectus that follows requirements set out in legislation. This acts like a prospectus, ensuring that there is sufficient publicly available information to enable users to form investment judgements.[28] However, there is an EU-inherited requirement that means that all admissions to a Regulated Market, i.e. a main market, have to have a prospectus drawn up. There are no exceptions for companies that have already been admitted to a junior market.

When considering all of the steps involved in a long-term plan for growing a company, duplication during that process, particularly of an expensive step that involves multiple external experts and legal advice, is something that logically, a company would seek to reduce. Estimates for the cost of producing a prospectus vary, however in the government's impact assessment of the Public Offers and Admissions to Trading Regulations, that replace the EU Prospectus Regulation, they cited the results of a survey by the Centre for Strategy and Evaluation Services that put the cost of an equity prospectus at, on average, €912,000.[29]

The government is currently reforming the prospectus regime alongside the FCA who will be responsible for writing more detailed rules.[30] Under the revised rules, a company seeking admission to a junior market will still have to prepare an admission document following the market's rules rather than those set by the regulator however the government has clarified that it will be covered by the same level of liability as a prospectus approved by the FCA.[31] Following admission to a junior market, the company must publish annual accounts as well an annual report. In an 18 month period they will have done this at least once. Beyond this, they will have been subject to the Market Abuse regime meaning they will have been required to disclose information to the market on an ongoing basis subject to very similar conditions to those on a main market.

The requirement to produce an FCA-approved prospectus after having already followed all these provisions therefore seems like an unnecessary and expensive barrier to a company seeking a multi-stage divestiture strategy and would have limited value to new shareholders as relevant information would already be available. It would however, require a clear role for a sponsor in ensuring that this relevant information is available. Noting the different role that a Nomad/Corporate Adviser performs for companies admitted to junior markets, the requirement for a sponsor on admission to a main market would be important to retain.

Further, as admission to an overseas main market from a junior market would be subject to the filing obligations of that jurisdiction, in some cases involving re-statement of accounts for local accounting rules etc. removing this requirement for admission to a UK Regulated Market may encourage any companies admitted to a UK junior market in the future to remain in the UK as they grow.

Consideration should also be given to whether the same alleviation could be granted to companies that have been admitted to non-UK junior markets where the regulatory regime governing them is similar to the UK, for example the 20 markets in the EU that have been granted SME Growth market status. This would be in keeping

[28] FCA Handbook, REC 2.16A Operation of a Multilateral trading facility or an organised trading facility Paragraph 9D – Specific requirements for multilateral trading facilities disclosures
[29] HM Treasury, The Public Offers and Admissions to Trading Regulations 2024, Impact Assessment, July 2023
[30] FCA CP24/12 Consultation on the new Public Offers and Admissions to Trading Regulations regime (POATRs), Jul 2024
[31] Change introduced by the Public Offers and Admissions to Trading Regulations 2024, due for implementation when the FCA makes the underlying rules- expected first half of 2025

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with the principle of having open and international accessible UK capital markets to overseas companies as well as those based in the UK.

The substantive changes that are being made under the Public Offers and Admissions to Trading Regulations mean it is not currently possible to conduct detailed analysis of the difference between junior market admission documents and prospectus requirements. Both are likely to change in the near future. When these changes are being made, in order for this recommendation to be effected, it will be important to ensure that divergences between the content requirements for junior market admission documents and prospectuses are fully considered to ensure they would not create an unnecessary barrier to this recommendation being enacted.

Policy recommendation 2: Sustain the tax incentives currently provided in relation to 'unquoted' or 'unlisted' companies (Enterprise Investment Schemes, Venture Capital Trusts, Inheritance tax and Capital Gains) when they graduate from a junior market to a senior market for a limited period of time.

Tax policy is a strong tool for influencing companies' decision-making. The alleviations from Inheritance tax and Capital Gains tax are seen as particularly powerful in relation to founder-led companies. While we do not have direct experience dealing with smaller companies on admission to junior markets, we do see the import placed on these types of provisions with larger founder-led companies.

Use of the Enterprise Investment Scheme and Venture Capital Trust tax incentives to support small and growing businesses is contingent upon companies planning multi-year investment and capital raising strategies in order to ensure eligibility. Changes were introduced in 2014, 2015 and 2018 to ensure they were focussed on investment in early-stage companies that have the intention to grow and develop in the longer term.[32] At the moment, these schemes cease to apply even if all other conditions are met if a company graduates to a main market giving up their 'unquoted' status.

This means companies that are undertaking the planning involved in maintaining this status would not be considering graduation to a main market as it would represent a cliff edge, where they could lose what might be a significant part of their investor base. If for example, the Enterprise Investment Scheme relief were maintained, graduation to a main market could theoretically form a larger part of a company's growth strategy. A share offer, in line with the Enterprise Investment Scheme, made at the same time as admission to a main market could be a significant event for the company.

Beyond this, in keeping with the results presented above, retaining use of the tax incentives for investing in companies that have previously been admitted to a junior market would allow those companies to retain these investors from the junior market while smoothing the path to a different investor base that comes with admission to the Main Market. As these incentives would only be granted to companies graduating to a UK senior market, this could encourage a company towards admission to a senior market in the UK over another jurisdiction.

It would be important to ensure a taper to the various tax reliefs was introduced, so they expire a reasonable time period after the company has been admitted to a main market. This is already inherent to how the EIS and VCT schemes run in that they are time-limited related to the age of the company. In this way the policy intention of providing a boost to UK capital markets would be achieved and the cliff edge of joining a main market would be removed, but any perceived advantage to having joined a main market from a junior market would only be sustained for a short period of time. While this would run the risk of further complicating the set of tax reliefs

[32] HMRC, Enterprise Investment Scheme, Seed Enterprise Investment Scheme and Social Investment Tax Relief statistics: 2024, May 2024

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for fast growing companies, they are already complex to navigate so this may not add meaningfully to the burden for a company to understand.

Policy recommendation 3: Review the application of Stamp Duty Reserve Tax for all transactions in shares of companies taking into account the evidence from junior markets

The 0.5% transaction tax levied on a wide range of share purchases known as Stamp Duty has not been charged on transactions in shares on the junior markets since 2014. Announced in the 2013 budget, it was abolished to "help boost investor participation in equity growth markets and improve the conditions for growing companies raising equity financing."[33]

Smaller companies on both junior markets and main markets often struggle with liquidity, and this note shows evidence of the similarities in liquidity profile of smaller companies regardless of market. Considering the effects that removing stamp duty has had on liquidity and investor demand for junior market stocks could provide insight into the positive effect that could be had if it were removed from transactions on main markets.

This would be in keeping with the objective of improving the attractiveness of UK capital markets more broadly. Recent independent modelling by the Oxera consultancy for the Centre for Policy Studies shows that abolishing stamp duty on shares could be expected to lead to a permanent increase in GDP of between 0.2% and 0.7% in the long run, alongside an increase in the annual business investment of FTSE All Share index companies of up to £6.8 billion.[34]

Policy recommendation 4: When putting EU-inherited files through the Smarter Regulatory Framework, active attention should be paid to whether specific alleviations could be included to support the needs of UK junior markets.

The profile of the UK's junior markets is partly dependent on investors' perceptions of how they are regulated. While this report has sought to provide evidence to support one specific area where junior markets could be improved, it also shows the merit of taking a closer look at the broader regulatory framework regarding junior markets to see where it may not be serving the needs of new economy, growing companies and can be improved.

The EU Markets In Financial Instruments Directive (MiFID II) first introduced the regulatory concept of an SME Growth market in 2014.[35] Itself, a subject of political wrangling between Member States, using it in other legislation has also proven controversial at an EU-level due to different experience and philosophies around the purpose of capital markets. At the EU-level there are therefore limited specificities allowed for SME Growth markets.

As the UK government and regulators are going through the process of replacing retained EU law with rules set by financial services regulators they should consider where there is opportunity to tailor the new rules for the way junior markets operate in the UK. Whilst investors will continue to value high quality financial information and reporting from companies no matter which market they are admitted to, targeted calibrations could be introduced to the regulatory regime that would enhance the profile of UK junior markets for new economy, high growth companies. While these changes may not result in large differences between main markets and junior markets they could be carefully tailored to suit the needs of the UK with its high number of unicorn companies

[33] HMRC Abolition of stamp duty and stamp duty reserve tax on growth market shares , 2014
[34] Stamp duty on shares is 'a tax on growth', new CPS modelling shows, March 2024
[35] Article 33 SME Growth Markets, Markets in Financial Instruments Directive (MiFID II)

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as well as sophisticated institutional investor base in a way that was not possible to agree across the EU previously.

This has already begun under the Public Offers and Admissions to Trading Regime that will replace the EU Prospectus Regulation where HM Treasury and the FCA are developing a specific regime for operators of Primary MTFs, the most prominent of which are which are the two junior markets.[36]

Box 3: Summary of policy interventions recommended to the European Securities and Markets Authority in response to their Consultation Paper on the functioning of the regime for SME Growth Markets under the Markets in Financial Instruments Directive and on the amendments to the Market Abuse Regulation for the promotion of the use of SME Growth Markets.[37]

- Alleviations from the market abuse regime:
  - Removal or simplification of the documentation requirements related to the delay of public disclosure of inside information
- Timing around disclosure of inside information when markets are not open
  - Simplification of insider lists
- Considering the appropriateness of the tick size regime under MiFID
- Tailoring of non-financial disclosure requirements to reduce burden

Policy recommendation 5: The FCA should provide guidance and supervisory support to junior market operators so that they are able to use the discretion granted them under the new Public Offers and Admissions to Trading regime. Further the FCA should articulate publicly, to the extent possible, why the use of this discretion is in line with the FCA's objective to protect and enhance the integrity of the UK financial system.

The Public Offers and Admissions to Trading Regime, due for implementation in 2025 is premised upon Primary MTFs, including junior markets, setting the content requirements for admission documents and specifying when such documents would be required, for example, for further issues of shares. This gives them considerable discretion to tailor market rules to the needs of junior markets where these are required. This could go beyond existing discretion currently used. For example, given many companies seek admission to junior markets specifically to conduct multiple capital raises attention could be paid to the process surrounding this to enhance efficiency for companies while still ensuing investors have enough information to make informed investment decisions. In isolation, alleviations such as these this could be interpreted by investors as lowering standards on junior markets, affecting market confidence. The FCA will have the ability to either hinder or help the market operators in this regard via their rule making and the supervisory role they have over the junior market operators.

The way this discretion and any alleviations made are approved by regulators and communicated to the market will provide the backdrop to how companies and investors perceive junior stock markets. Both the regulators and the junior market operators will need to be clear in explaining where differences are made that these are for specific purposes and will still ensure that the integrity of junior markets will be maintained. They may not be hugely different to those that apply to the main markets.

The FCA used this approach during the pandemic when they announced temporary relief for companies delaying publication of audited accounts, publishing a joint statement with the FRC and PRA encouraging investors,

[36] FCA, Engagement Paper 6: Primary Multilateral trading facilities, July 2023
[37] ESMA, CP on the functioning of the regime for SME Growth Markets under the Markets in Financial Instruments Directive and on the amendments to the Market Abuse Regulation for the promotion of the use of SME Growth Markets, open 6 May 2020 to 15 July 2020 (responses included)

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lenders and other users of financial statements to take into account the exceptional circumstances of covid should companies use the relief granted.[38] The FCA should make clear the ways in which they supervise junior markets and if there are specific alleviations be open about how they have worked with market operators to mitigate any concerns they may have had with regards to market integrity in the process.

Improving the profile of junior markets will require a careful approach to ensuring alleviations for fast growing companies are balanced by the need to ensure investors have enough information to make informed investment decisions. The FCA can help in how it communicates its decisions in this regard to the market. An approach based on encouraging innovation and allowing markets to consider new ways of operating that support new business models will require a collaborative approach between the market operators and regulators.

[38] FCA, Joint statement by the FCA, FRC and PRA, March 2020

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