Regional Stock Exchanges – A Viable Option for Wales and Other UK Regions?

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1. Introduction

Policy debates regarding the existence of regional equity and funding gaps across the UK are now well and truly rooted within economic development circles. Encouragingly, both the UK government and the National Assembly for Wales have reacted positively to these claims with the introduction of regional venture capital funds across England and *Finance Wales*, which operates the enterprise development fund for Wales. However, despite these positive steps towards plugging the regional equity gap, we contend that it must now seriously address the issue of regional stock exchanges, particularly as they would naturally complement the work of the regional venture capital funds.

It is our argument that both national and regional governments should undertake detailed feasibility work to scope the potential for establishing a series of regional stock exchanges and markets throughout the UK. The primary objective would be to introduce companies to equity stake models of investment – which are embedded in the region – and to promote to indigenous firms the financial and regulatory procedures and structures associated with such financing modes: in other words, providing a regional market for investing in local businesses, as well as creating the stepping-stones towards possible membership of a large exchange such as London. This article provides an initial contribution towards the feasibility work we are recommending.

Although we are continuing to witness the devolution of certain political powers to the more excluded areas of the UK, an equitable UK economy can only be generated through the decentralisation of the nation's financial and business assets. At present, the majority of these assets – and, therefore, the decision-making processes determining their future – reside in London and the South East, leaving large tracts of the UK as the low value-added servicing grounds of these assets. If knowledge exchange, transfer and interaction occur most naturally and effectively between actors that are relatively proximate in geographic terms, then it follows that the finance required to commercially exploit these activities should also ideally be made available through geographically consistent channels. Furthermore, as policies relating to regional entrepreneurship development take root within their respective economies, issues regarding the mobilisation of financial resources through equity investment will become increasingly pertinent.

We consider that the introduction of regional stock exchanges in the UK could play a key role in:

- ‘Championing’ smaller firms indigenous to the region;
- Providing an on-going support mechanism, and ensuring value for both businesses and investors;
- Working predominately with the indigenous banking and brokerage sectors, enhancing the financial and business service sector capabilities of the region;
- Encouraging the local ownership of equity;
- Seeking to develop linkages and networks between the companies listed on the regional exchanges;
- Facilitating a greater degree of flexibility in terms of developing future growth and investment routes, based primarily on long-term planning as opposed to short-term gainism;
- And most importantly, make a significant long-term contribution to the economic growth of both the regions they are situated in and the UK as a whole.

2. Regional Stock Exchanges in the UK - Back to the Future?

The notion of stock exchanges operating at the regional level within the UK might sound a wild notion within an age of corporate consolidation, mergers and acquisition. However, within the arena of economic development policy, where intervention has become increasingly focused on regional sector cluster building and the creation of localised centres of knowledge-based activities, it is a concept which would appear to be an almost logical progression of this current policy evolution. Indeed, as economic development policies have looked back to future, in terms of recreating the environment and conditions of the industrial districts described in the UK by Alfred Marshall around the turn of the twentieth century, it is clear that regional stock exchanges were a key part of these conditions. By 1914 there existed 22 regional exchanges across the UK, including exchanges in Bristol, Cardiff, Halifax, Liverpool, Sheffield and Swansea. It may surprise many to learn that a number of these exchanges continued to be operational until as late at the 1970s.

The evolution of these regional exchanges was based on the requirements for secondary market functions and operations not performed adequately by the central market at the London Stock Exchange (LSE), in particular plugging the gap between the official LSE list of stocks and the non regulated informal exchange markets. In other words, the regional exchanges also performed the function of providing the business networks between local individuals and exchanges as well as those associated with the main exchange in London. This networked structure benefited both London and regional traders and investors, and became influential with the regional exchanges offering a portal of information and wider access for London investors seeking to diversify their portfolio. Therefore, the relationship between the LSE and regional exchanges was clearly one of complementarity rather than competition. However, by the 1970s the changing industrial regional order across the UK – leading to the economic divides we see today – deemed a situation where the remaining regional exchanges were absorbed into the international LSE in 1973. Understandable as this decision may have been at the time, the (re-)generation of stock exchanges at key regional points across the UK could act as key nodes and facilitators of the knowledge-based economic development sought today. The demise of regional stock exchanges was tied to the ever increasing centralisation of government in London. Now there is an opportunity to entwine political devolution with financial innovation.

Regional stock exchanges might be a 'back to the future' policy scenario in the UK, but this is not the case in many other countries where such exchanges have become embedded in their economies. For instance, although the New York Stock Exchange (NYSE) is the most prominent exchange in the United States, there are also five vibrant and growing regional exchanges in Boston, Chicago, Cincinnati, Philadelphia and San Francisco. These exchanges trade companies located within their region, alongside some of the largest US and multinational companies. The five regional exchanges, along with the NYSE and American stock exchange, work under the umbrella of the National Market System, which was formed in 1975 in order to promote competition and ensure that investors get the best price available regardless of where their order is executed. Since this period the status and importance of the regional exchanges has continued to increase. For example, over the last ten years the trading volume of the Boston Stock Exchange has increased more than tenfold. In general, regional stock exchanges in the US have carved a niche by handling small orders quickly and efficiently, maintaining low transaction costs and fees.

A similar system operates in Canada, where alongside the primary market in Toronto there exists a regional venture exchange operated through Alberta, Vancouver, Winnipeg and a major regional exchange in Montreal. Also, in Japan, alongside the main market in Tokyo there are also exchanges in Osaka, Nagoya and Sapporo. In Germany, although the majority of trade is routed through the Frankfurt exchange, it forms one of eight regional exchanges across which trade has been traditionally segmented. These exchanges operate through a joint-stock corporation - Deutsche Borse AG – which is primarily owned by Germany's three major banks. Although some commentators have predicted the eventual elimination of the regional exchanges outside of Frankfurt, they have continued to play an important role in raising finance for many German companies, and in the cases of Hamburg-Hanover and Berlin-Bremen have evolved through the establishment of regional strategic alliances.

Furthermore, the consolidation of the largest stock markets is occurring in tandem with the proliferation of smaller exchanges. In total, 43 nations opened indigenous stock exchanges between 1980 and 1998, with many of the smaller and newer European nations now having their own exchanges, including exchanges in Vienna, Zagreb, Prague, Copenhagen, Helsinki, Budapest, Amsterdam, Oslo, Warsaw, Lisbon, Bucharest, Madrid, Barcelona and Stockholm. The Irish Stock Exchange was also re-established through devolution from the LSE in 1995.

3. The UK's Current Stock Exchange System

The current market for the buying and selling of company stocks and shares in the UK is monopolised by the London Stock Exchange (LSE), which is primarily engaged within a system of international competition of hosting large stock trades in global marketplace. This has evolved as the world's largest markets and exchanges have sought to rationalise and consolidate their positions. The outcome of this is that the position of middle and small market companies is increasingly becoming squeezed as the blue-chip stocks become the order of the day – every day. The LSE has fought to combat this situation by the introduction of its Alternative Investment Market (AIM) in 1995 with just ten companies, and operates as a second tier market targeting new and small companies. Membership requires no minimum trading record, no minimum assets or profit levels, no minimum capitalisation and no minimum free float of shares. Since its establishment, approximately 700 companies have sought equity through AIM.

Also established in 1995, outside the realms of the LSE, was the off-market trading facility OFEX created by the market-maker JP Jenkins Ltd. OFEX is neither regulated nor a market, but aims to provide a more cost effective and less regulated alternative to AIM, and is a vehicle for creating liquidity and sourcing new funding opportunities. By 2002 OFEX had provided more than 450 companies with access to capital, and organises trading in the shares of more than 180 companies. Another recent initiative has occurred in Scotland, where a local stock brokerage attempted to launch *ScotX* in 2002, a marketplace for unquoted companies to have their shares traded on a dedicated trading platform. Current market conditions have delayed its development and the project is currently on hold. However, the project appears to be nearer a buyer-seller matchmaker since it cannot create liquidity for companies.

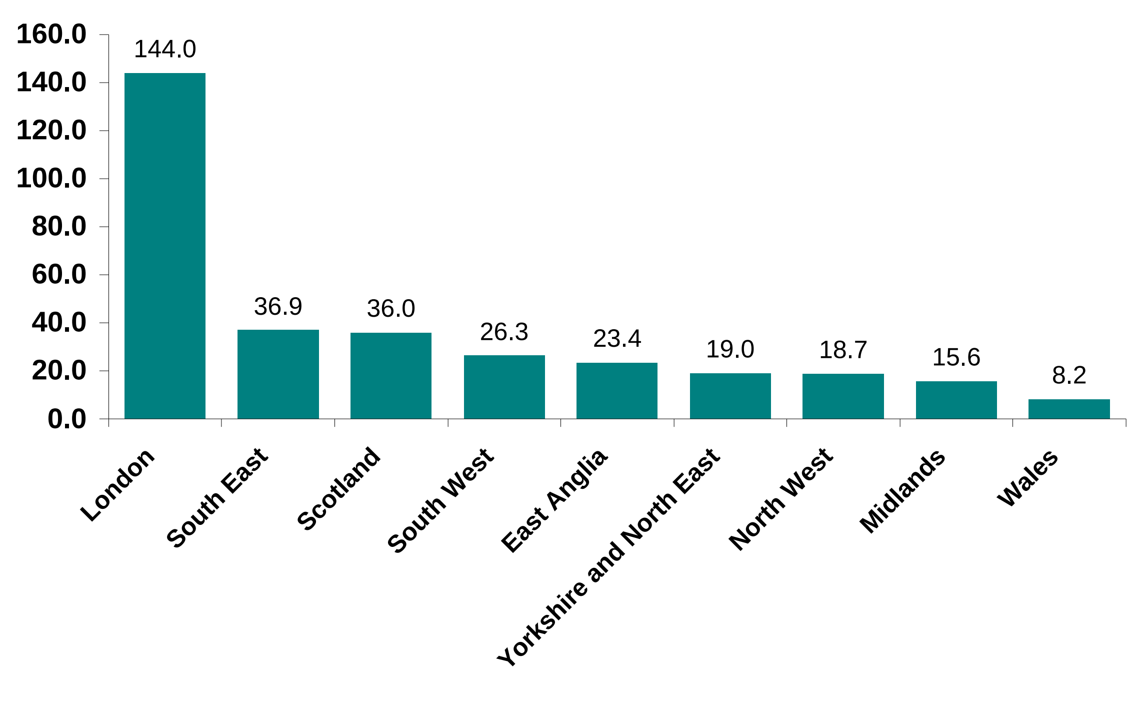
Despite the developments, there is little evidence that indicates an alleviation of the long-term equity gap among those regions outside of the south-eastern England arc. Table 1 indicates the number of firms currently listed on the LSE and AIM by region, along with the total market capitalisation of these companies and the relationship between regional market capitalisation and regional gross domestic product (GDP). We can see that some of the lowest levels of listed companies and total market capitalisation exist in the English regions of the South West, North West, the Midlands, and the North East and Yorkshire. However, completely dislocated from the rankings is Wales, with only 21 listed companies and a total market capitalisation of only £1.4bn, equating to only a 5% share of total GDP in Wales. Compare this with London, which has 960 listed companies with a market capitalisation of £763.3bn, which equates to more than six-times London's GDP. Figure 1 illustrates this disparity on a per capita basis, confirming the dominance of London and the South East as the location for the headquarters of a significant proportion of the UK's publicly-quoted companies.

Table 1: Number of Companies Listed on the London Stock Exchange and Market Capitalisation by UK Region (Number of companies as at March 2003)

Region	Number of companies	Market Capitalisation (£bn)	Regional Market Capitalisation as a proportion of GDP
London	960	763.3	621%
South East	261	169.5	139%
Scotland	159	79.0	123%
Midlands	138	28.9	25%
North East, Yorkshire and Humberside	134	51.1	61%
East Anglia	132	31.7	39%
North West	118	12.5	16%
South West	109	18.6	32%
Wales	21	1.4	5%
Total	2032	1156	153%

Source: London Stock Exchange

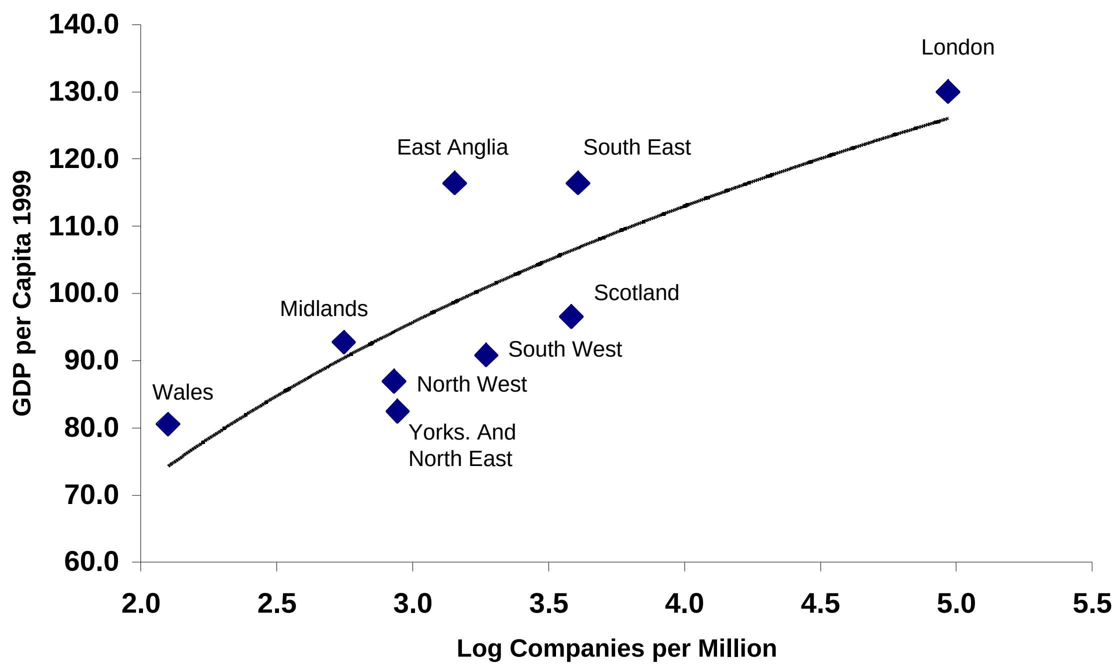
Figure 1: London Stock Exchange Listed Companies per Million Inhabitants by Regional Location of Registered Offices



Source: London Stock Exchange

This has a negative effect on both the more peripheral regions as well as the South Eastern arc, which has increasingly become over-heated through a seemingly insatiable demand for land and space, while the peripheral regions continue to be starved of investment. These effects have resulted in the polarisation of economic performance between the North and South of the UK. The Government has sought to narrow this divide through the establishment of community investment and financial development programmes. However, it is our belief that a mechanism for stimulating businesses in the most economically weak regions to raise finance through the public offering of stock market has a greater capacity to develop a more even economic landscape in the UK, as well as providing a more even flow of resources across regions. Evidence of this potential is clear from Figure 2, which shows an undoubted relationship between regional GDP and stock listed companies per capita. The UK Government has stressed that it is committed to implementing economic reforms to remove the barriers which prevent markets from functioning efficiently. This structurally embedded financial divide must surely constitute one of the barriers to achieving this efficiency, and is an indication that market failure exists on a cross-regional basis.

Figure 2: Relationship between GDP per capita and London Stock Exchanges Listed Companies per Million Inhabitants by Region



Source: London Stock Exchange, EUROSTAT

4. Economic Development, Market Failure and Barriers to Entry

As the financial economists Klaus Weber and Gerald Davis argue ‘stock markets are at once a means of channelling capital, a probe for taking the pulse of an economy and assessing its future prospects, a mechanism for effective governance, and a fulcrum for producing institutional and social change within an economy.’ Fundamentally, the objective of a stock exchange is to provide a market for the buying and selling of shares that is both liquid and open. In particular, stock market listings provide companies with a potentially long-term source of funds for investment requirements. Therefore, from an economic development perspective this should be an efficient means of circulating wealth and allowing business development opportunities to be fulfilled. In other words, although economic development issues tend to be focused on the production of goods, services and businesses, it is as much about institutions within the sphere of finance and investment.

Stock market centred institutions of corporate governance, through the growth of shareholder capitalism, have become increasingly important actors across economic systems. Unfortunately, within the UK, the current stock exchange has becoming institutionally-centric towards both large investors and large businesses. For instance, the Sunday Times recently stated that 'The City has turned its back on scores of small quoted firms and now many are quitting the stock market' (November 3, 2002). The rationale behind this claim is that fund managers increasingly only want to invest in large companies – large usually referring to companies with a market capitalisation in excess of £1 billion. Without such institutional interest many of the – relatively – smaller members of the LSE do not possess the clout required to make the investment deals they require.

The relationship between institutional investors and stock markets becomes one primarily involving large national and multinational companies and the equity gap in the least prosperous regions of the UK grows, as they are home of many of the middle and smaller market firms unable to acquire the investment required to develop and innovate. Crucially, poor liquidity – liquidity that stock exchanges facilitate - and the administrative burden of accessing finance investment are the major problems for many of these firms. One result of these problems is that these companies, particularly within knowledge-based sectors, become prey to involuntary acquisition principally because of the lack of equity investment they are able to access.

Interestingly, and in relation to involuntary acquisition, dependency economic theorists consider that the penetration of foreign capital affects the ability of regions or nations to act as rationally as possible in their best interests, due to a lack of informed and empowered decision-making. This further suggests that a relative dependence of foreign direct investment, such as exists in the northern parts of England and Wales, impedes the ability of these regions to become sufficiently involved in accessing stock markets, as the foreign-owned businesses become the lead actors within business and economic development decision-making.

The finance 'escalator' for potentially growing firms in the UK appears to be suffering from serious mechanical failure. In an ideal world, as a company grows it exploits new avenues of funding; moving from the initial stages of friends, family and banks, to business angels and eventually the capital markets. This system assumes that a seamless flow is possible, and that finance markets respond to the needs of firms. There is also a clear exit route depicted for each investor; reducing the perceived level of risk. However, in the UK this flow is usually far from smooth. As larger companies have come to increasingly dominate global markets, the financial market response has been to develop a complex and strict regulatory system. This has inevitably added substantial costs, in terms of both time and funds, to the process of stock exchange listing. Recent research by SWR Worldwide found that the cost of listing on the stock market has been highlighted as the number one concern amongst potential issuers of public shares in the UK. Although we do not have figures available for the LSE, it is interesting to note that the New York Stock Exchange, which operates according to a similar system as the LSE, generates 40% of its revenues from listing fees alone.

Poor liquidity has been repeatedly identified as a major problem for the UK's SMEs. Nevertheless, an examination of the LSE's extensive regulatory requirements highlights the burden placed on companies wishing to list, and even the marketing literature warns that it is a long and expensive process. With an average cost of an Initial Public Offering (IPO) on either the LSE or the small Alternative Investment Market (AIM) estimated at £500,000, the cost of listing is also prohibitive for many middle market companies. Furthermore, a key component of the prospectus required by the LSE is the disclosure of information which is essentially subjective, and the interpretation of requirements needs a relatively high degree of sophisticated experience, most of which only exists within London's financial centre. This can pose pragmatic problems for companies based in other regions, as well as issues of unease and unfamiliarity.

The efficiency of a stock market is vital not only to the firms which enter and exit it, but also crucially to the venture capitalists, for whom an IPO stock market listing is an important potential exit route. However, within the UK a negative trickle down effect is emerging, whereby smaller and middle market companies are becoming increasingly unlikely to list themselves on the LSE or any other exchange, and venture capitalists are also become less and less likely to invest due to the lack of a visible exit route. The domino effect being that smaller companies increasingly find the doors of venture capitalists shut. Our conclusion is that the current structure of the UK capital markets does not aid smaller companies in their quest for development, and currently is also acting as a powerful deterrent to potential investors. A factor in defence of the LSE, as we will see below, is that the competitive performance of those firms that do achieve an LSE or AIM listing is usually superior to the majority of unlisted companies in the UK. The objective of regional stock exchanges is to permeate this performance potential across a far wider stock of businesses in the UK.

5. The Challenges for Regional Stock Exchanges

The key features of any stock exchanges that are established in the UK's regions should include a: (1) a regulatory structure that is transparent and does not overburden the administration functions of listed companies; (2) a fee structure that is not prohibitive to the majority of smaller and middle market companies; and (3) an application process that is flexible and responsive to the resources and capacity of these companies. The rationale behind a company listing should be to financially empower these businesses to undertake the innovations, adaptations and transformations they require to grow. However, it is clear to us that the proposed regional exchanges will face a myriad of challenges if they are to be able to achieve their aim as the catalysts of this growth. The following sections outline these key challenges.

Create Tangible Business Benefits

If regional stock exchanges are to be considered a realistic option for the UK they must bring clear benefits to both the businesses involved and the economies within which they participate. The most tangible measures of business benefits are those of profitability and growth, and research demonstrates that listing on a stock exchange significantly improves the likelihood of higher sales and profit growth than their unlisted counterparts. A survey undertaken by Mark Clatworthy and Michael Peel of Cardiff Business School of more than 150,000 listed and unlisted companies in the UK found:

- 78.4% of LSE or AIM listed companies achieved sales growth in during a given year, compared with 60.6% of unlisted companies.

- 66.7% of listed companies had employee growth, compared with 57.4% of unlisted companies.

- 67.9% of listed companies achieved profit growth, compared with 45.8% of unlisted companies.

- 85.1% of listed companies actually made a profit, compared with 68.3% of unlisted companies.

The differentials are equally noticeable for both firms listed on the main LSE exchange as well as those on AIM, the market for smaller listed companies, which again suggests the higher number of firms that could achieve these benefits if they were stock exchange listed. Crucially, the cost of capital is also reduced for stock exchange listed companies. If regional exchanges are further able to reduce to regulatory burdens and fee, then a regional listing would become an increasingly viable alternative to accumulating debt. As regional exchanges become an efficient and cost effective method of raising finance; it will also improve the gearing ratios of members companies, as the balance between debt and equity shifts to the latter.

Reduce Information Asymmetries

Resource allocation within the UK capital markets is currently inefficient partly due to the information asymmetries that exist between the key investors and many of those businesses outside the pool of preferred investor companies, mainly the blue-chips. We consider that these inefficiencies are most accentuated for those smaller companies that are the most geographically remote for the financial and business institutions in London. This argument is supported by evidence from a number of financial economists.

For instance, Ross Levine has found that individuals and institutions are unlikely to invest in companies or activities about which there is little reliable and comprehensive information, with smaller companies suffering from a relative lack of interest and research by organisations such as investment banks and research agencies, primarily due to the high transactions costs of obtaining this information. These high costs harm the liquidity potential of these businesses and restrain capital from flowing to its most productive use. In his paper ‘Location Matters’, the German economist Harald Hau found a significant relationship between the trading profits of stock traders in Germany and their relative geographic proximity to the corporate headquarters of the companies they trade in. This strongly suggests that geography plays an important role within the principles of efficient market hypothesis relating to stock trading.

If prices are to reflect all relevant information, this must include local knowledge, and this is an area where the LSE’s performance is perhaps weak, with the vast majority of analysts concentrating upon the major stocks. Regional stock exchanges will be challenged with increasing the availability and interest of smaller company information and research. This will reduce current informational asymmetries, and in turn develop a more efficient system of resource allocation through stock price discovery that is far more fully informed.

Attract Investors

Regional stock exchanges should play an important role in maintaining a breadth of investment choices for both individuals and institutions. Despite the *No Logo* thesis of globalisation, the business world still predominately operates within a framework where a market for any particular product or service consists of many customers all having different needs and wants, and if these customers can be segmented, then adopting a local design strategy may be the most appropriate method of product delivery. We can apply this method to the concept of regional exchange since all customer needs many not be currently met by the national exchange. For instance, although the UK has the largest financial services market in the world, with a large pool of wealthy investors, only 25% of the UK adult population own shares, compared with 48% of the US adult population. This suggests that the market for shareholding in the UK has room to grow, and the current 'products' on offer do not fully meet the requirements of either issuers or investors. By diversifying the product range on offer, a wider market can be accessed, and the level of demand for investing can be grown and developed.

Create Stock Exchanges Responsive to Economic Policy

It was in the late 1960s that John Hicks suggested that primary causes of the industrial revolution were the capital market improvements that mitigated liquidity risk. In other words, the industrial revolution was reliant on the financial revolution. Much is this same today, with the implementation of economic policy relating to development and regeneration highly dependent on the financial capacity and framework to support such policies. The success of innovation-related policy, in particular, is not only reliant on a stream of public sector funding, but also businesses themselves being able to supply at least part of the necessary investment to undertake research and development activities. This implies a clear link between economic development and the liquidity of businesses.

An important benefit of regional stock exchanges should be to stimulate innovation through liquidity. The link between the lack of innovation in the UK and the lack of patient investment capital within London's centralised stock system is now a well-rehearsed and documented argument, with investors shy of providing finance in companies that are innovative projects that may possess a level of liquidity that is inverse to the short-term equity that is usually their preference. Regional stock exchanges represent an opportunity to develop an investment culture that is both more long-term and suited to the regional economic requirements.

For instance, the stock exchange of Switzerland is currently being re-modelled, in terms of its market segments, which will align with the industrial cluster and sector policies of the federal and local governments. In particular, a special emphasis is being placed on healthcare and related growth industries, with increased sector-specific information and acquisition activities being encouraged and stimulated within these areas. This is coupled with a high standard of transparency for companies listed in these sectors, even though they may have a relatively brief track record of business operations. The Italian stock exchange is following a similar path with regard to firms within the designer fashion sector.

We consider that regional exchanges and the LSE in the UK could each fill a distinct economic space that thrives on its specialities and niches, within a coexisting environment that is collaborative as opposed to hostile. Such an approach would allow regions to play to their strengths and capacities, and enhance their overall economic potential.

Build Regional Finance and Business Clusters

Although the creation and expansion of regional finance and business sectors should not be a direct aim of regional stock exchanges, as we have argued above, this infrastructure will be an important factor in alleviating the current information asymmetries resulting in improved knowledge and resource flow. Under the current system, the majority of advisors to LSE list firms are, as one might expect, based in London, which adds to core-periphery information imbalance and limits the scope of regionally-based advisors.

However, as a regional exchange develops so too should the concentration of feeder services, such as research agencies and financial and business advisory services. A regional stock exchange should become the institutional trigger for the establishment of a finance and business cluster, creating quality employment within these sectors. In general, we find that those regions and cities around the world possessing a stock exchange have between 25% and 50% more employment in the finance and business service sector than their national averages. Within a system of regional exchanges local advisors can flourish; taking a more substantial role, and forge long-term relationships with local businesses. As the advisors and analysts produce increasingly sophisticated information, any perceived investor risk of those companies listed on the regional exchange – or seeking to list - should decline, encouraging further investment and reducing of the equity gap.

Encourage Greater Worker Productivity

Other indirect benefits of regional stock exchange should include the establishment of a market encouraging the expansion of the employee share schemes, which the UK government have sought to stimulate in order for businesses to accrue increased motivational and productivity benefits. Equity ownership is seen to create an incentive for employees to work more effectively; however, a key barrier is creating a mechanism for taking monetary advantage of such ownership. At present, employee shares schemes are most prevalent among larger stock-listed companies based in the South-Eastern parts of England. Clearly, the establishment of regional stock exchanges could encourage further widespread development of these schemes, stimulating both local firms and their employees, with share schemes typically 2-3 times more likely to be found in stock listed businesses.

Generate a Significant Macroeconomic Impact

The macroeconomic impact of stock exchange activity is best measured by the investment potential of listed firms through the exchange of equity. This investment potential consists of total market capitalisation of each firm. Investment is a key component of economic output, since it is a major constituent of national income accounting identity and plays a major role in determining future levels of economic output. At the regional level in the UK there is strong correlation between current economic output and total investment (as measured by Gross Fixed Capital Formation). The model summarised below examines the forecast effects of increasing the number of firms within particular UK regions that gain investment through the public offering of shares. The model is based on the assumption that the mean market capitalisation of the newly listed companies will in due course equate with mean market capitalisation of firms already listed on the LSE that are headquartered within their region. Therefore, the analysis takes account of the differing regional industrial structures in terms of average business size and sector of activity. However, it should also be viewed as a relatively long-term indication of the potential effects of establishing stock exchanges within these regions.

The model is based on analysing the relationship between levels of investment (as measured by gross fixed capital formation), the relative size of equity markets and economic output across UK regions. Fundamentally, the model anticipates that levels of investment rise given increases in the market capitalisation of listed companies across UK regions. The modelled relationship utilised between the levels of investment (measured by Gross Fixed capital Formation) and total regional market capitalisation is presented below as equation (1).

*Equation (1) - Gross Fixed Capital Formation (GFCF) = (100.16*Total Regional Market Capitalisation) + 3734.6*

The relationship between levels of investment and economic output is given in equation (2).

*Equation (2) – Gross Domestic Product (GDP) = (GFCF*0.0116) – 5.6*

Combining equation (1) and (2) results in equation (3), which determines the relationship between the size of regionally listed firms and overall economic output.

*Equation (3) - GDP = (((100.13*Total Regional Market Capitalisation)+3746.6)*0.0116)-5.6*

Table 2 illustrates the forecast change in GDP per capita across the UK's least prosperous regions assuming a range of increases in the number of stock listed companies within each region. The changes in GDP per capita are based on an assumption that other regions remain static in terms of their number of listed companies. However, if any of the scenarios listed below become a reality, the effect on the UK's total economic output would be profound. We can see that in the case of Wales, the embedding of 30 new listed companies on a stock exchange has the capacity to increase regional GDP per capita from 80.5% of the UK average to 84.7%. At the same level the GDP per capita of the South West of England region would increase from 90.8% of the UK average to 99.9%, and the North West from 86.9% to 93.1%. In the cases of Yorkshire and the Humber, the East and West Midlands as well as the South West, if any were to establish and embed 40 more stock listed companies then potentially their GDP per capita would exceed the UK average in the long-term.

If the model we have utilised comes anywhere near matching economic reality, it is clear that the establishment of a wider group of firms with access to investment through public equity offerings across the UK's least prosperous regions has the potential to have a very significant impact on their macroeconomic performance. The outstanding question is whether these regions possess a strong enough base of companies that have potential to undertake this approach. This is a question that we consider should formulate a key part of the feasibility work we are recommending. However, as an initial barometer it is worth highlighting that there are more than 32,000 middle market companies across the UK - with an annual turnover of more than £5m - that are not currently listed on any recognised stock exchange. Even assuming an uneven spread of these businesses across regions, we would anticipate that even the least endowed regions will have a minimum of 1,000 firms of this size. This suggests that there is more than enough scope for further companies to take a stock listing approach to raising investment.

Table 2: GDP per Capita Scenarios Relating to an Increase in the Number of Stock Listed Companies within particular UK Regions

Region	Current Index of GDP per Capita	20 more listed companies	30 more listed companies	40 more listed companies	50 more listed companies	60 more listed companies
Wales	80.5	83.1	84.7	86.3	87.9	89.4
North East	77.3	83.9	87.5	91.0	94.5	98.0
North West	86.9	91.0	93.1	95.1	97.2	99.2
Yorkshire & the Humber	87.9	95.7	99.7	103.7	107.7	111.7
East Midlands	93.6	99.4	102.6	105.8	109.0	112.1
West Midlands	91.7	97.8	100.9	104.0	107.2	110.3
South West	90.8	96.8	99.9	102.9	105.9	109.0
UK	100.0	100.0	100.0	100.0	100.0	100.0

Source: Robert Huggins Associates

6. Conclusion and the Way Forward

The current economic climate in the UK may not be right to launch a regional stock exchange, or exchanges, at this point in time. However, it is the right time to undertake the feasibility and planning work required, so that the framework for their introduction is in place once market forces are more conducive. We consider that the fundamental concept is robust within a UK context and represents the next logical stage of decentralised economic policymaking relating to the finance gap experienced by many businesses in the UK. At this moment in time we do not have strong considerations on the number of exchanges or their role in relation to the national LSE. In many ways, the process should mirror that relating to political devolution in the UK. Each region should decide whether there is sufficient potential demand for the product, and if so the product should be given the freedom to evolve its status and role. In terms of this status, there are at least four overlapping possibilities; (1) regional markets as a feeder for the LSE or other global markets; (2) regional markets become self-defined markets operating within specialist and niche sectors; (3) regional markets operate within a framework where dual listing between the regional exchange and LSE is possible; and, perhaps most unlikely (4) regional exchanges attempt to compete with the LSE. As far as economic impact is concerned, it is the first option that is likely be the most beneficial, whereby as firms grow they gravitate towards the larger markets in search of further investment with which to develop. The success of this approach would hinge upon close collaboration and cooperation between the regional and national exchanges. The LSE, therefore, should not view the development of regional exchanges as a threat, but as a long-term source of new business.

We believe that the next stages of development should involve regional policymakers undertaking a detailed analysis relating to: potential demand; infrastructural and supply requirements; scope for public sector intervention; and cost-benefit analysis. In the case of Wales, we suggest that Finance Wales has both the capacity and competence to become the architects of a Wales Stock Exchange, and is closely in keeping with its aims and objectives of providing an affordable means for Welsh businesses to attract investment capital. In particular, *Finance Wales Investments*, a wholly-owned subsidiary of *Finance Wales*, is already involved in procuring private and public sector funding, and investing in pre-IPO businesses, in a loan, mezzanine or equity fashion. *Finance Wales* has the expertise to both select and assess companies according to their potential, and advise businesses as to their requirements in a post- IPO environment. Finance Wales is ideally placed to feed Welsh companies into a Wales stock exchange. Another potential role – which would require in-depth study – would be to ensure that there is a sufficient degree of liquidity within the regional market, i.e. both companies and investors can trade stock at a fairly valued price, rather than be prone to the wide spread in buy and sell prices that are often a feature of small exchanges and markets. This could be achieved by developing mechanisms whereby shares are held by a large base of investors, rather than within one or two large organisations. Also, it is essential that businesses are fully market ready before any IPO, once again to maximise appeal to a wide range of potential investors, and that help is available to minimise listing fees and other transaction costs. This investigation of current and future market conditions, and the potential role and relationships between existing agencies and the proposed exchanges, will ensure that policymakers and businesses across the regions are fully aware of the potential opportunities and attached implications.