TheCityUK

Catalysts for Growth:

Boosting UK Growth Markets

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About TheCityUK

TheCityUK is the industry-led body representing UK-based financial and related professional services. We champion and support the success of the ecosystem, and thereby our members, promoting policies in the UK and internationally that drive competitiveness, support job creation and enable long-term economic growth. The industry contributes 12% of the UK's total economic output and employs over 2.4 million people – with two thirds of these jobs outside London across the country's regions and nations. It pays more corporation tax than any other sector and is the largest net exporting industry.

Introduction

The UK is a nation of entrepreneurs, with SMEs (small and medium-sized enterprises) accounting for 99.9% of the business population in the UK.[1] Of those SMEs, high-growth companies represent over 50% of the total SME turnover.[2] The UK ranks third in the world for the ease of doing business,[3] has a highly skilled and diverse workforce and strong infrastructure to support innovation-driven businesses. Over 700 companies have shares traded on UK Growth Markets[4] with a market capitalisation ranging from just a few hundred thousand to over £3bn. There are 13 million people in the UK with cash savings of approximately £430bn that could be proactively[5] invested[6], with more than four million people who want to take at least some form of investment risk.[7] Taken together these factors create the ideal backdrop for growing companies.

However, while the UK has a strong record of building innovative growth companies, too many of them are choosing to continue their growth outside the UK. Despite their reputation for easier access to capital than on a main market, there is concern that UK Growth Markets[8] have been overlooked by recent capital markets reforms. Recent market volatility has affected investor confidence; Liquidity concerns have made it harder for companies to trade shares and for investors to exit positions and a narrower pool of institutional investors has impacted price discovery. The lack of focus on the markets alongside these concerns has created a challenging environment for growth companies looking to go public in the UK.

To keep the value, innovation, jobs, tax revenue and economic growth that UK Growth Markets support we must treat them as a source of strength, building economic security for individuals across the country and supporting the governments drive for growth.

Throughout their lifetime, growth companies will access various equity and debt funding options as they grow and their business needs evolve. From bank loans, government-backed or regional schemes such as the Enterprise Investment Scheme (EIS), angel investors and venture capital, to private equity to public equity markets, the right funding option for a business depends on factors such as their stage of development, the sector in which it operates and its growth potential. UK equity markets are one source of funding that can play a critical role in enabling entreprenuers up and down the country to build their businesses, create jobs, support their local communities and drive economic growth.[9]

1 TheCityUK, 'Making the UK the leading global financial centre: An international strategy for the UK-based financial and related professional services industry', (September 2021), p.10, available at: https://www.thecityuk.com/media/q0mewp0i/making-the-uk-the-leading-globalfinancial-centre.pdf
2 The UK Fast Growth Index
3 The Global Financial Services Index 36
4 Over 600 on AIM & and over 100 on Aquis Graduating from a Junior Stock Market in the UK FINAL.pdf
5 Based on Money and Pension Service (MAPs) view that 3-6 months' worth of outgoings should be held in cash- but other savings really would benefit both individuals and the wider growth of the economy by being invested
6 Are there UK savers who could become investors that grow the UK economy?
7 The Centre for Policy Studies, Retail Therapy
8 For this paper we have used the term Growth markets but would highlight that regulatory definition is SME Growth Market
9 Overview of exchange | London Stock Exchange (AIM) | Cross-Border Listings Guide | Baker McKenzie Resource Hub

Recent UK capital markets reforms have come at a time of renewed focus from the government on improving the business environment. In parallel, the European market is experiencing an increase in the backlog of demand for listings, and geopolitical developments are leading innovative companies across the globe to consider which jurisdictions will best align with their values to support their strategic goals. This gives the UK a significant window of opportunity to assess and address actions that together can supercharge the growth and competitiveness of the UK's Growth Markets.

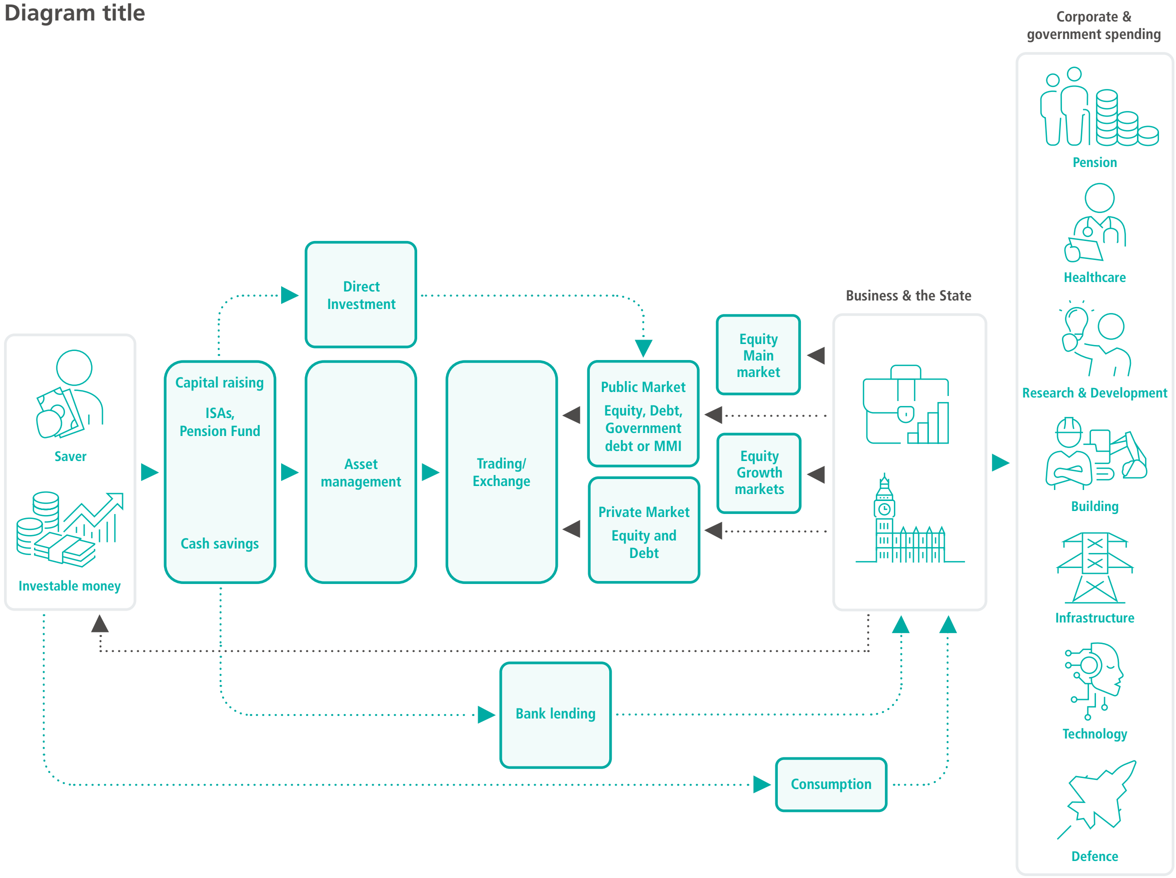
As we approach the 30th anniversary of AIM, and as public markets are undergoing a period of introspection, this paper sets out the advantages of a healthy Growth Market environment for companies with high growth potential, why it matters to the UK. It also details 10 strategic enablers to strengthen UK Growth Markets and their contribution to the nation's wider growth agenda. While the focus of this paper is on public equity markets, we briefly set out the strengths of the private capital markets and the interactions between those markets and public markets. The importance to the UK of other types of business financing and their potential contribution to the real economy should also be considered.

Across our industry, and among the trade associations with whom we worked on this paper, there is growing evidence[10] for the need to support and promote all parts of the UK's capital markets landscape to drive growth across the government's eight priority, sectors as set out in its 'Invest 2035: modern industrial strategy' and increase returns for investors.

Growth companies are those which have the potential to experience significant and rapid increases in revenue, profits, or market capitalisation, often outpacing industry peers and the overall economy.

Growth Markets in the UK, such as the Alternative Investment Market (AIM) and Aquis Growth Market, typically attract smaller, high-growth companies seeking to raise capital. While they are public markets, like the Main Market on the London Stock Exchange, company's shares are 'admitted' directly to them rather than needing to be 'listed' by the FCA and so are subject to a slightly different regulatory regime, tailored to meet the needs of growing companies.

Diagram title



10 For example: UKFinance: Growth Escalator, The Quoted Companies Alliance: The future of smaller company Capital markets, British Venture Capital and Equity Association: Venture Capital in the UK

Why do equity markets matter?

Equity is an important form of longer-term funding for companies, enabling them to finance expansion projects such as research and development (R&D) and, thereby, contribute to growth and innovation across the economy. Equity allows companies to share the risk inherent in any new venture, leading to more stable and resilient businesses. Equity markets, both public and private, offer a wide range of investment options, allowing investors to diversify their portfolios and opening the potential for higher returns.

[Infographic: Location and GVA of AIM Companies from Grant Thornton analysis of London Stock Exchange and Office for National Statistics data]

CASE STUDY

Breedon, a British construction materials company based in Leicestershire, England employs approximately 3,700 colleagues across 300 sites. Breedon was admitted to AIM in 2008 and following a period of growth transferred to a listing on the Main Market in 2023.

"For over a decade AIM provided us with access to diverse and engaged investors within a supportive community that understands the needs of entrepreneurial businesses"

Amit Bhatia, Non-Executive Chairman, BreedonGroup

Breedon entered the FTSE 100 in September 2023 and is an example of a British company which has used UK public equity markets to support its growth and value creation.

Why do public markets matter?

Funding for growth may initially be provided through the private markets. As businesses grow and reach a certain size and maturity, it becomes possible for them to access this funding through public markets. Companies will transition from private to public markets for several strategic reasons, primarily relating to capital generation, visibility, and liquidity. A recent innovation that aims to help with this transition is the Private Intermittent Securities and Exchange System (PISCES), a new type of stock market that will allow for trading of shares while a company remains private. Public Growth Markets will typically suit more mature companies with different needs, including higher liquidity from continuous trading, a broader retail investor base, the opportunity for new capital raising and increased public visibility.

Public markets function as a convener of a broader base of those who have capital (investors) with those who need capital (businesses). There are several benefits to public markets:

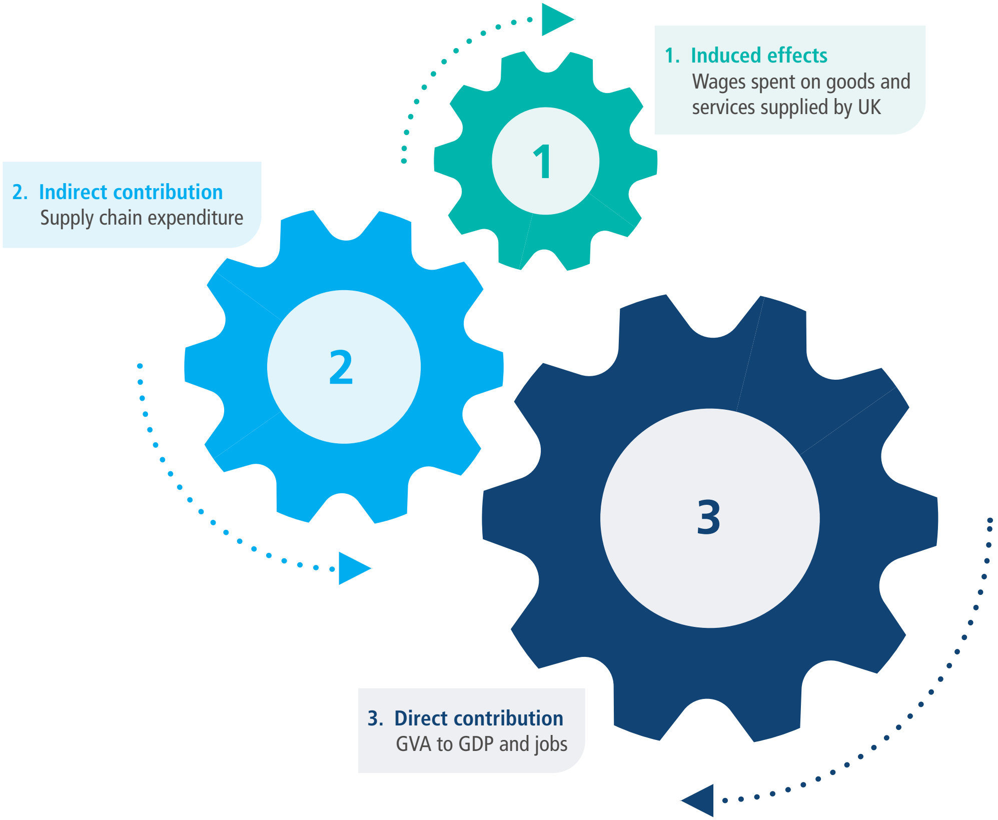
- They offer an important path for governments to democratise access to investment opportunities, as they allow a wider range of investors to participate.
- Unlike private markets, public markets allow investors to buy and sell their shares quickly, giving them access to capital when needed.
- They can help to stabilise the financial system and support economic recovery in times of need. Over £7bn of new money[11] was raised by UK listed companies, with £450m of secondary raises on AIM between 18 March 2020 and 9 April 2020[12] that supported businesses to re-establish their normal operations through the unprecedented stress of the Covid-19 crisis.
- The public nature of the companies on the markets means the capital is managed within an open system. Publicly traded companies are required to disclose certain information and adhere to regulatory requirements, both of which provide a level of protection for investors.

SulNOx Group, based in London develop natural biodegradable solutions to decarbonise liquid hydrocarbon fuels, reducing the production of harmful, environmentally damaging greenhouse gas emissions. With a international business model they could have chosen to go public in a number of regions. The main reason for choosing the UK was access to UK capital which allowed them to finalise development of their fuel additives.

They were admitted to Aquis Growth Market in 2021. The market has given them credibility when negotiating with much larger business partners around the world.

11 Addleshaw Goddard, Equity raising by UK PLCs in Covid-19 times
12 Equity fundraising considerations for AIM companies during COVID-19

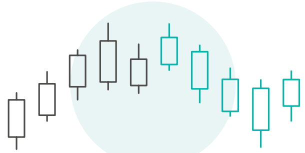
Within public markets, there is a distinction between those markets designed for smaller businesses that may be at an earlier stage of growth, and those for larger and potentially more mature businesses. Public markets give companies a sense of place, helping them to build visibility and cement ties in the country in which they choose to list. The companies that go public on these markets in the UK make a real contribution to the economy - directly through the value of goods, services and job creation, and indirectly through supply chains and employees' wages spent on goods and services supplied by UK businesses.



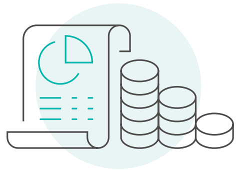
What are UK Growth Markets and why do they matter?

UK Growth Markets, including AIM and Aquis, are a significant component of the UK's equity markets. They support the vibrant, diverse range of companies being nurtured up and down the UK, enabling them to raise funds, promote their businesses and engage with larger more established companies. Most new admissions onto UK Growth Markets (83% on AIM since 2015 and 76% on Aquis since 2020) are UK incorporated companies. These Markets provide a home for companies across the UK's regions and nations, who in turn support government's plans for national growth. Not only do they serve growth companies, but also a range of companies that benefit from being on public markets. The market enables individuals and pension funds to put their savings to work in some of the most innovative companies in the UK, as well as offering the opportunity for individuals to support the pioneering and entrepreneurial work of UK companies. The regulated nature of these markets provides a level of protection that private markets do not. The businesses the markets facilitate play a vital role in balancing regional disparities by providing anchor institutions for local economies and drawing additional revenues into the UK from overseas through exports.

In 2023 AIM companies contributed **£35.7bn** gross value added to UK GDP and directly supported more than **410,000** jobs.



Approximately **25%** of shares held on AIM are held by retail investors compared to **10%** on Main Market



These companies made a corporation tax contribution of **£5.4bn** to the Exchequer.

AIM companies are, on average, more productive than the national average with productivity of **£87,100** GVA per employee[13]

13 Grant Thornton, The Economic impact of AIM companies

Number of companies admitted to AIM	Number of companies admitted to NASDAQ First North
753	531

Number of companies admitted to AIM vs NASDAQ First North in 2023

By providing access to finance, UK Growth Markets enable new and existing companies to make the investment needed to turn ideas into products, services and jobs. Mid-sized companies are often drawn to Growth Markets not only as a platform to raise capital, but also because of the increased visibility and credibility that comes from going public under a regulatory regime tailored to their needs. The capital generated by the markets is used by companies to execute their strategies, invest and drive growth within their locales. For example, Watkin Jones, based in Bangor, Wales, develops residential properties for students and young professionals. Verici Dx plc, a Penarth based company, develops advanced clinical diagnostics for organ transplant disease. Shepherd Neame, based in Faversham, Kent, is Britain's oldest brewer.

CASE STUDY

Diaceutics, based in Dundalk, Northern Ireland is a diagnostic and data company providing services to many of the largest global pharmaceutical companies.

"Diaceutics was founded out of a desire to get more patients access to improved healthcare. Our IPO helped us in our mission to continue this great work"

Peter Keeling, Chief Executive Officer

Since going public the Diaceutic's market capitalisation has almost doubled. Being admitted to the market has also helped their visibility supporting them to secure contracts across international markets.

Companies like these create jobs in their local communities, advance R&D, attract investment into regional hubs, build and preserve infrastructure and support local universities. Businesses admitted to UK Growth Markets can have significant positive impacts on regional economies across the UK through job creation, supply chain relationships, and attracting investment to their local areas. They also give individuals opportunities to invest in assets that can deliver returns to support their financial resilience and save for their retirement aspirations and needs.

CASE STUDY

KR1 PLC, based in Douglas, Isle of Man is an investment vehicle which makes investments in new technology opportunities, particularly in blockchain-based digital assets.

KR1 were seeking capital in order to make strategic investments in digital assets in 2018. Due to the lack of understanding around these types of investment then, the company was finding it difficult to raise money through private investment.

By creating a public company and complying to the rules of an exchange, particularly in a country as financially sophisticated as the UK, KR1 was able to reassure investors of its credibility, thus giving them the confidence to invest.

What does a successful Growth Market look like?

A healthy Growth Market plays a crucial role in fostering economic growth by providing small and medium-sized companies access to capital. The advantages we believe that contribute to a thriving Growth Market include:

- **flexible and proportionate regulatory environment:** Once admitted to a Growth Market, a company operates under a regulatory framework that is appropriate and accessible for their size and growth potential. A clear, proportionate and well-enforced rule book supports a company's reputation by boosting confidence in its conduct.
- **Efficient capital raising, liquidity and trading:** Enabling public companies to raise funding for growth through both an 'initial public offering' (IPO) and secondary market offers. The market will create access to a diverse pool of investors with an interest in funding growing businesses, while enabling investors to buy and sell shares with relative ease. A thriving growth market helps companies develop a mature investor base by attracting a mix of retail and institutional investors.
- **Sector and geographical diversity:** A thriving Growth Market attracts companies from various sectors, providing investors with a broad range of investment opportunities and contributing to a well-rounded economy.
- **Technologically enabled:** Technology and innovation help to streamline and optimise systems and processes, minimising costs and burdens for companies going public.
- **A supportive ecosystem:** An effective Growth Market offers a company credibility and visibility, increasing its attractiveness to potential investors, partners and customers. It also offers the possibility to engage with a network of experienced advisors, brokers and investors (through the market they are admitted to) who can offer guidance. A market should offer resources such as mentoring programs and business development support.

While UK Growth Markets possess significant strengths in all these areas, there is potential to enhance these strengths and build on recent capital markets reforms to ensure that UK capital markets support businesses of all sizes and sectors across the UK to invest, innovate and grow.

Sectoral distribution of fundraising on AIM and AQUIS

Strategic enablers for the UK's Growth Markets

We recommend that government and regulators work with UK Growth Markets and the industry to deliver action in the following areas, to maximise this potential and support growth across the economy.

1. **Establish a Growth Markets Industry Group:** Government should convene a specialist group[14] of experts to help it identify and enact specific ways to improve and champion the UK's Growth Markets over a specified time-limited period. This non-statutory group should include Growth Market representatives, market practitioners, investors, issuers and regulators, with a clear commitment from all to implement its recommendations.
2. **Extend support programmes for scaling businesses:** Government should consider extending programmes such as those run by the British Business Bank, to include investment in UK growth companies.[15] Ensuring a nurturing business environment for growth companies will be a key component of boosting the attractiveness and benefits of UK Growth Markets.
3. **Apply a Growth Market lens to regulation:** Policymakers (particularly in HM Treasury (HMT), HM Revenue & Customs (HMRC) and the Financial Conduct Authority (FCA)) should use one definition[16] for UK Growth Markets to optimise clarity and consistency of policy and regulations for those seeking to invest in, or become, Growth Market stocks. A review of where market infrastructure rules designed for senior markets could be adapted to meet the specific needs of both companies and investors on Growth Markets is also recommended. Specifically, regulators should consider how REUL (retained EU Law) can be tailored for Growth Markets[17] at the point at which the Smarter Regulatory Framework is being used to convert legislation into FCA rules.
4. **Rethink marketing rules:** Government and regulators should use behavioural analysis and an outcome-based approach to inform their approach to marketing rules, including Conduct of Business Sourcebook (CoBS) and Markets in Financial Instrument Directive (MiFID). Policymakers should be more granular and balanced in setting out the risks and rewards that UK Growth Markets offer to potential investors (given they have met market admission requirements) in comparison to largely unregulated assets such as crypto-assets, and adapt policy and regulation accordingly.
5. **Remove barriers that reduce liquidity in the markets:** Policymakers and regulators should review measures that have negatively impacted liquidity in the markets including 'Dear CEO' letters, Consumer Duty best practice guidance, and requirements for additional checks on the liquidity of Growth Markets shares. These measures are severely hampering the competitiveness of UK Growth Markets. The availability of high-quality investment research will help democratise UK capital markets and support liquidity in UK Growth Markets. The FCA/HMT should progress next steps in reforming the regulation of investment research.
6. **Review asset management reporting requirements:** Excessive passive investment can lead to an over emphasis on investing in funds that track Main Market indexes. This reduces the potential demand for investment in companies on Growth Markets. UK regulators should review reporting requirements with a focus on their behavioural and outcome impacts, to ensure they are not too burdensome and unintentionally reduce active fund management. Requirements should include a realistic evaluation of liquidity and its perceived impact on risk.
7. **Boost institutional investment into UK Growth Markets:** Government should use policy reforms to boost institutional investment in UK Growth Markets. Signatories to the Mansion House Compact should consider the ease of investing in Growth Markets[18] as part of fulfilling their commitment and specify the proportion of their funds invested in Growth Markets in their annual reports. Disclosures of investments in UK Growth Markets should be included in the FCA Value for Money Framework. The government should also consider fiscal incentives to increase investment in UK Growth Market shares to support the growth of the UK economy. Growth Market companies that are firmly rooted in a region should have the potential to benefit from Local Government Pension Schemes (LGPS) investment by being included in the 5% local target.
8. **Set out a clear strategy for retail participation:** Too many UK savers are not taking advantage of the potential to build their savings and financial resilience by investing in capital markets. Government should democratise the benefits of capital market investing by setting out a long-term strategy to make investing more accessible and attractive to a broader range of individuals, contributing to inclusive growth. The strategy could be framed by three pillars:
    - **Understanding:** A holistic, long-term, UK-wide strategic programme is needed to improve financial literacy and confidence, with clear leadership and adequate resources to widen the societal benefits of investing. The strategy should set out the overarching public policy objectives to guide the coordination of policy and regulatory regimes such as the Advice and Guidance Boundary Review (AGBR), to ensure the provision of effective targeted support for investing.
    - **Incentivisation:** The strategy should rebalance fiscal incentives, particularly those in the ISA regime, to encourage people with adequate levels of cash savings to invest further savings in equities. It should articulate the Money and Pensions Service (MaPS) view[19] that three to six months' worth of living expenses should be held in cash, and that people should consider putting further savings into diversified investment funds that meet their risk appetite.

14 Similar to the Productive Finance Working Group operating on a non-statutory basis, co-chaired by both Regulators and Government, operating for a limited period of time.
15 'quoted' companies are currently excluded. This includes Growth companies.
16 For example, 'quoted', 'unlisted', 'growth market shares' etc.
17 Section 138K of FSMA explicitly requires the PRA (and FCA) to consider how proposed rules may impact mutual societies differently from other types of firms. The same requirement should be considered for the needs of Growth markets, as a different type of trading venue.
18 noting they do not include a geographical restriction.
19 https://www.moneyhelper.org.uk/en/savings/types-of-savings/emergency-savings-how-much-is-enough

- **Facilitation:** Taking inspiration from other jurisdictions, the UK should work with our industry to consider where technological innovations could be adopted to empower retail investors to invest in local growth companies. For example: (i) institutional-level data and analysis tools, or AI-enabled 'robo advisors', to support confident, well informed and considered decision-making; (ii) clear pathways[20] for first time investors, to guide them towards suitable entry-level investment opportunities. The government should also focus on the supply of investment opportunities by ensuring that regulatory regimes that govern the issuance of equity and the offer of financial instruments to potential investors do not discourage retail investor access, and that steps are taken to encourage issuers to include retail investors.

9. **Be a world-leader in the development of tools to innovate and digitise UK markets:** The government should build on the UK's excellence as a centre for technology, by supporting the adoption of key technologies such as AI and distributed ledger technology (DLT) across UK capital markets. Technology-driven efficiency gains could reduce costs and allow more companies to participate in the markets, unlocking their growth potential. Consideration could be given to the current Retail Service Provider (RSP) Model, to ensure it provides a modern and effective way of executing retail investor orders and providing liquidity and price discovery.

10. **Encourage catalytic capital to remain in the UK:** It should be easier and more attractive for a UK company to raise further funding in UK Growth Markets, or graduate to a UK Main Market, than to seek funding via markets outside the UK. Additional admission requirements could be removed for companies that have been admitted to a UK Growth Market and have demonstrated an appropriate level of maturity from both a financial and corporate governance perspective. Government should ensure that a move into the Growth Markets does not cause a loss of fiscal incentives. The Mid-Market Council should include a focus on preparing companies for Growth Markets. Public markets could work in unison with the Growth Markets Industry Group on that objective.

20 Barclays, Empowering retail savers to engage with investing

Conclusion

If the UK fails to nurture our important Growth Markets, it will limit access to capital for UK growth companies with ambitions and potential to scale up, inadvertently sending jobs, tax revenues and talent overseas. This would harm communities up and down the country and reduce opportunities for individuals and institutions to generate returns from investing in the UK. It would also constrain the ability of innovative startups to fund expansion and deliver products and services that could generate wider economic and social benefits to the UK and create jobs. Ultimately, failure to act will impact the UK's competitiveness and capacity in emerging technologies and other sectors crucial to the its growth and resilience.

As the UK's revolutionary listing regime changes start to have an impact, a pipeline of UK-based companies are moving through their maturity cycles and preparing to take the next step on their growth journey. To harness their potential and the positive impacts for the economy and society, government must act swiftly to ensure public markets - particularly Growth Markets - can continue to compete and evolve to support companies across the country to grow, develop and remain in the UK.

The health of the UK's Growth Markets is the collective responsibility of all those who engage with them. TheCityUK stands ready to support the government and regulators in boosting the enabling role that Growth Markets can play across the UK economy.

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