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POST DEMUTUALIZATION AND FINANCIAL PERFORMANCE OF NIGERIAN EXCHANGE LIMITED (NGX)

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Abstract

The study focuses on evaluating the financial performance of the Nigerian Exchange Limited (NGX) following its demutualization. The study utilizes secondary data obtained from the published financial statements of the Nigeria Exchange Limited -NGX in the first and second years after demutualization. The study was based on a longitudinal research design, and key financial performance indicator ratios related to liquidity, leverage, efficiency, profitability, and market value are computed and analyzed for both the first year (2021) and the second year (2022). Descriptive analysis and independent sample t-tests are conducted to test the hypotheses. The study concluded that there is no significant difference between the mean values of the NGX financial performance in the first year (2021) and the second year (2022) post-demutualization. This conclusion is supported by the insignificant mean difference of 0.68700 between the financial performances of the two periods and a p-value of 0.616 at a significance level (α) of 0.05 revealed by the study. Based on this conclusion, it is recommended that stakeholders and potential investors interpret the financial ratios alongside other critical factors such as future industry opportunities and the governance structure of the Nigerian Exchange Limited. Taking these additional considerations into account will lead to a more comprehensive understanding of the overall financial prospects of the company. Additionally, the study suggests that the government should closely monitor the performance of the NGX and implement effective policies that stimulate its financial performance, considering its impact on the GDP growth of the Nigerian economy.

Keywords: Demutualization, Nigerian Exchange Limited, NGX Group,

Introduction

The global economy has experienced significant mayhems, characterized by instability influenced by political divisions among nations. These incidents have amplified uncertainty, resulting in adverse effects on economic growth. In response, stock markets worldwide are undergoing adjustments to enhance their efficiency and provide improved services to stakeholders. Nigeria, as an emerging economy, has

also encountered new economic circumstances, prompting investors and market operators to seek alternative approaches.

Recognizing the substantial impact of stock markets on GDP growth, both developed and developing nations have prioritized strengthening their stock markets. Traditionally, Nigeria viewed a mutual stock exchange as an institution that promotes national interests. However, aligning with the prevailing trend

of demutualization which has become crucial to ensure stability, address liquidity issues, and mitigate financial downturns. Demutualization would enhance security measures, mitigate risks, and provide protection against potential financial shocks.

Researchers and writers have extensively studied stock market demutualization and its potential benefits globally, as many exchanges have already undergone this transformative process. Their studies have highlighted the advantages of demutualization, such as improved market efficiency, transparency, and competitiveness.

In 2015, The Nigerian Stock Exchange has recognized the need for demutualization and embarked on the long-term objective of converting its corporate structure from a non-profit, mutually owned organization to a shareholder-based, profit-making company. The Demutualization of The Nigerian Stock Exchange Bill was enacted into law in August 2018, resulting in the formation of Nigerian Exchange Group Plc (Non-operating Holding Co), Nigerian Exchange Limited (Operating Exchange), NGX Regulation Limited (Regulatory Company), and NGX Real Estate Limited (Property Company). After receiving a 'No Objection' to demutualization from the Securities and Exchange Commission (SEC) in December 2019, the NSE's members unanimously agreed to the necessary resolutions at the Court Ordered Meeting and Extraordinary General Meeting held in March 2020. In March 2021, The Nigerian Stock Exchange successfully completed its demutualization process, obtaining statutory approvals from the SEC and Corporate Affairs Commission (CAC).

The completion of the NSE's demutualization has generated enthusiasm among the Exchange's leadership, existing investors, and potential investors. They firmly believe that the NGX Group will undergo a rapid transformation into a financially robust entity, strategically positioned to capitalize on new income opportunities and display improved governance, technological prowess, and financial performance. This transformation is expected to significantly contribute to Nigeria's economic growth and provide enhanced support. (NSE, 2019). In line with these

developments, this paper aims to assess the post demutualization financial performance of the Nigerian Exchange Group by evaluating the key financial performance indicators: Liquidity, Leverage, Efficiency, Profitability and Market Value ratios.

The global economy has been hit by significant shocks in this 21st century, resulting in a period of heightened turbulence. These disruptions, partly due to financial fragmentation among countries, have led to unprecedented levels of uncertainty, hence negatively impacting economic growth.

In 2019, the Nigerian economy experienced sluggish GDP growth, with a growth rate of 2.27%. This can be attributed to reduced private consumption and cautious investor behaviour in economic and capital market investments. Consequently, macroeconomic conditions in Nigeria, combined with prevailing market factors, had a substantial effect on the country's primary stock exchange. The NSE All Share Index (ASI) witnessed a decline of 14.60% points, closing the year at 26,842.07 points. However, according to NSE annual reports (2020), the NSE ASI rebounded, gaining 50.03% and becoming the best-performing index in the world, reaching 40,270.72 points. Similarly, the equity market capitalization increased by 62.42%, closing at N21.06 trillion.

On the other hand, writers, experts, and literature emphasize that demutualization, despite inevitable challenges, is driven by various factors such as the need for improved governance, increased capital opportunities, revenue growth, technological advancement, improved financial performance, and a strengthened governance structure. These factors in still confidence among stakeholders and position the NGX Group as a profit hub entity capable of capitalizing on new income opportunities and supporting Nigeria's economic growth. By restructuring the business into a more agile and customer-focused entity, demutualization becomes essential for future competitiveness and the growth of Nigeria's global financial markets.

As the NSE completes its demutualization, the leadership of the Exchange, along with existing and

potential investors, strongly believes that the NGX Group has been transformed into a profit hub entity that is well-positioned to seize new income opportunities and better contribute to Nigeria's economic growth (NSE, 2019). Khatun (2018) posited that the stock exchange is considered an institution that serves the nation's interests. Tahir (2013) similarly observed that establishing a new business entity by merging and developing economies is a complex endeavor, with attracting investors proving even more challenging than the actual creation process. In a demutualized stock exchange, shareholders' main objective is to maximize profits, while management should prioritize delivering exceptional customer service and enhancing shareholders' wealth. As a result, management decisions should be centered on the financial performance of the stock exchange and ultimately serve the interests of its owners (Aggarwal, 2002; Hughes and Zargar, 2006). Demutualization can be beneficial for stock exchanges as it allows them to improve their performance through various means. These include adopting modern technology, enhancing the responsiveness and flexibility of the governing body to market signals, preventing broker monopolies, ensuring better decision-making processes, and ultimately increasing the value for shareholders (Aggarwal, 2002; Lee, 2002; Morsy and Rwegasira, 2010). But to avoid instability, liquidity and other financial ratios it is the demand of time to implement demutualization of stock exchanges. With The Nigeria Exchange Group (NGX) successfully publishing two years of post-demutualization annual reports, this paper aims to assess the post demutualization financial performance of the Nigerian Exchange Group by evaluating the key financial performance indicators: Liquidity, Leverage, Efficiency, Profitability and Market Value ratios.

The objective this paper is to assess the two years (2021&2022) post demutualization financial performance of the Nigerian Exchange Group. The paper focused on answering the research question, is there any significant difference between the two years post demutualization financial performance of the NGX Group? While the hypothesis set for the study is.

H₀: there is no significant difference between the two years post demutualization financial performance of the NGX Group.

Literature Review

Demutualization of Securities Exchanges

The process of demutualization, which involves transforming a mutually owned company into a shareholder-owned entity, has gained prominence in the global financial landscape. This transformation requires regulatory approvals, the conversion of membership rights into equities, and the issuance of shares through an initial public offering (IPO) (Hammad, Awan & Rafiq, 2015). Demutualization ultimately leads to the reassignment of control rights and residual claims among shareholders, resulting in demutualized firms with public limited liability status (Fulton & Girard, 2015).

The concept of demutualization originated in 1993 when the Stockholm Stock Exchange transformed from a non-profit organization to a profit-oriented entity (Sial & Talib, 2015). Since then, demutualization has gained widespread acceptance worldwide, with various prominent exchanges like the Australian Stock Exchange, Bombay Stock Exchange (BSE), London Stock Exchange, and New York Stock Exchange adopting this conversion. In Kenya, the process of demutualization for the Nairobi Securities Exchange (NSE) began in 2005. The driving factors behind this decision were commercial viability, increased competitiveness, improved governance, agility in responding to market needs, bolstered capital base, and a reduction in conflicts of interest (Rydzewska, 2015). The main focus of this study is to assess the impact of demutualization on the financial performance of the NSE post demutualization. However, it is essential to note, as pointed out by Khatun (2018), that demutualization is not a singular concept and can take various forms, with experiences differing significantly across the globe.

Financial Performance

Performance serves as a fundamental measure of an organization's effectiveness in achieving its goals and

objectives within a specified timeframe. It can be assessed through both financial and non-financial measures. Financial measures, such as return on assets, return on investment, return on equity, and profitability, are quantitatively expressed and are integral to the existence of profit-oriented firms (Ubochioma, 2016). Similarly, Non-financial measures, on the other hand, are primarily qualitative and subjective. They encompass factors related to people and the environment. People-related measures include employee morale, customer satisfaction, and loyalty. Environmental measures evaluate the impact of an organization's operations on its surroundings and are often documented in sustainability reports (Yang & Pangastuti, 2016). Also, Demutualization can lead to the formation of publicly listed or privately held demutualized companies. Going public through an IPO enables demutualized companies to raise capital for profitable investments, thus influencing their financial performance. Davis (2016) asserts that demutualization increases trading volume in stock exchanges, enhancing competitiveness, flexibility, and governance, which in turn directly impact financial performance.

Studies have explored the relationship between demutualization and financial performance. Azzam (2010) found that demutualization improves organizational efficiencies and effectiveness, positively influencing financial performance in stock markets. Similarly, Magadi, Muza, and Kandiero (2015) established a positive relationship between demutualization and the financial performance of firms. However, Hammad, Awan, and Rafiq (2015) discovered that the announcement of demutualization had mixed effects, both positive and negative, on the financial performance of stock markets. These findings indicate the existence of a relationship between demutualization and performance, which this study aims to explore further. According to Crystal Partners (2023), Earnings Per Share (EPS) is a critical metric that offers valuable insights into a company's profitability. To calculate EPS, one divides the net earnings of a company by its outstanding shares of common stock. This ratio provides a simple and easily

understandable way to assess a company's ability to generate profits for its shareholders and evaluate its overall financial health. For investors, EPS serves as a useful tool to make informed decisions when considering investment opportunities. A higher EPS indicates that the company is generating more significant earnings, making it a more appealing investment prospect. Hence, another important metric discussed is the Price to Earnings (P/E) ratio, which helps assess the relative value of a stock and its attractiveness as an investment. The P/E ratio is calculated by dividing the stock price by the earnings per share. Investors use this ratio in conjunction with other factors to make well-informed investment decisions. A high P/E ratio suggests that investors are willing to pay a premium for each dollar of earnings, possibly indicating an overvalued stock. On the other hand, a low P/E ratio may suggest that the stock is undervalued, potentially presenting a favorable investment opportunity. However, it's important to note that solely relying on the P/E ratio to make investment decisions may not always result in a good investment. *The Return on Equity (ROE)*, ratio evaluates a company's profitability and its efficient use of shareholder investments. The ROE (Return on Equity) ratio is an essential indicator used to gauge a company's ability to generate returns from shareholder capital. By understanding a company's ROE, investors can gain insights into its profitability and efficiency in generating returns, helping them make informed investment decisions based on the company's financial performance. ROE is calculated by dividing the company's net income by its shareholder's equity. A higher ROE usually indicates a well-performing company. On the other hand, Return on Assets (ROA) is a financial ratio that measures a company's profitability in relation to its total assets. It provides valuable information for corporate management, analysts, and investors, enabling them to assess how effectively a company utilizes its assets to generate profits. ROA is typically expressed as a percentage and is calculated by dividing a company's net income by its average total assets. A higher ROA suggests that the company is more efficient and productive in utilizing its balance sheet to generate profits.

According to Hargrave (2022), a lower ROA indicates that there is room for improvement in utilizing assets to generate profits. Lindow (2013) suggests that ROA can also be determined by dividing a firm's EBIT (Earnings Before Interest and Taxes) by its total assets. Regardless of the exact formula used, ROA remains a widely-used measure for evaluating the profitability of a company's operations, assessing its ability to generate profits relative to its asset base, and serving as a reliable indicator of its financial performance..

Demutualization and Financial Performance of Stock Exchanges

Demutualization can lead to the formation of a self-listed public company or a demutualized private company. In the case of a demutualized company, it has the option to become publicly traded through an initial public offering (IPO), which can generate capital for funding profitable investments and ultimately contribute to improved performance. As highlighted by Davis (2016), demutualization has the potential to enhance the trading volume of a security exchange. It also brings about improvements in competitiveness, flexibility, and governance of institutions, all of which directly impact performance. According to Azzam's (2010) study, the process of demutualization in a stock market has been found to enhance efficiencies and effectiveness within the organization. The study highlighted a positive influence of demutualization on the financial performance of the stock market. Similarly, in a study conducted by Magadi, Muza, and Kandiero (2015), it was found that demutualization had a positive impact on the financial performance of firms. On the other hand, Hammad, Awan, and Rafiq (2015) conducted a related study and discovered that the announcement of demutualization had a mixed effect, with both positive and negative impacts on the financial performance of stock markets. These findings suggest that there is a relationship between demutualization and performance, which the present study aims to investigate.

Theoretical framework

This study utilizes four theoretical frameworks to conduct a thorough examination of how demutualization affects the financial performance of the Nigerian stock exchange. The theoretical frameworks incorporated in this analysis consist of the Theory of the Firm, Transaction Cost Theory, Agency Theory, and Stakeholder Theory.

The Theory of the Firm posits that the primary objective of a company is to maximize profits. In the context of demutualization, the decision of a stock market to undergo this process is driven by the aim of generating profit and improving overall performance, aligning with the principles outlined in the theory of the firm (Morsy, 2010).

Transaction Cost Theory emphasizes the concept that firms exist to lower transaction costs, thereby increasing trade volume and creating more value. Demutualization is seen as a means of lowering transaction costs indirectly and, in turn, improving financial performance (Mwangi, 2018).

Agency Theory suggests that conflicts of interest can arise between different stakeholders within an organization. In the context of demutualization, the theory helps explain the shift from a mutual structure to a shareholder-based structure. Demutualization aligns the interests of shareholders with the goal of maximizing financial performance, addressing potential conflicts (Mwangi, 2018).

Stakeholder Theory emphasizes the importance of various stakeholders in the success of an organization. Demutualization can have an impact on different stakeholders, including shareholders, investors, market participants, and the broader economy. Evaluating the interests and perceptions of these stakeholders in relation to the financial performance of the Nigerian stock exchange is crucial for a comprehensive analysis (Haataja, 2020).

Methodology

Research Design

This research paper adopts a longitudinal research design, which enables a comprehensive examination of the company's performance trends over time and yields valuable insights into its evolution from one year to another. The data for this study was sourced from the statement of financial position and the statement of comprehensive income of NGX for the years 2021 and 2022, representing the first and second years post-demutualization. The method of data analysis utilized

in this study encompasses descriptive statistics and independent t-tests. Specifically, the data used for analysis was extracted from the published annual reports of The Nigerian Exchange Group for the two years following its demutualization, namely 2021 and 2022. The study primarily focuses on two key financial performance indicators for each category, namely Liquidity, Leverage, Efficiency, Profitability, and Market Value ratios. These ratios are calculated and analyzed meticulously to provide valuable insights into the company's financial performance during the chosen time period.

Table 1: The study variables and measurement

Indicators	Ratio	Measurement	Source
Liquidity ratios	Current ratio	Current assets / Current liabilities	Olayinka & Muspha, (2022)
	Acid-test ratio	Current assets – Inventories / Current liabilities	Olayinka & Muspha, (2022)
Leverage ratios	Debt to equity ratio	Total liabilities / Shareholder's equity	Khalifa <i>et al</i> , (2022)
	Interest coverage ratio	Operating income / Interest expenses	Khalifa <i>et al</i> , (2022)
Efficiency ratios	Asset turnover ratio	Net sales / Average total assets	Khalifa <i>et al</i> , (2022)
	Receivables turnover ratio	Net credit sales / Average accounts receivable	Khalifa <i>et al</i> , (2022)
Profitability ratios	Return on assets ratio	Net income / Total assets	Khalifa <i>et al</i> , (2022)
	Return on equity ratio	Net income / Shareholder's equity	Khalifa <i>et al</i> , (2022)
Market value ratios	Earnings per share ratio	Net earnings / Total shares outstanding	Khalifa <i>et al</i> , (2022)
	Price-earnings ratio	Share price / Earnings per share	Khalifa <i>et al</i> , (2022)

Source: Researcher's compilation, 2023

The financial ratios mentioned serve as valuable tools for assessing different aspects of a company's financial health and performance. *Liquidity ratio*: The current ratio provides insight into a company's ability to meet its short-term obligations by using its current assets. Similarly, the acid-test ratio focuses on quick assets, emphasizing the company's ability to settle short-term liabilities without relying on inventory. *Leverage ratio*: The debt to equity ratio helps determine the

balance between a company's total debt and financial liabilities compared to its shareholders' equity. It provides an indication of the company's financial leverage and risk. *Efficiency ratio*: The interest coverage ratio sheds light on the company's capacity to meet its interest expenses, indicating its ability to handle debt obligations. On the other hand, the asset turnover ratio evaluates how effectively a company generates sales from its assets, highlighting its

operational efficiency. Additionally, the accounts receivable turnover ratio quantifies the frequency of converting receivables into cash, reflecting the effectiveness of the company's credit and collection policies. *Profitability ratio*: The return on assets and return on equity ratios measure the efficiency of utilizing assets and equity, respectively, to generate profit. These ratios provide valuable insights into a company's profitability and the returns it generates from its investments. Lastly, the earnings per share ratio reveals the net income earned per outstanding share, providing a measure of profitability on a per-share basis. *Market value ratio*: The price-earnings

ratio compares a company's share price to its earnings per share, helping investors gauge the market's valuation of the company. Overall, these ratios offer a comprehensive view of a company's financial performance and aid in making informed decisions regarding investment and financial management.

Discussion of Result

Using the first year (2021) and second year (2022) published financial statements; the table below presents the computed key financial performance indicator ratios with discussion and interpretation, thus;

Table 2: Nigerian Exchange (NGX) Group Financial performance

Financial Performance Ratio	2022	2021	Shift
Current ratio	0.36	2.84	-2.48
Acid-test	0.36	2.84	-2.48
Debt to equity	0.55	0.11	0.44
Interest coverage	-0.63	-	-0.63
Asset turnover	0.11	0.15	-0.04
Receivables turnover	0.45	0.17	0.28
Return on assets	0.01	0.06	-0.05
Return on equity	0.02	0.07	-0.05
Earnings per share	0.35	1.13	-0.78
Price-earnings	13.1	0.44	12.66

Source: researcher's computation, 2023

The financial performance ratios of the Nigerian Exchange (NGX) Group for the years 2022 and 2021 paint a mixed picture. The liquidity ratios, including the current ratio and acid-test ratio, experienced a significant decline in 2022, indicating a decreased ability to cover short-term liabilities with current and quick assets. The leverage ratios showed a notable increase in the debt to equity ratio, suggesting that the NGX Group has taken on more debt relative to its equity, potentially increasing financial risk. However, the interest coverage ratio improved from 2021 but remained negative in 2022, indicating ongoing challenges in covering interest expenses. In terms of efficiency, the asset turnover ratio declined slightly,

while the receivables turnover ratio improved, suggesting a mixed performance in generating sales and converting receivables into cash. Profitability ratios, including return on assets and return on equity, saw a decrease, indicating a decline in profitability relative to assets and equity. The market value ratios showed a decrease in earnings per share, but a significant increase in the price-earnings ratio, suggesting a shift in market valuation of the NGX Group's shares.

Overall, these changes reflect a varied financial performance index for the NGX Group during the specified period 2021 to 2022 post demutualisation,

signalling both areas of improvement and challenges that need attention.

Table 3: Group Statistics

	Years	Mean	N	Std. Deviation	Std. Error Mean
Ratio	First year of demutualization (2021)	1.4680	10	4.10089	1.29682
	Second year of demutualization (2022)	0.7810	10	1.13402	0.35861

Source: Researchers' computation, 2023

Table 3 presents the group mean and standard deviation results for key financial performance ratios of the NGX Group in the first year (2021) and the second year (2022) following demutualization. The analysis demonstrates that the mean value of financial performance in 2021 is 1.4680, surpassing the mean value of 0.7810 observed in 2022. Furthermore, the standard deviation of financial performance in 2021 is 4.10089, compared to the standard deviation of 1.13402 in 2022.

These findings indicate that the financial performance ratio was stronger and more appealing to stakeholders in the first year after demutualization when compared to the second year of 2022. A higher mean value

signifies a more favourable overall financial performance, while the higher standard deviation in 2021 suggests a broader range of variability in the data points, potentially reflecting greater financial growth opportunities or risks.

Consequently, these results imply that the NGX Group exhibited a robust financial performance in the initial year of demutualization, rendering it more attractive to stakeholders. However, the financial performance in the second year, as indicated by the lower mean and standard deviation, may have experienced a decline or lower growth rate in comparison to the preceding year and this may not be unlinked stabilization challenges of the post demutualisation.

Table 4: Independent Samples Test

Measures	Mean difference	Std. difference	Error t	Sig. (2-tailed)
Values	0.68700	1.34539	0.511	0.616

Source: Researchers' Computation, 2023

Table 4 presents the results of independent sample t-tests and their corresponding significance levels for the variables examined in the study. Prior to this, it was observed in the table that the means and standard deviations of NGX Group's financial performance were higher in the first year of 2021 compared to the second year of 2022. However, the significance values determine whether this difference is statistically significant, providing a test of the study's hypothesis.

The null hypothesis of the study asserts that there is no significant difference in the financial performance of the NGX Group between the two years following demutualization. According to Table 4, the probability

value (p-value) for the financial performance of the NGX Group is 0.616, exceeding the significance level of 0.05 at a 95% confidence interval. This suggests that there is no statistically significant difference between the mean values of the financial performance in the first year (2021) and the second year (2022) post-demutualization.

Consequently, the study fails to reject the null hypothesis. Therefore, this study found that there is no significant difference between the mean values of the NGX Group's financial performance in the first year (2021) and the second year (2022) post-demutualization.

Conclusion and Recommendation

The objective of this study was to evaluate the financial performance of the Nigerian Exchange Group during the two years following demutualization (2021 and 2022). Analysis of the results and hypothesis testing indicate that there is no significant difference in the financial performance between these two years. The ratios examined in the study exhibit consistent patterns, showing positive and negative trends during these years, as presented in Table 2. This finding suggests that the financial performance of the Nigerian Exchange Group in the first year (2021) is comparable to that of the second year (2022), with no statistically significant differences observed in the mean values of the ratios.

Based on this conclusion, it is recommended that stakeholders and potential investors should interpret the ratios in conjunction with other crucial factors, such as future industry opportunities, market opportunities, global visibility and the governance structure of the Nigerian Exchange Group. These additional considerations will provide a more comprehensive understanding of the company's overall financial prospects. Additionally, the policy implication of this study is that the government should closely monitor the performance of the NGX Group and implement sound policies that can stimulate its financial performance, taking into account its connection to the GDP growth of the Nigerian economy.

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