Raising Capital in the Securities Market

COVID-19 has given rise to financial challenges among several small and medium-sized local enterprises and conglomerates. During this period of economic uncertainty, raising capital may seem daunting but it is one of the most critical aspects of building a successful business and is likely to be required at several stages of a business's life cycle. Over the next three weeks the TTSEC will be discussing the concept of raising capital in the securities market. This information may be timely since, in the current circumstances, companies may be seeking access to funding to, among other reasons:

- Augment capital after a period of economic decline/loss;
- Finance necessary organisational restructuring;
- Fund infrastructure that facilitates increased remote working or social distancing requirements;
- Fund mergers and acquisitions based on available opportunities; and
- Fund start-ups as the 'new normal' may create opportunities for new greenfield businesses or activities.

As businesses seek to raise capital for various purposes, it is important that entrepreneurs understand all of their available options to ensure that their capital requirements are met as cost-effectively as possible. The various options available to companies to raise financing include Bank loans, Angel and Venture Capital and the Capital Market.

There are a number of advantages and disadvantages associated with each option. For instance, **Bank loans** may incorporate restrictive covenants, they generally offer shorter repayment terms and repayment obligations represent a fixed draw on cash flow. On the other hand, the loan approval process may be speedier than other fund-raising options, the processing costs are generally lower and this funding option does not normally commit the borrower to public disclosure of financial and corporate information.

Are you familiar with the term Angel and Venture Capital? Angel investors, sometimes known as business angels, are individuals who invest their personal finances in a start-up entity owned by another individual or company. Venture capital firms, on the other hand, invest money into companies with the objective of earning profits from a successful business venture and, ultimately, capital appreciation after take-out. For reasons that are unclear, **Angel and Venture Capital** initiatives have suffered from a paucity of Angel Investors and a still-born Venture Capital Market in Trinidad and Tobago. However, Angel and Venture Capital funding can connect the business to an engaged investor, more likely to understand its model and activities and therefore more likely to provide patient capital. Because of the built-in investor take-out requirement associated with both funding options, Angel and Venture Capital financing provide a good take-off base for a transition to the Capital Market.

The **Capital Market** is a marketplace that facilitates the raising of debt and equity funding by companies and the buying and selling of financial securities. Capital Markets allow for more direct interface between the investor to the investee/borrower through the issuance and investment in securities, whereas, in the bank markets, banks act as the intermediary between the saver and user of capital. Dependent on the type of security floated, access to the Capital Market may be costlier when compared to traditional sources of financing when legal and other costs; and the costs of maintaining ongoing disclosure requirements, are factored in. Additionally, investors and investees/borrowers are exposed to variations in security values due to market volatility, which may restrict market access for investees during bearish cycles.

However, financing via the Capital Markets can be an attractive and superior means of raising funding that can complement or even replace the traditional sources of financing. In some developed and developing markets, the Capital Market is deeper than the traditional banking sector and therefore the size of successful Issues can be larger due to market capacity. For successful investees, Capital Markets can offer better pricing and longer maturities, as well as access to a wide investor base. Some projects that require funding, in particular the non-traditional, "new normal" projects, that may not meet the credit hurdles of traditional banking, may be ideal candidates for Capital Market funding. These would include Security Issues that connect sector-specific investors with investees, e.g., environmentally sustainable projects or Fintech initiatives. These projects can contribute significantly to economic development and innovation, but may not see the light of day in the absence of a properly functioning Capital Market.

The securities market of Trinidad and Tobago provides options for entrepreneurs to raise capital/funds. These options include the issuance of securities (mainly through Equities and Bonds), and the issuance of a Limited Offering.

Equities - A company seeking to list on the Trinidad and Tobago Stock Exchange ("TTSE") for the first time can raise capital via an Initial Public Offering ("IPO"). A currently listed company can raise additional capital via Rights Issues. In addition to cash offers, share for share offers can be used to fund acquisitions of other companies and internally as a performance incentive for employees. Equity/shares represent ownership interest in a corporation mainly in the form of ordinary/common stock or preferred stock.

- ***Ordinary or Common Stock*** - A Common Stock is a security representing a unit of ownership in a company. It gives the stockholder (shareholder) the right to vote at the company's Annual General Meetings(AGMs) and a proportionate claim on any dividends declared, after preference shareholders. As owners of the company, common shareholders assume the risk (up to the value of their shareholding) and returns associated with a business and vote to elect the Board of Directors of the company.
- ***Preferred Stock*** - Preferred stockholders enjoy priority over the common stockholders with respect to the payment of dividends and the distribution of assets in the event of dissolution of the company. Preferred stockholders generally do not have a right to vote at the company's Annual General Meetings.

Bonds - A debt investment in which an investor loans money to an entity (corporate or governmental). The funds are borrowed for a defined period of time at an agreed interest rate. Bonds are traditionally used by companies and governments to finance a variety of projects and activities. As an alternative to Bonds, Notes can also be issued by companies to obtain funding. A Note is a formal legal undertaking from a borrower to a lender or to an investor. Notes typically obligate issuers to repay to the creditor the principal advanced plus the agreed interest, at a predetermined date or dates.

Limited Offering – This is a distribution of securities by a "government entity" or "private issuer" where those securities will be distributed to less than 35 persons (excluding employees or former employees of the issuer and its affiliates), where there are restrictions on the transferability of those securities and where there is no general marketing of the securities being distributed. Funds raised from Limited Offerings can be used for a number of strategic purposes within a business.

What role does the TTSEC play?
The mission of the Trinidad and Tobago Securities and Exchange Commission ("TTSEC") is to protect investors and promote and enable the growth and development of the securities industry by nurturing fair, efficient and transparent securities markets, cooperating with other regulators and mitigating systemic risk. No security shall be distributed or listed with any securities exchange in Trinidad and Tobago (i.e. Trinidad and Tobago Stock Exchange) unless it is registered with the TTSEC. The TTSEC registers all securities issued in the securities market of Trinidad and Tobago inclusive of all Equities and Bonds. Where the securities being distributed are part of a Limited Offering, the Securities Act, 2012 provides for an exemption from registration of the issuer as well as the securities. However, issuers of Limited Offerings must adhere to certain regulatory requirements which the TTSEC ensures are observed.

Diagram 1 below displays securities approved by the TTSEC for the period 2018 and 2019. Based on this information, Bonds/Debt securities consist of the largest category of security issued over the last two years (The bulk of Bonds were issued by the Government of Trinidad and Tobago). In next week's article, the processes involved in registering Issuers and securities will be discussed in further detail.

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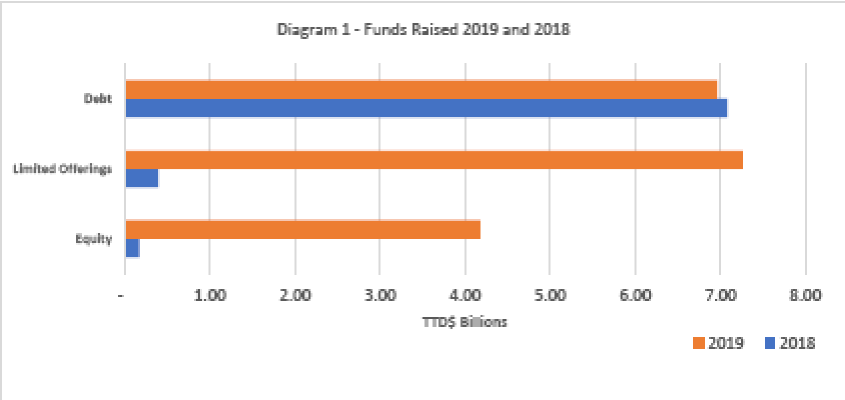
Funds Raised 2019-2018



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