

# Stock Market Development In The United Kingdom: Prospects And Challenges

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## ABSTRACT

*This paper highlights the origin and development of the U.K. stock market. The country consists of one major stock market, known as the London Stock Exchange, which is one of the world's largest stock markets. Stock market reforms have been implemented since the Big Bang of 1986 and the Exchange responded positively to most of these reforms, but not so positively to others. As a result of the reforms, the U.K.'s stock market has developed, in terms of market capitalisation, the total value of stocks traded and the turnover ratio. Although the U.K. stock market has developed over the years, it still faces wide-ranging challenges, such as the uncertainties that come with new regulation and regulatory changes dominating at both domestic and international levels and the sovereign debt crisis that has left the U.K. stock market volatile.*

**Keywords:** United Kingdom; London Stock Exchange; Stock Market Growth; Stock Market Capitalisation

## INTRODUCTION

Stock markets provide market liquidity that enables the implementation of long-term projects, thereby promoting a country's economic growth (Levine, 1991; Bencivenga, *et al.*, 1996). The key role of stock market liquidity in economic growth is further supported by Yartey and Adjasi (2007) and Levine and Zevros (1998), who argued that, overall, stock markets provide market liquidity that enables the implementation of long-term projects with long-term payoffs, thereby promoting a country's economic growth. They further argued that efficient stock markets not only avail resources to investors, but they also facilitate the inflow of foreign financial resources into the domestic economy and they promote risky, entrepreneurial investments through their risk-sharing and monitoring functions.

Stock market development is an important component of financial sector development as it supplements the role of the banking system in economic development (Goldsmith, 1969; Boot and Thakor, 1997). Specifically, stock markets assist in price discovery, liquidity provision, reduction in transaction costs, and risk transfer. They reduce information costs through the generation and dissemination of information on firms, thereby leading to efficient markets in which prices incorporate all the available information (Yartey and Adjasi, 2007). Stock markets have proved to lower the cost of mobilising savings, thereby facilitating investments into the most productive technologies (Greenwood and Smith, 1996). Obstfeld (1994) shows that international risk sharing through internationally integrated stock markets improves resource allocation and accelerates growth. Even the most recent studies have reinforced the vital role stock markets play in economic development (Bolbol *et al.*, 2005; Odhiambo, 2011). The role of the stock market in the development of an economy can, therefore, not be overemphasised.

The U.K. stock market is one of the most highly developed stock markets in the world. There is one major stock exchange in the U.K. – known as the London Stock Exchange, established in 1801 where the trade in stocks and shares, among other capital market instruments, takes place. Despite the presence of a highly developed banking sector in the U.K., its stock market plays an important role in the process of economic development in various ways, including the mobilisation of domestic savings to bring about the reallocation of financial resources from dormant to active agents and the enhancement of the inflow of international capital.

Despite the undisputed role of the stock market in the economic growth process of the U.K., research on the country's stock market is scant (Handa and Khan, 2008; Fraser and Oyefeso, 2005). This paper, therefore, aims to put the U.K. stock market in the limelight by highlighting the origin and growth of the stock market in the U.K. since the establishment of the London Stock Exchange in 1801 through to 2011.

## **THE ORIGIN OF THE STOCK MARKET IN THE UNITED KINGDOM**

Although there are other exchanges in the U.K. that specialise in various trades – for example, the London International Financial Futures and Options Exchange (LIFFE), which is a futures exchange based in London; the London Metal Exchange, which is an exchange for futures contracts and options on base and other metals; and the Baltic Exchange, which is a membership organisation at the heart of the global maritime marketplace that provides independent daily shipping market information, maintains professional ship-broking standards and resolves disputes. The London Stock Exchange (LSE) is the main stock exchange of the United Kingdom where stocks, bonds, and other financial instruments are sold on a day-to-day basis. The LSE utilises telecommunication and electronic resources to accept and execute trades. The Financial Times Stock Exchange (FTSE) 100 Share Index (or "Footsie") is the dominant index of the LSE. It has two equity markets - the Main Market and the Alternative Investment Market where international stocks are traded (LSE, 2012a).

The London Stock Exchange was founded in 1801 and is located in the City of London in the United Kingdom. As of December 2011, the Exchange had a market capitalisation of US\$3.332 trillion, making it the fourth-largest stock exchange in the world and the largest in Europe (World Federation of Exchanges, 2012). The Exchange is part of the London Stock Exchange Group.

The London Stock Exchange is one of the world's oldest stock exchanges and can trace its history back more than 300 years. Starting life in the coffee houses of 17<sup>th</sup> century London, the Exchange quickly grew to become the city's most important financial institution. Over the centuries that followed, it has consistently led the way in developing a strong, well-regulated stock market and today lies at the heart of the global financial community (LSE, 2012a).

In 1698, the earliest evidence of organised trading in marketable securities in London began to show as John Castaing began to issue a list of stock and commodity prices called "The Course of the Exchange and other things". During the same year, stock dealers were expelled from the Royal Exchange for rowdiness and they started to operate in the streets and coffee houses nearby, in particular, in Jonathan's Coffee House in Change Alley. Twenty-two years later, the stock traders encountered a wave of speculative fever known as the "South Sea Bubble" bursts (LSE, 2012a).

In 1761, a group of 150 stock brokers and jobbers formed a club at Jonathan's Coffee House to buy and sell shares. In 1773, the brokers erected their own building in Sweeting's Alley, with a dealing room on the ground floor and a coffee room above, briefly known as "New Jonathan's". However, members soon changed the name to "The Stock Exchange" (LSE, 2012a).

On 3 March, 1801, the business reopened under a formal membership subscription basis. On this date, the first regulated exchange came into existence in London and the modern Stock Exchange was born. A year later, the Exchange moved into a new building in Capel Court. In 1836, the first regional exchanges opened in Manchester and Liverpool. In 1854, the stock exchange was rebuilt and in 1876, a new Deed of Settlement for the stock exchange came into force (LSE, 2012a).

The Great War in 1914 meant that the exchange market had to be closed from the end of July until the new year. During this time, the Stock Exchange Battalion of Royal Fusiliers was formed – 1,600 volunteered and 400 never returned. In 1923, the Exchange received its own Coat of Arms with the motto "Dictum Meum Pactum" (My Word is My Bond). In 1939, the start of World War II saw the Exchange closing for six days, only to be reopened on 7 September. In 1945, the floor of the house closed for only one more day due to damage from a V2 rocket – trading then continued in the basement (LSE, 2012a).

In 1972, Her Majesty, the Queen, opened the Exchange's new 26-storey office block with its 23,000 square foot trading floor. A year later, 11 British and Irish regional exchanges amalgamated with the London Exchange. In 1986, the market was deregulated, known as the "Big Bang". Under the big bang, ownership of member firms by an outside corporation was allowed; all firms became brokers/dealers able to operate in a dual capacity; minimum scales of commission were abolished; individual members ceased to have voting rights; trading moved from being conducted face-to-face on a market floor to being performed via computer and telephone from separate dealing rooms; and the Exchange became a private limited company under the Companies Act of 1985. Five years later (1991), the governing council of the Exchange was replaced with a Board of Directors drawn from the Exchange's executive, customer and user base. The trading name became "The London Stock Exchange" (LSE, 2012a).

In 1995, the London Stock Exchange launched AIM, its international market for growing companies. Two years later, the Stock Exchange Electronic Trading Service (SETS) was launched to bring greater speed and efficiency to the market. The CREST settlement service was also launched in the same year. In 2000, the LSE transferred its role as U.K. Listing Authority with HM Treasury to the Financial Services Authority (FSA). Shareholders voted to become a public limited company - London Stock Exchange plc. In July 2001, LSE listed on its own main market. In 2003, the LSE created EDX London, a new international equity derivatives business, in partnership with OM Group. The LSE also acquired Proquote Limited, a new generation supplier of real-time market data and trading systems. A year later, the Exchange moved to a brand new headquarters in Paternoster Square, close to St Paul's Cathedral. In 2007, the LSE merged with Borsa Italiana, creating the London Stock Exchange Group (LSE, 2012a).

Today, the London Stock Exchange is at the heart of the global financial market and is home to some of the largest, most successful and dynamic companies in the world. The Exchange has been built on a long history of integrity, expertise and market knowledge to become the world's most international stock exchange. The Exchange is the most international of all the world's stock exchanges, with around 3,000 companies from over 70 countries admitted to trading on its markets (LSE, 2012a).

The LSE has the main market and a secondary market called the AIM. The London Stock Exchange's Main Market is the world's most international market for the listing and trading of equity, debt and other securities. Its location at the heart of the world's leading financial centre makes it the ideal home to over 1,600 companies from 60 countries, including many of the world's largest, most successful and most dynamic companies (LSE, 2012a). Underpinned by London's balanced and globally-respected standards of regulation and corporate governance, the Main Market represents a badge of quality for every company listed and traded on it and an aspiration for many companies worldwide (LSE, 2012a). It offers the lowest cost of capital to issuers (LSE, 2012a).

The AIM is the London Stock Exchange's international market for young and growing companies. AIM provides an ideal environment for these ambitious businesses to access the capital and liquidity of the London markets – one of the largest and deepest pools of international capital in the world. AIM's unique regulatory framework is based around balancing the flexibility a growing company needs. Businesses from all over the world continue to be attracted to AIM. In August 2012, over 1,100 companies from numerous countries and sectors were on the market and a total of £79 billion had been raised since AIM's launch (LSE, 2012a).

The U.K. stock market is regulated by the Financial Services Authority, which sets the standards that the market must meet and can take action against firms and stock exchanges if they fail to meet the required standards (Financial Services Authority "FSA", 2012a).

## **STOCK MARKET REFORMS IN THE UNITED KINGDOM**

The U.K. stock market underwent various forms of reforms. The Big Bang of 1986, which saw the deregulation of the U.K. stock market, marked the commencement of a chain of serious reforms (Yadav and Pope, 1990; Peel *et al.*, 1993; Chambers, 2009). The deregulation took various forms, including the abolition of fixed commission charges and of the distinction between stockjobbers and stockbrokers on the London Stock Exchange and the change from open-outcry to electronic, screen-based trading, enacted by the United Kingdom Government in 1986. The day the London Stock Exchange's rules changed – 27 October, 1986 – was dubbed the "Big Bang"

because of the increase in market activity expected from an aggregation of measures designed to precipitate a complete alteration in the structure of the market.

In the U.K., the Big Bang became one of the cornerstones of the then government's reform programme. Prior to these reforms, the once-dominant financial institutions of the city of London were failing to compete with foreign banking. While London was still a global centre of finance, it had been surpassed by New York and was in danger of falling further behind. The government claimed that the two problems behind the decline of London banking and stock exchanges were over-regulation and the dominance of elitist networks and that the solution lay in the free market doctrines of unfettered competition and meritocracy.

The effects of Big Bang were, however, dramatic, with London's place as a financial capital decisively strengthened to the point where it is arguably one of the world's most important financial centres, even to the present day (Peel *et al.*, 1993; Chambers, 2009). An economic boom created a new class of nouveau riche that has persisted for two decades and the boom expanded beyond the city of London. Deregulation stimulated financial innovation and enabled new entrants to provide services (Chambers, 2009).

The stock market reforms also encompassed reform of the stock market regulatory landscape, leading to the formation of a single regulatory body for the financial sector - the Financial Services Authority - in 1997 (FSA, 1997). The chancellor of the Exchequer announced his decision to merge banking supervision and investment services regulation into the Securities and Investments Board (SIB) on 20 May, 1997. The SIB formally changed its name to the Financial Services Authority in October 1997 (FSA, 1997).

The first stage of the reform of financial services regulation was completed in June 1998 when responsibility for banking supervision was transferred to the FSA from the Bank of England. In May 2000, the FSA took over the role of the U.K. Listing Authority (UKLA) from the London Stock Exchange. The Financial Services and Markets Act, which received Royal Assent in June 2000 and was implemented on 1 December, 2001, transferred to the FSA the responsibilities of several other organisations; namely, the Building Societies Commission, the Friendly Societies Commission, the Investment Management Regulatory Organisation, the Personal Investment Authority, the Register of Friendly Societies, and the Securities and Futures Authority. The government's decision to establish a single regulator for the full range of financial business provided an important opportunity to enhance the regulatory system in ways which benefited firms, consumers and investors (FSA, 1997). However, in June 2010, the chancellor announced the government's intention to replace the FSA as a single financial services regulator with two new successor bodies and to restructure the U.K.'s financial regulatory framework (FSA, 2012).

In 1999, the LSE ran the Share Aware campaign, which was launched in London to encourage more people to consider equity investment. In the same year, the LSE went ahead with demutualisation. The Exchange announced its plans to move from mutual ownership to a new basis of owning its shares. The change was designed to equip the Exchange's business more appropriately to meet the competitive demands of the electronic market place (LSE, 2012a). In 1999, the London Stock Exchange also announced the launch of a new market for technology companies – techMARK. The new market brought together London-listed companies involved in leading edge technologies, creating a central focus for investors. Streamlined rules provided a wider range of young, innovative growth companies with access to the U.K. equity market. The new market went live in November 1999, linking companies from across the main market – ranging from the FTSE 100 to the FTSE Fledgling. It marked a new approach to stock market investment, uniting companies that share common attributes – in this case, a commitment to technological innovation. This 'attribute approach' was particularly beneficial to smaller companies which gained from the increased visibility of being grouped with their peers (LSE, 2012a).

During the late 2000s, the Listing Regime was reviewed with the purpose of ensuring that there is greater clarity of the regime's structure and the obligations on issuers under it. This was done so that investors can make more informed investment decisions and for issuers to have appropriate flexibility over how they would like to raise capital. Changes to the Listing Regime made, effective from 6 April, 2010 include: 1) restructuring the regime into two segments - Premium and Standard - where Premium indicates the more stringent super-equivalent standards and Standard indicates European Union (EU) minimum standards (Companies were able to migrate from one listing

segment/category to another without the need for cancellation and relisting.), 2) strengthening the corporate governance standards for overseas companies by requiring overseas companies with a Premium listing of equity shares to ‘comply or explain’ against the U.K. Combined Code and to offer pre-emption rights, 3) requiring overseas companies with a Standard listing of shares or global depository receipts (GDRs) to comply with the EU Company Reporting Directive which required them, amongst other things, to provide a corporate governance statement and to describe their internal control and risk management systems’ main features, and 4) making the Standard listing segment, which was then only for overseas companies, available to U.K. companies – effective from 6 October, 2009 – to provide a level playing field (United Kingdom Listing Authority “UKLA”, 2012).

On 8 July, 2009, the HM Treasury published its long-awaited White Paper titled “Reforming Financial Markets” (the “White Paper”). The White Paper was part of a comprehensive review by the U.K. government of U.K. financial regulation and supervision, which has been on-going since the outbreak of the global financial crisis in 2007 and the ensuing turmoil in the U.K. financial markets.

As such, it provided the U.K. government’s formal response to the proposed actions recommended in the Turner Review titled “A Regulatory Response To The Global Banking Crisis” released on 18 March, 2009 (the “Turner Review”), which sets out in-depth analyses of the causes of the financial crisis and identified a number of key areas requiring regulatory reform.

The White paper also enhanced the FSA’s powers, granting it greater rule-making, information-gathering and enforcement powers – for example, suspension or penalisation of individuals or firms – in order to address not only market or consumer risks but also systemic risk. The Financial Services and Markets Act of 2000 was also amended to give the FSA continuing power to impose emergency short-selling restrictions (HM Treasury, 2009).

In 2010, a number of stock market disclosure requirements were updated to improve transparency to the public, investors and potential investors (LSE, 2012a). Changes applied to Short Selling disclosures and the new disclosure regime from the Takeover Panel. The Takeover Panel announced changes to its disclosure regime with effect from 19 April, 2010. The new rules applied to all offers and possible offers from that date. The new rule stipulated that "opening position disclosures" must be made by any person who is interested in 1% or more of any class of relevant securities of an offeree or offeror company. The new rules required disclosure of positions even if no trades were made during the offer period (LSE, 2012a).

The UKLA issued an update to clarify its interpretation of the Disclosure and Transparency Rules (DTRs) with regard to the production and announcement of the Annual Financial Report. DTR 6.3.5 (1) required issuers to publish regulated information in unedited full text. While the Annual Financial Report (previously known as the Annual Report) was exempt from this, certain key information contained in the report was to be released in full text via a Regulatory Information Service. Issuers were to announce this information no later than when they make the annual financial report public. The annual financial report had to be published no later than four months after the end of each financial year. The annual financial report produced by an issuer had to include at least: 1) audited financial statements prepared in accordance with the applicable accounting standards, 2) a management report, 3) an appropriate statement of assurance from persons responsible in the issue, and 4) provision of an indication from which website the annual financial report is available (LSE, 2012a). This promoted accurate information dissemination timeously to avoid speculation.

To promote the growth and development of the U.K. stock market, the Finance Act of 2012 was passed. The Act extended tax benefits of the companies listed on the LSE AIM by making several key changes to the Enterprise Investment Scheme (EIS) and Venture Capital Trust Scheme (VCTs). These changes include an increase in the limits on the size of qualifying companies to up to 250 employees and gross assets of £15 million, from the previous limits of up to 50 employees and gross assets of £7 million (LSE, 2012b). The maximum annual amount that can be invested through EU State Aided funding, including the Enterprise Investment Scheme and the Venture Capital Trust Scheme in an individual qualifying company, was increased to £5 million. There was also the removal of the £1 million maximum investment limit that any one VCT can invest in a company (subject to a joint venture rule) (LSE, 2012b). The Finance Act of 2012 also brought an increase in the maximum annual amount that an individual can invest through EIS to £1 million. In addition, the government has also introduced a new scheme for

earlier stage businesses. The Seed Enterprise Investment Scheme (SEIS) offers tax reliefs to individuals investing in start-up and early stage companies (LSE, 2012b). Although SEIS is not directly relevant for AIM companies, it forms part of the measures in place to help encourage an effective funding environment for smaller, growing businesses. These changes were effective from April 2012 (LSE, 2012b).

In 2012, in further action to make Britain one of the best places in the world to start, run and grow a business, the government, together with the London Stock Exchange, developed a set of ambitious proposals to attract entrepreneurs and high-growth companies (U.K. Department for Business, Innovation and Skills, 2012). Proposals included a planned new route to the U.K. IPO market for high-growth companies, which is likely to feature reformed rules on free float, eligibility criteria and reporting requirements. This will ensure that the needs of dynamic businesses and their investors are met (U.K. Department for Business, Innovation and Skills, 2012).

### **STOCK MARKET GROWTH IN THE UNITED KINGDOM**

The U.K. stock market responded largely positively to most stock market reforms but not so positively to others. To date, there are more than 500 firms worldwide that trade as members of the London Stock Exchange, while about 2,494 companies are listed on the London Stock Exchange, with a total market value of £3.8 trillion (LSE, 2012a). The growth of the stock market has awarded LSE the honours of being the most international of all stock exchanges, with companies from over 70 countries admitted to trading in their markets (LSE, 2012a).

The number of listed companies on the LSE did not change much over time. From 2895 in 1999, the number decreased to 2,778 in 2000 but bounced back to 2,927 in 2001. Between 2001 and 2004, the number decreased, while it increased between 2005 and 2007, creating a V impression. The number of listed companies reached a peak in 2007, recording 3,305 listed companies. With the global financial crisis, the number of listed companies started its descent in 2008, recording 3,298 before further tumbling to 2,792 in 2009. Since then, listed companies have been on a decrease. Between 1999 and 2012, the highest number of listed companies was recorded in 2006, while the lowest number was in 2012. Table 1 shows the number of listed companies on the LSE during the period 1999 to 2012.

**Table 1: Number Of Listed Companies On The London Stock Exchange (1999-2012)**

|  | 1999  | 2000  | 2001  | 2002  | 2003  | 2004  | 2005  |
|--|-------|-------|-------|-------|-------|-------|-------|
| <b>Number of Listed Companies on the London Stock Exchange</b> | 2,895 | 2,778 | 2,927 | 2,880 | 2,814 | 2,681 | 2,844 |
|  |       |       |       |       |       |       |       |
|  | 2006  | 2007  | 2008  | 2009  | 2010  | 2011  | 2012  |
| <b>Number of Listed Companies on the London Stock Exchange</b> | 3,088 | 3,305 | 3,298 | 2,792 | 2,670 | 2,594 | 2,494 |

Source: London Stock Exchange (2012a)

The number of domestic-listed companies in the U.K. also shows the growth of the U.K. stock market. Between 1988 and 2001, the number of listed domestic companies in the U.K. fluctuated around 2,000, increased to 2,405 in 2002, decreased slightly in 2003 before increasing again in the subsequent year, reaching a peak of 2,913 in 2007. From 2006, the number decreased gradually over the years until it reached 2,001 in 2011 (World Bank, 2012). Table 2 shows the number of listed domestic companies in the U.K. during the period 1988 and 2011.

The London Stock Exchange saw record volumes traded on its international and domestic markets during 1999 – with international business up 10.1% in value and domestic business up 36%. Like many equity markets, London enjoyed buoyant levels of trading in 1999. The continued growth of its international business provided a positive reminder of one of London's key strengths (LSE, 2012c). On the domestic market, the total value of U.K. equities traded during 1999 rose to 1,406.6 billion – up 36% from 1,037.1 billion in December 1998. The total number of U.K. bargains also increased to a record 20,920,000 – up 29% from 16,220,000 bargains in 1998 (an average of 81,644 a day). All the major U.K. FTSE indices set records in 1999. Trading in international equities also showed solid gains. At the end of 1999, turnover value reached 2,403 billion – up over 10.1% from 2,183 billion in

December 1998. The number of bargains increased to a record 7.49 million, up from 7.12 million in 1998 (LSE, 2012c).

**Table 2: Number Of Listed Domestic Companies In The United Kingdom (1988-2011)**

|                                  | 1988  | 1989  | 1990  | 1991  | 1992  | 1993  | 1994  | 1995  | 1996  | 1997  | 1998  | 1999  |
|----------------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| <b>Listed Domestic Companies</b> | 2,054 | 2,015 | 1,701 | 1,623 | 1,874 | 1,646 | 2,070 | 2,078 | 2,171 | 2,157 | 2,087 | 1,945 |
|                                  | 2000  | 2001  | 2002  | 2003  | 2004  | 2005  | 2006  | 2007  | 2008  | 2009  | 2010  | 2011  |
| <b>Listed Domestic Companies</b> | 1,904 | 1,923 | 2,405 | 2,311 | 2,486 | 2,759 | 2,913 | 2,588 | 2,584 | 2,179 | 2,056 | 2,001 |

Source: World Bank Development Indicators (2012)

AIM also saw strong growth in 1999. The value of trading grew to a record 5.26 billion – up 170% from 1.95 billion at the end of 1998. The number of bargains rose to 814,334 – up 261% from 225,494 in 1998. On 13 December, the AIM index reached a new high of 1,872.4 – an annual increase of 133% – making it the best-performing U.K. index during 1999. The new market for technology companies – techMARK – was launched successfully in November. Its two supporting indices - the FTSE techMARK All Share and FTSE techMARK 100 - both showed strong growth. The techMARK 100 Index (which highlights those companies with a market capitalisation of under 4 billion) has grown 60% since the market's launch, making it the best-performing index for technology companies in Europe (LSE, 2012c).

The growth of the U.K stock exchanges can also be portrayed by the number of terminals taking the Exchange’s real-time market data. In 2006, there were 104,000 terminals compared to 95,000 in 2005, representing a 9% growth. Of this total, 88,000 terminals, compared to 83,000 in 2005, were attributable to professional users. SEDOL Masterfile, the extension to the Exchange’s securities numbering service, now provides unique identification for more than a million securities on a global basis, and Proquote, the Exchange’s provider of financial market software and data, increased the number of screens at year-end by 11% - to 3,000 - 300 more than the 2005 figure (LSE, 2006).

In 2010, there were 93,000 professional users accessing London Stock Exchange real time data via the stock exchange’s direct network and also via over 200 network service providers and market data vendor partners (LSE, 2010). While these figures were lower than a year earlier – 104,000 in 2009 – the number of users stabilised in the second half of the year. Although the Exchange expected the financial year that followed to show signs of improvement alongside an economic upturn, the number of professional users accessing real time data remained at 93,000 in 2011 and decreased to 90,000 in 2012 as a consequence of adverse market conditions (LSE, 2012d) The LSE has, however, managed to offset this decline by introducing fees for non-display data licences, taken by customers using trading algorithms, smart order routers or for data used in databases.

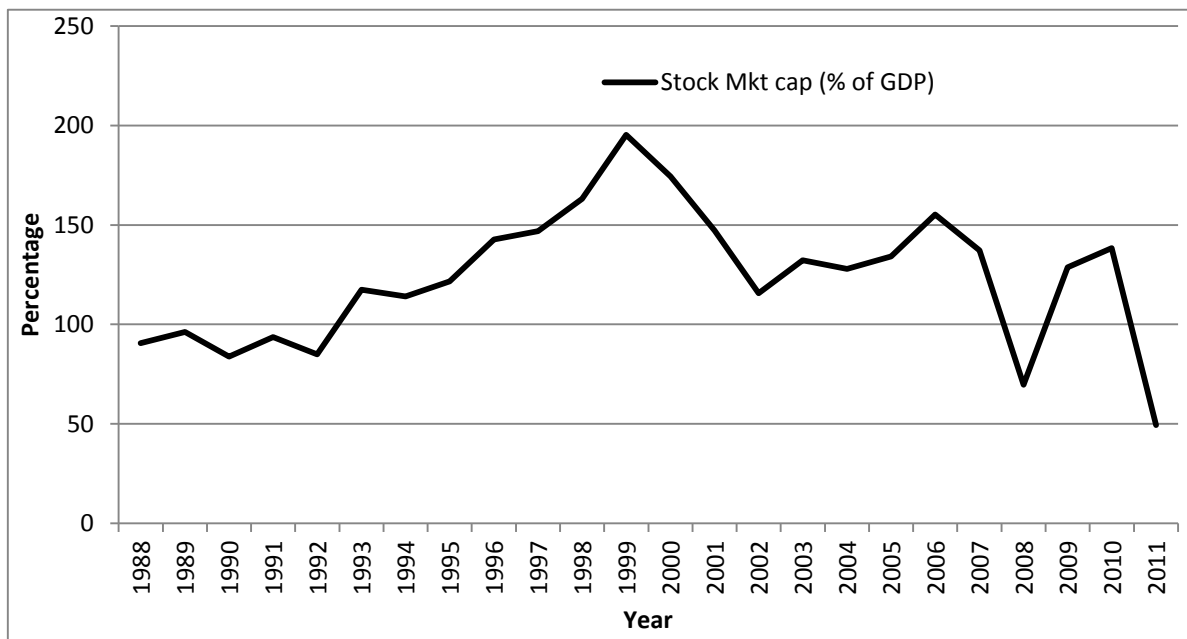
In 2006, companies raised a record £29.4 billion through IPOs on the London Stock Exchange’s markets, with IPO fundraising by companies up 81% from 2005. By the end of December, the total money raised by IPOs on the London Stock Exchange had reached £29.4 billion. The Exchange’s Main Market and AIM attracted IPOs from a total of 367 companies during 2006. During the same year, the Exchange attracted 107 international IPOs from companies incorporated in 26 countries. Among them, these international companies raised £14.0 billion on the Exchange’s markets, of which £2.9 billion was raised on AIM (LSE, 2012c).

During 2007, London’s markets attracted 86 international IPOs by companies from 22 countries (excluding the U.K.). Among them, they raised £14.5 billion. Overall, companies across the Exchange’s markets raised £43.8 billion in new and further issues during the year. This included 252 IPOs on the Main Market, Professional Securities Market and AIM, which raised £26.1 billion in total. An additional £17.5 billion was raised through further issues, including a record £8.6 billion in further issues on AIM. It can, however, be noted that the number of IPOs and the amount raised from IPOs in 2007 were less than those in 2006 (LSE, 2012c).

In 2012, there were a total of 159 new companies listed or admitted to trading on LSE markets, compared to 185 in 2011 (LSE, 2012d). Although the number of IPOs on the LSE has been on a gradual decrease since 2007, the number has been higher than that of some reputable stock markets and much higher than IPOs in developing economies. The global financial crisis and a downturn in economic activities have been the major culprits for this decline.

The growth of the U.K. stock market can also be explained using stock market capitalisation of listed companies, total value of stocks traded and turnover ratio of stocks traded. The stock market size of the U.K., as measured by stock market capitalisation expressed as a percentage of GDP, was growing at a slow pace between 1988 and 1992, fluctuating just below 100%, only to increase growth momentum between 1993 and 1999. The stock market growth reached its peak in 1999, registering a market capitalisation of 195.2%, 16.3% more than the U.S.'s peak during the same period. However, the year that followed, the stock market size dwindled sharply, only to improve after 2002, although it failed to reach its 1999 size. In 2007, the U.K. stock market suffered another blow, which saw the market capitalisation tumbling, reaching a low of 69.7% in 2008. Since then, the market has never fully recovered from the aftermath of the late 2000's financial crisis (World Bank, 2012).

In terms of market liquidity, as measured by total value traded/GDP and turnover ratio, the U.K. had a less liquid stock market until 1997, although it was relatively more liquid than other countries' stock markets during the same period. The total value of stocks traded improved from 61% of GDP in 1997 to 126.5% in 2001 to 182.8% in 2005 before further increasing to a peak of 367.3% in 2007, then sharply declined soon afterwards to 246.1% in 2008 and further down to 122.2% in 2011. The turnover ratio depicted the same trend as that of total value of stocks traded, reaching its peak in 2007 at 269.8%, before sharply declining to 227.2% in 2008, 146.4% in 2009, 101.9% in 2010, and slightly increased to 137.9% in 2011 (World Bank, 2012). Figures 1 – 3 track the performance and growth of the U.K. stock market during the period 1988-2011.



**Figure 1: Trends In Stock Market Capitalisation In The U.K. (1988-2011)**  
Source: World Bank Development Indicators (2012)



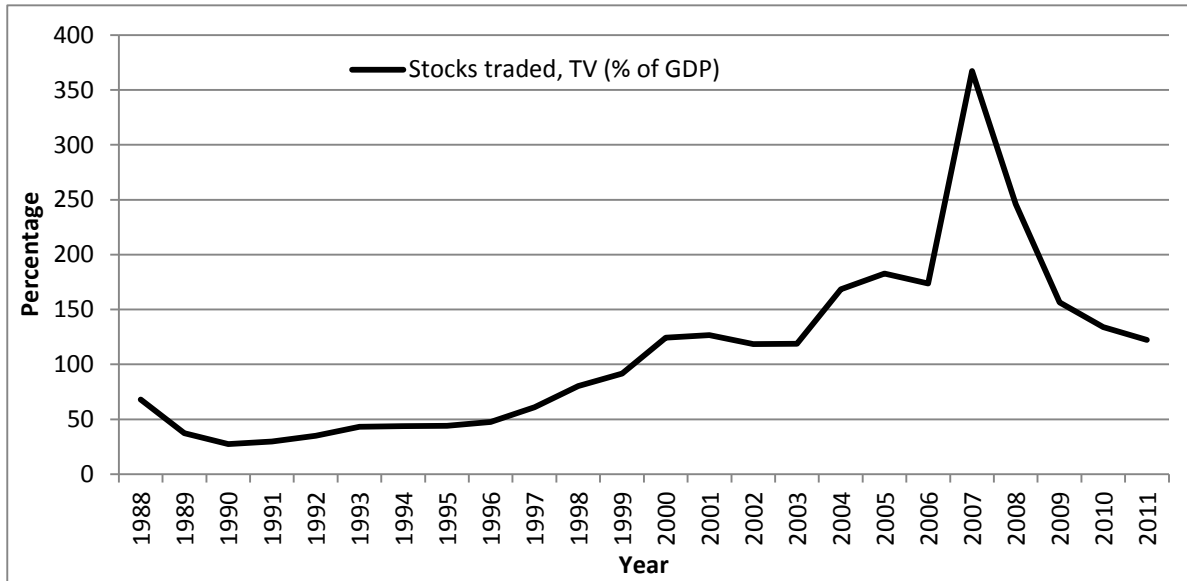


Figure 2: Trends In Total Value Of Stocks Traded In The U.K. (1988-2011)  
 Source: World Bank Development Indicators (2012)

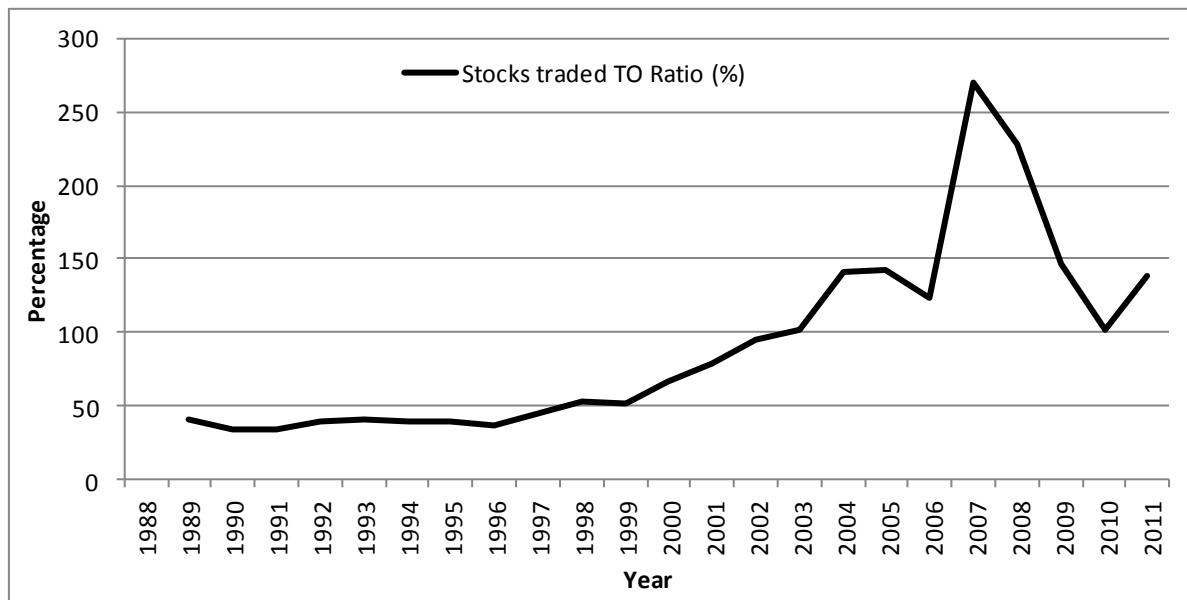


Figure 3: Trends In Turnover Ratio Of Stocks Traded In The U.K. (1988-2011)  
 Source: World Bank Development Indicators (2012)

**CHALLENGES FACING STOCK MARKET DEVELOPMENT IN THE UNITED KINGDOM**

The LSE continues to operate in an environment where new regulation and regulatory changes dominate at domestic and international levels. Although fundamental shifts in the way markets are structured and governed create significant opportunities, they have also created challenges for the U.K. stock market. Although the outcome of all this regulatory change is not clear, the LSE is committed to active engagement and discussion with policy makers around the world, promoting safe, efficient, competitive, innovative and successful stock markets – those in which all participants can thrive (LSE, 2012d).

The U.K. stock market suffers from the challenges that come with the globalisation of financial markets. The globalisation of financial markets has increased rapidly in recent decades. It has become easy for financial firms and markets to operate across borders, which has led to the emergence and importance of large, complex financial institutions operating on an international scale. Although financial integration can bring benefits for financial stability as risk is diversified more widely and as it can increase prosperity as new markets develop, the growing importance of cross-border firms and markets also brings with it challenges for financial stability and for the authorities with responsibilities for it. The scale, complexity and cross-border nature of firms and their activities – straddling national boundaries, legal jurisdictions and supervisory remits – present particular challenges to national authorities in preventing, managing and resolving crises in financial markets, in general, and to the U.K. stock market, in particular. These issues have been highlighted by the financial crisis and have demonstrated the need for strong domestic regulatory systems to be complemented by enhanced supervision of international firms and markets through robust international standards, closer cooperation between authorities, and a more coherent international regulatory architecture (HM Treasury, 2009).

Although opening up operations to the international market/domain is regarded as progress and development of a country's stock market, it has also brought challenges in the U.K. stock market. The openness of the U.K. stock market to the international stage exposes it to greater risks emanating from problems faced by the international stock markets. Thus, volatile international markets lead to volatility of the domestic market.

A slow economic pace in the U.K. has also posed a challenge to the development of the economy's stock market. It has dampened the appetite for new listings and the number of LSE-listed companies has been dwindling of late (see Table 1).

The sovereign debt crisis has also left the U.K. stock market volatile, with the value of U.K. stocks mostly fluctuating as markets across the continent are rocked by a wave of panic selling amid renewed fears about the impact of savage austerity measures in some of the Euro Zone's biggest economies.

## **CONCLUSION**

This paper discussed the origin of the U.K. stock market, the reforms undertaken to develop the market, the growth of the stock market, as well as the challenges facing stock market development in the U.K. The U.K. has one major stock exchange where the trading of stocks takes place, known as the London Stock Exchange. The U.K. stock market is well developed by any standard and is one of the biggest stock markets in the world.

In order to foster stock market development in the country, a number of reforms targeting the stock market have been undertaken over the years. These included the deregulation of the stock market, which took various forms. The stock market reforms also encompassed reform of the stock market regulatory landscape, leading to the formation of a single regulatory body for the financial sector - the Financial Services Authority in 1997. The market responded positively to some of the reforms but not so positively to others. The net effect of reforms, however, has been positive, leading to the development of the stock market over the years.

Although the U.K. stock market has developed over the years, as evidenced by the increasing number of listed companies, stock market capitalisation, the total value and turnover ratio of stocks traded, the market was hit hard by the financial crisis of the late 2000's and, to date, it is still recovering. Some of the challenges still facing the U.K. stock market include the uncertainties that come with new regulation and regulatory changes dominating at both domestic and international levels and the sovereign debt crisis that has left the U.K. stock market volatile.

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