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A more robust sponsor-based regime for Catalist is needed

But taking this route is likely to drive up sponsor fees – and companies listed on Catalist are particularly cost-sensitive. Balancing these two imperatives will not be easy. BY MAK YUEN TEEN AND CHEW YI HONG

LAUNCHED in November 2007, the sponsor-based Catalist board welcomed its first sponsor-approved listing in June 2008, when Mencast Holdings raised S$6.3 million. JK Technology Group was the first SESDAQ company to transfer to Catalist in March 2008.

Over the last 10 years, Catalist listings have outpaced those on the Mainboard. They now account for 30 per cent of all SGX listings, up from 17 per cent in 2010. As at June 2020, 216 issuers were listed on it.

Catalist is modelled after the Alternative Investment Market (AIM) in the UK; sponsors on Catalist are equivalent to nominated advisers on AIM. A Catalist company is required to appoint a full sponsor for its listing and have a continuing sponsor throughout its life on Catalist. The continuing sponsor helps ensure that the Catalist issuer complies with listing rules. While Catalist, like AIM, requires companies to retain a sponsor throughout its entire life on that board, other sponsor-based regimes in HK and Malaysia require only a compliance adviser and sponsor respectively to be appointed for a limited period. Clearly, in the latter cases, the stock exchange regulator will have to play a more active role in monitoring companies.

In an article earlier this year headlined "Sponsors' conflicts symptomatic of a bigger issue" (BT, Feb 11), we highlighted relationships between continuing sponsors and companies they sponsor that may create conflicts of interest, impairing the sponsors' ability to discharge their responsibilities.

Our new report, "Who's sponsoring who? Challenges of the Catalist board", covers these conflict of interest issues in greater detail. It also examines the frequency of changes in sponsor, average duration of relationship, recent trends in sponsor appointment and termination, quality of companies currently sponsored by the major sponsors, and identification of registered professionals responsible for the issuers. Case studies are presented, which raise issues as to whether sponsors are able to adequately discharge their responsibilities. The Catalist rules for sponsors are also compared with those in UK, Hong Kong and Malaysia.

It may be timely to assess how Catalist companies have performed and whether this board is meeting its objectives. Only six companies have made the leap to the Mainboard since 2015. BT FILE PHOTO

CHANGE IN SPONSOR

A Catalist issuer listing directly on Catalist has to retain the full sponsor as continuing sponsor for at least the first three years, after which it can freely choose sponsors and change them as frequently as it wishes. In effect, an issuer is able to pick and change its "frontline regulator", which is the role of the continuing sponsor. Companies that migrated from the previous SESDAQ board or downgraded from the Mainboard to Catalist are not subject to any minimum retention period for their continuing sponsor.

While a company may change sponsor for various reasons, another report has identified a change of Catalist sponsor as a potential warning sign of impending problems. Multiple changes in sponsors and/or a short-lived relationship are more likely to indicate problems with the issuer.

We found that from 2008 to June 2019, 102 out of the 261 issuers included in our study, or 39 per cent, changed their sponsor at least once. Thirty-seven have had at least three different sponsors since their listing on Catalist, with nine having four sponsors and two having five.

For those with at least three sponsors, we examined the length of the relationship with their previous sponsors, excluding delisted companies, companies that transferred to the Mainboard and "forced" changes of sponsors that ceased their sponsorship business altogether. The overall average duration is 38 months. There are several issuers which have stayed with the same sponsor since 2008.

We further looked at the recent trends of termination and appointment of sponsors from January 2018 to July 2020. Excluding delistings, there were 20, 18 and four instances of issuers switching sponsors in 2018, 2019 and 2020 (up to July) respectively. In 2018 and 2019, the percentage of Catalist issuers which changed sponsor was higher than the average annual percentage change since Catalist started.

Of these 42 changes, three sponsors stood out for signing up the most number of issuers – Novus Corporate Finance, ZICO Capital and SAC Capital with nine (21 per cent), eight (19 per cent) and seven (17 per cent) respectively.

Novus Corporate Finance was authorised as a full sponsor only in June 2018, but in just two years, has picked up 29 per cent of the companies that changed sponsors during this period. Meanwhile, PrimePartners Corporate Finance, with about 25 per cent of market share for continuing sponsorship, was relatively inactive in signing up issuers looking for new sponsors.

In fact, PrimePartners has been replaced as sponsor by 12 issuers since January 2018, followed by Stamford Corporate Services with six, and RHT Capital and SAC Capital with five each. Based on recent trends, the newer sponsors are picking up market share aggressively.

Issuers currently sponsored by Asian Corporate Advisors, RHT Capital, Stamford Corporate Services and ZICO Capital underperform the overall median for corporate governance and financial performance indicators; those under CIMB Bank and UOB Bank outperform. However, we caution that this is based on only single-year indicators and we did not consider Novus Corporate Finance, which has recently become active as a sponsor.

The Catalist rulebook requires the annual return lodged by the sponsor with SGX to disclose the names of the Registered Professionals (RPs) involved with each issuer, and those involved in specific transactions. Announcements by a Catalist company must include the full name and contact details of the contact person from the sponsor. However, it is unclear if the contact person named is always a RP involved with the issuer. When an issuer makes an announcement of a change in sponsor, it identifies the outgoing and the incoming RP although any subsequent changes to the RP are not announced.

For the top 10 sponsors, six individuals are currently named as the contact person for 10 or more issuers, with the highest number being 26 issuers, from PrimePartners. For ZICO, the same contact person is named for all 20 issuers currently sponsored by it.

We understand from some sponsors that they name the responsible RP as the contact person. For others such as PrimePartners and ZICO, where one RP is named as the contact person for many companies, it is unclear if that person is indeed the sole RP responsible or one of the RPs involved – or just purely a contact person with no involvement with the issuer. This raises issues of lack of transparency and accountability, or RPs who may be far too busy to adequately discharge their responsibilities.

We believe that SGX should simply require sponsors to name the RP in charge in the announcements. It may also need to review if some RPs are involved in too many companies and whether a limit is necessary.

There are currently 16 full sponsors and four continuing sponsors on Catalist. With 216 Catalist issuers, the ratio of Catalist issuers to sponsors is less than 11. As at January 2019, there were 850 companies on AIM in the UK and 34 Nomads, or a ratio of 25. There is a question of whether there are too many sponsors given the number of Catalist issuers, which may lead some sponsors to look for other work which may lead to conflicts or treat their sponsorship business as ancillary. We believe SGX should be cautious about increasing the number of sponsors, perhaps hoping that more full sponsors will mean more listings.

SUSTAINABILITY OF CATALIST

Based on the 214 Catalist issuers in our study, for which the FY2019 net income is available, 121 out of 214 – or 56.5 per cent – made losses for FY2019. For those listed for under seven years, about 37 per cent made losses; 71 per cent of those listed for more than seven years made losses.

One would expect growth companies to start as relatively unprofitable companies and become more profitable over time. Our analysis is inconclusive, but it may be timely to assess how Catalist companies have performed and whether it is meeting its objectives. Only six companies have made the transition to the Mainboard since 2015, with more Mainboard issuers having transferred to Catalist.

Evidence from AIM has not been positive, as the headline of a 2015 article in *The Financial Times* (June 19, 2015) "Aim – 20 years of a few winners and many losers" says it all. It reported that research by Professors Elroy Dimson and Paul Marsh at the London Business School found that AIM's annualised total return over the two decades from its establishment in 1995 was negative 1.6 per cent a year. Over the 20 years, investors would have lost money in 72 per cent of all companies to have listed on AIM.

Based on the 2,877 companies that have listed on AIM, investors would have lost at least 95 per cent of their investment in more than 30 per cent of the cases. Only 39 companies, or 1.4 per cent, have given investors multi-year returns in excess of 1,000 per cent. With many more losers than winners, they argue that "the people less equipped to sort the wheat from the chaff are private investors, and the people best equipped are the professional fund managers".

A robust sponsor-based regime requires greater transparency in sponsor and non-sponsor fees; stricter restrictions on other work that can be undertaken by sponsors and relationships between sponsors and issuers; and strong safeguards where the fees earned from non-sponsor work by the sponsor or its affiliates are substantial. This is likely to drive up sponsor fees and for companies listing on Catalist, cost is likely an important consideration. The tension between a robust sponsor-based regime and cost of listing is not easy to reconcile.

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