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Are there equity market opportunities for easing access to finance for SMEs with Belarusian shareholders in the EU?

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Abstract

The policy paper reviews opportunities and challenges stemming from worldwide and regional experience of public equity markets for small and medium-sized enterprises (SMEs), such as NewConnect in Poland and Nasdaq First North Baltic, that are relevant for companies with Belarusian shareholders registered in the EU. There is a large number of businesses owned by Belarusians in the EU (at least 8,623 as of January 2024) contributing to the economies of Member States, in particular by creating tens of thousands of jobs (at least 19,400 as of January 2024). Their access to financing through traditional bank lending channels is very restricted, mainly because of their lack of collateral, the sanctions, and the applicants' short credit history. However, there are alternative non-banking ways of funding businesses open for Belarusian entrepreneurs, including crowdfunding, private venture capital, and going public. This paper analyses equity financing through initial public (or private) offerings and trading on organised markets, focusing on markets for SMEs. Although going public requires much effort, can be costly, and is typically suited for young and fast-growing companies, it has a lot of advantages that this paper lists and explains. First of all, it provides a funding alternative to companies that do not currently have access to bank lending at all. Secondly, it broadens companies' funding alternatives (for example through Secondary Public Offerings), and it even opens access to bank lending since listed equity can be a source of collateral. Finally, it enhances companies' governance frameworks, creates value in investor relations, and makes a company more transparent and thereby credible to all types of business partners. The paper refers to the challenges and even drawbacks of IPOs (including costs and complexity), and addresses potential solutions to these problems for companies with Belarusian shareholders. The proposed solutions may have long-term benefits, since they integrate Belarusian entrepreneurs further into the EU economy, strengthen their impact on the hosting economies as well as on the Belarusian diaspora, create a network of companies well established and connected in the West that may be stakeholders of the future economic reforms in Belarus, and enhance the economic transition there.

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ABBA – Association of Belarusian Business Abroad is the biggest association of Belarusian business abroad bringing together more than 120 members from 11 countries from the EU, USA and Canada. ABBA’s goal is to integrate, protect the interests and develop the legal and ethical businesses of entrepreneurs with Belarusian roots for the development of New Belarus as an independent democratic country.

CASE – Center for Social and Economic Research is an independent, non-profit research institute founded on the idea that research-based policy-making is vital for the economic welfare of societies. Established in Warsaw in 1991, CASE today is recognised as the top think tank in Central and Eastern Europe and is one of the most highly regarded think tanks internationally. CASE carries out policy-oriented research and development assistance projects, specialising in the areas of: 1) Fiscal, monetary and financial policies; 2) Sustainable development policies; and 3) Trade, innovation and productivity policies.

Introduction

The private sector emerged as the key driver of protests following the fraudulent presidential election in Belarus in August 2020 (OSCE, 2020), and faced a harsh government response in the aftermath. The political crisis affected many Belarusian private companies in various sectors. According to a survey conducted by the Imaguru Startup Hub and the Coordination Council in October-November 2021,[1] the political crisis led to financial losses for more than 60% of the surveyed businesses. Subsequently, following the Russian invasion of Ukraine on 24 February 2022, the private sector experienced further pressure to relocate from Belarus due to the challenges related to the newly imposed economic sanctions against Belarus. These challenges included: i) the toxicity of Belarusian export-oriented companies, including those in the IT industry, resulting in the loss of western clients and higher operational expenses for existing contracts; ii) significant restrictions related to the Belarusian banking sector that made international payments and settlements to and from Belarus increasingly difficult, risky and expensive; iii) the looming threat of sanctions, posing a material risk to businesses; (iv) western companies implementing supply boycotts against Belarus, leading to a fall in imports, supply chain disruptions, and inflated logistics expenditures; and (v) increasing uncertainty and business costs due to the instability of the Belarusian rouble exchange rate and the reduced purchasing power of consumers in Belarus.

As a result, between August 2020 and June 2022 the cumulative potential of the Belarusian business community in the EU was estimated to have increased by around 4,100 private businesses, varying in scale and legal form (Naŭrodski, 2022). This number covered both complete and partial company transfers, as well as self-employed individuals. Most of them chose to relocate to Poland, Estonia, Lithuania and Latvia.

Responding to the financing needs of these companies, ABBA and CASE have drawn up a series of policy papers aimed at exploring alternative non-bank financing options for businesses with Belarusian shareholders in the EU.[2] The outcome will be solutions involving non-bank debt and equity financing instruments designed to encourage improved risk allocation and risk-taking, thereby supporting the development and growth of young and fast-growing firms with Belarusian shareholders. Insights from these policy papers will be further utilised in discussions with stakeholders involved in Belarusian business support programmes in the EU.

The structure of the review is as follows. The first part discusses why financing poses a problem for Belarusians interested in investing in the EU, while also providing estimates of the investment gap for Belarusian firms in the EU. The second part presents the essence of SME equity markets, outlining how SMEs are represented on the public equity platforms, and examining their key opportunities and challenges. Finally, the third part describes two specific SME equity market solutions, namely NewConnect in Poland and Nasdaq First North Baltic. It offers insights into issues

[1] Survey conducted in October-November 2021, covering 154 companies (the survey is not publicly available).

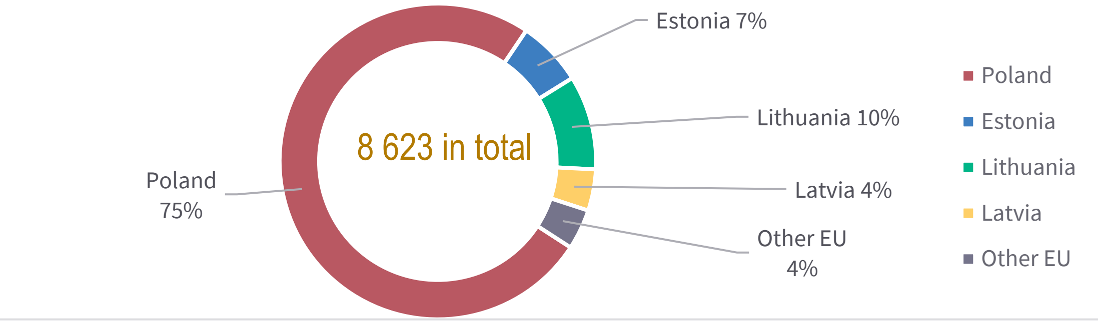
[2] We define a EU business with Belarusian shareholder or Belarusian capital as a EU-based enterprise with at least one shareholder being a citizen of Belarus or a business registered in Belarus. The definition "Belarusian business" in the text refers to a business with Belarusian shareholder registered in one of the EU countries.

that could be relevant for businesses with Belarusian shareholders in the EU. We conclude the review with policy solutions that can potentially be implemented at the EU or national levels.

Problem statement and market gap analysis

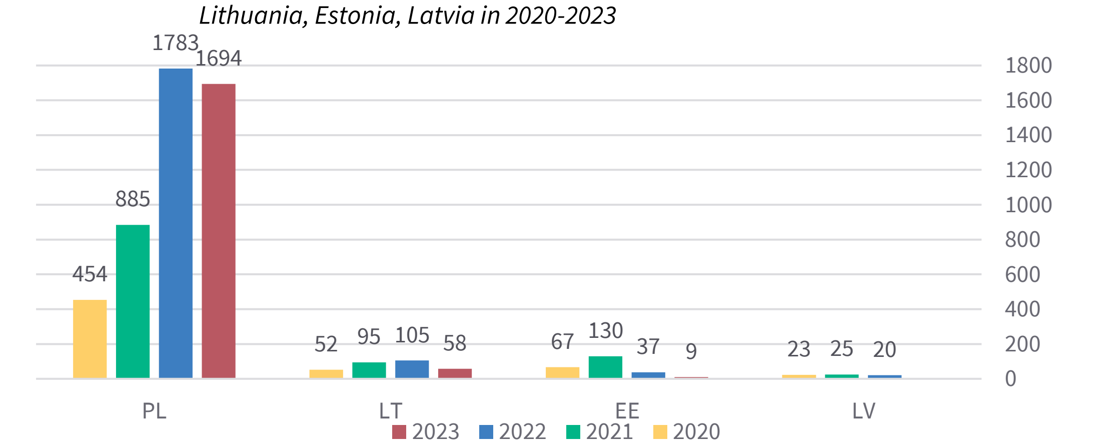
The relocation of Belarusian businesses to the EU continued in 2022 and 2023. According to statistics acquired from open data platforms,[3] as of January 2024 there were at least 8,623 businesses with Belarusian shareholders registered in the EU (excluding self-employment) (Figure 1). Poland, Estonia, Lithuania and Latvia remained the primary destinations for Belarusian entrepreneurs. The number of new registrations was record high in 2022 (Figure 2). In 2023, new business registrations were lower in each of the four key countries, and in Lithuania and Estonia the number of registrations was significantly lower than in 2022 and 2021.

Figure 1. Total number of companies with Belarusian beneficiaries in the EU, as of Jan 2024



Source: open source databases

Figure 2. Number of new business registrations by Belarusians in Poland, Lithuania, Estonia, Latvia in 2020-2023



Source: open source databases

3 Open data is available for Poland (www.coig.com.pl), Estonia, Lithuania, and Latvia (www.okredo.com). When estimating the number of businesses with Belarusian capital in other 23 Member States, we made the assumption that a country's share in the total number of Belarusian firms in the EU is equal to the country's share in the total number of Belarusian immigrants in the EU. We use Eurostat's data for first resident permits in the EU for 2020-2022 as a proxy of total number of Belarusian immigrants in EU countries, and use this proxy to estimate the share of "Other EU countries" (other than Poland, Estonia, Lithuania, and Latvia) in the total number of firms with Belarusian capital in the EU.

Poland, Estonia, Lithuania and Latvia together account for 96% of all firms with Belarusian shareholders registered in the EU. 58% of all businesses were registered in 2020-2023. The enterprises with Belarusian roots in these four key destinations are predominantly micro and small firms (with up to 50 employees) in service sectors. The top 4 sectors in terms of number of businesses are retail, wholesale, transport and construction.

At the moment, the situation of businesses with Belarusian owners in the EU is quite unique compared to businesses registered by immigrants from elsewhere, for six key reasons:

- restrictions related to financial assets[4] which froze the potential collateral that Belarusian citizens in the EU could pledge in exchange for traditional bank funding;
- the severe limitations on bank transfers to and from Belarus due to the financial sanctions imposed by the EU;
- restrictions on Belarusian citizens introduced by the sanctions (the toxicity of the Belarusian passport), which make carrying out formalities in EU countries very troublesome and risky, especially in banking operations, despite Belarus passport holders receiving residence permits in the EU;
- uncertainty regarding the extension of EU legal status, due to some EU countries introducing restrictions on Belarusian nationals, and because of Belarusians being treated in general as a security risk;[5]
- the inability to provide collateral for a loan, often because of a combination of the above factors; this even includes real estate collateral (very common in funding small companies at the launch phase in some parts of the EU[6]), as creditors would not have recourse to it in the event of default; and, finally,
- the individual credit history of applicants with Belarusian passports in the EU is too short to be able to successfully apply for a loan.

Altogether, this significantly complicates investments by potential Belarusian entrepreneurs in the EU, despite their willingness to register new businesses and invest in their development.

Restricted access to finance for SMEs does not come as a surprise, as it is usually a significant growth constraint for small and medium enterprises worldwide.[7] EU evidence indicates, however, that access to finance is reported as the third major concern by euro area businesses (around 25% of firms reported access to finance as a major concern for their business in 2023, down from around 40% in 2012) (European Central Bank, 2023). We therefore assumed that a Belarusian immigrant in the EU would have relatively more restricted access to funding for starting and developing their own business than is the case for a EU citizen.

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[4] In 2022 the EC prohibited the acceptance of deposits exceeding €100,000 from Belarusian nationals or residents, the holding of accounts of Belarusian clients by the EU central securities depositories, as well as the selling of euro-denominated securities to Belarusian clients. Source: https://ec.europa.eu/commission/presscorner/detail/en/ip_22_1649

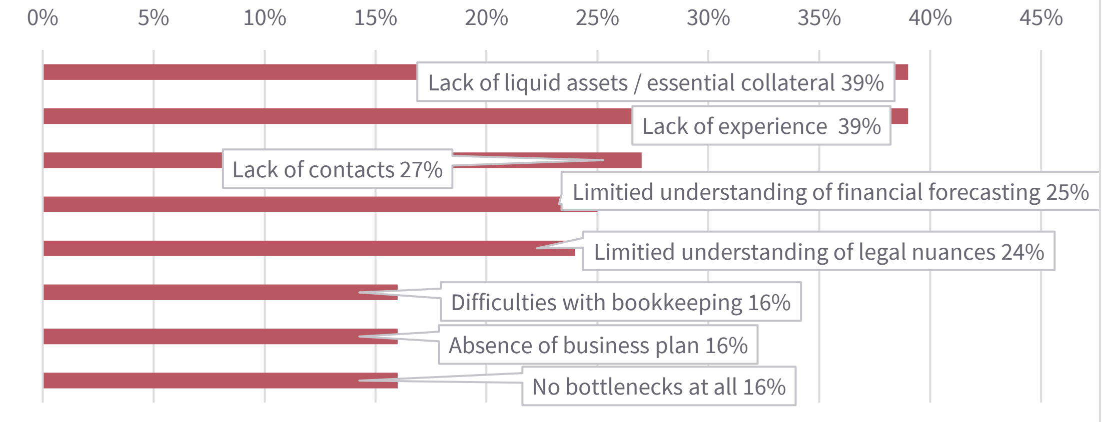
[5] Recent changes in the legislation of Estonia, Latvia, and Lithuania tend to set tougher conditions for holders of Belarusian passports to obtain a visa, residence permit or citizenship, to buy property, or even to drive a car with Belarusian plates.

[6] See, for instance, Banerjee and Blickle (2021).

[7] See, for instance, Beck and Demirgüç-Kunt (2006).

This assumption was studied in the two surveys of businesses with Belarusian shareholders in EU countries conducted in 2022–2023. The first survey of the financial needs of companies with Belarusian shareholders and self-employed Belarusian individuals in the EU in December 2022 – January 2023[8] showed that 80% of the companies expressed the need for a loan in the coming year of operations. Of the companies surveyed, only 18% had previously applied for a bank loan. Of those who had applied, 35% obtained a positive response from a bank. Companies with positive responses were registered between 2012 and 2022, which suggests that the year of registration was not a critical factor for bank decisions. The second survey of Belarusian entrepreneurs, in September – October 2023,[9] revealed a more modest appetite for external financing, and showed that almost every second business (47%) lacked the financial resources needed to develop their business. The key bottlenecks for external financing in the EU countries studied here are lack of liquid assets and essential collateral (answered by 39% of those who indicated a need for external financing) and lack of experience in obtaining external financing (39%) (Figure 3). As a result of the above-mentioned restrictions observed by entrepreneurs from Belarus in the surveyed EU countries, only 17% of all respondents applied to banks for loans in 2022–2023 (similarly to the first survey), while 28% said they planned to apply. The success rate among those who had already applied for a business loan was 24%, while 71% had their applications rejected and 5% were awaiting a decision.

Figure 3. External financing bottenecks for your company



Source: Survey of Belarusian business in the EU, October'23

The survey findings suggest that the unsatisfied demand for bank-based financing for businesses with Belarusian capital ranges between 65% and 75% of the total assessed financial needs. Based on the available statistics and data acquired from surveys, it is difficult to estimate the actual financial requirement among Belarusian enterprises registered in the EU. Simple calculations based

[8] Survey conducted in Dec. 2022 – Jan. 2023, addressed to businesses with Belarusian shareholders and self-employed individuals registered in Poland, Lithuania, and Germany. The responses were controlled for diversity in terms of country and region of registration, annual turnover, number of employees, and sector of operations. In total, 77 responses were collected, 61 (79%) of them were from Poland.

[9] Survey of businesses with Belarusian shareholders in the EU conducted in September–October 2023 by ABBA, CASE, and the Center for New Ideas. 102 Belarusian owners of businesses in the EU were surveyed, and a focus group with 5 owners was conducted. Sample profile: 69% of the respondents were from Poland, 20% from Lithuania, 11% from other EU countries, representing 15 various sectors of the EU economy. The share of micro-enterprises (up to 9 employees) in the survey was 89%, small businesses (11-49 employees) accounted for 8%, and 3% of the businesses were medium-sized (50-249 employees). 71% of the business owners were male, and 68% of all respondents had higher education.

on distribution of the businesses' responses regarding the scale of their requirement and the total number of Belarusian firms in the EU[10] indicate that the total financial need would be a 9-digit number, or in other words over EUR 100 million.

Bearing in mind that there is a market gap in external financing for businesses with Belarusian shareholders in the EU, and the fact that businesses with a Belarusian owner constitute a risky category of borrowers with limited access to liquid assets and essential collateral, there is potential for them to use the equity market instead of debt financing. Poland and the Baltic countries, as the key destinations for Belarusian businesses with well-developed equity markets, could provide capital market opportunities appropriate for SMEs with Belarusian shareholders, and become some kind of a role model of non-debt financing of the existing financing gap to supply a sufficient amount of external financing to SMEs.

[10] We realise that not all EU-registered firms have started operations. Data from the open data platforms show that only around half of the businesses have employees and turnover. We therefore took a threshold of 50% of the total number of businesses to be included in the market size for the calculations.

SMEs and Equity Markets: opportunities and challenges

Are SMEs present on the capital markets?

Access to finance is one of the main issues that SMEs face in the world in general, and in the EU in particular. As reported in a recent ECB study (European Central Bank 2023), nearly one in four SMEs report difficulties in accessing finance. Banks are extremely reluctant to engage in uncollateralised lending to companies, and SMEs in particular. Many SMEs are often unable to provide information on their creditworthiness to banks due to a lack of appropriate accounting records or collateral.[11] The SME financing gap exists as the market is unable to supply SMES with sufficient external financing. This market failure is rooted in the existence of information asymmetries, meaning a situation in which borrowers have better information than their lenders.[12]

Information asymmetry can constitute a bigger problem in the case of SMEs started by immigrants. A recent meta-analysis of the literature on sources of financing among immigrant entrepreneurs (Malki et al., 2020) indicates that the information asymmetry theory in finance is often used to explain obstacles to accessing finance faced by immigrant entrepreneurs.[13] For Belarusian immigrants who relocated to the EU after August 2020, it would seem that their limited access to finance for starting a business is due to information asymmetry. As shown in Chapter 1, SMEs with Belarusian owners or founders are unable to provide a sufficient credit history due to the brief lifespan of their company, they cannot find collateral due to the toxicity of Belarusian capital in the EU, and it is almost impossible for them to transfer cash from their accounts in Belarus to the EU due to sanctions and restrictions. It is challenging, costly, and often impossible for Belarusian immigrants to gather such information and find resources for investment. Many banks and leasing companies in Poland, Lithuania, and other EU countries consider the credit risk particularly high for SMEs with Belarusian origin. What those immigrants are left with is entrepreneurial spirit and ideas to invest in.

To overcome this financial gap, prime stock market operators around the world, national authorities, and several large international bodies such as the European Commission have promoted the development of capital markets in general, including the enhancement of platforms appropriate for SMEs. Such dedicated SME markets or trading segments cater for the specificities of SMEs with financially viable projects that face difficulties in obtaining the required financing from traditional financial institutions and attract investors interested in higher-risk equity investments.

11 Banks assess creditworthiness of SMEs and retail clients by applying their scoring methodologies. Clients provide the information, data and documentation requested by banks so that they can run their credit scoring models. This information is not only restricted to recent revenue but aims at establishing a historical record of a client. For clients with Belarusian shareholders this is often a technical hurdle as they simply do not have sufficiently long records in the EU. Moreover, they do not have eligible collateral or cannot dispose of it as result of the sanctions imposed.
12 See, for instance, Bebczuk (2003).
13 One of the solution to this problem, namely the creation of the guarantee fund at the EU or national level, was discussed in Naŭrodski & Alachnovič (2023).

These are the so-called SME markets, alternative markets, junior stock markets, second-tier stock markets or growth markets, to recall just a few of the terms used.[14] Any of these terms is used to describe a dedicated platform, market segment or exchange with differentiated requirements typically aimed at smaller and younger firms. While these markets have many features in common, there are also differences (see Chapter 3).

It is important to note that alternative markets do not have the legal status of a regulated market. This means that companies listed on alternative markets are subject to the rules of the markets where they are traded, but not the legal requirements for listing or admission to trading on a uniformly regulated stock exchange. In the EU such a market is often reported as a multilateral trading facility (MTF);[15] alternative trading facilities (ATSs) in the US are similar to the European MTFs. See Box 1 for more details.

Box 1. Multilateral trading facilities (MTFs) and SME growth markets

Marketplaces operate securities and derivatives markets traditionally treated as **regulated markets** (together with other Financial Market Infrastructures such as clearing houses or securities depositories) within the meaning of MiFID II[16] as trading venues enabling investors to benefit from being able to trade, clear and settle in a uniform way across various jurisdictions whilst also accessing a broad and deep pool of liquidity. Their traded assets usually include regulated equities, exchange-traded funds, warrants and certificates, bonds, derivatives, commodities, foreign exchange as well as indices.

In addition to the regulated markets, marketplaces also operate **non-regulated markets** that are regarded as **multilateral trading facilities (MTFs)** pursuant to MiFID II. They have their own dedicated listing rules.

MTFs therefore provide retail investors and investment firms with an alternative to traditional exchanges. Some MTFs may have fewer restrictions surrounding the admittance of financial instruments for trading, allowing participants to exchange riskier and potentially less liquid financial instruments.

Some MTFs specialise in the most liquid stocks and crossing trade orders of specialised investment firms. Their popularity in Europe has grown thanks to lower transaction latency, being able to match larger transaction blocks, and most importantly the lower fees and trading incentives. As a result MTFs have come to dominate some market segments. The largest European MTFs include BATS Chi-X Europe, Turquoise, Cboe Europe, and Aquis Exchange. According to the World Federation of Exchanges (WFE), more than 30 exchanges around the world provide dedicated equity market offerings with dedicated listing rules. Euronext, the leading marketplace in Europe, currently operates five MTFs, pursuant to MiFID II, that have their own dedicated rules: Euronext Growth, Euronext Access, Euronext Expert Market, Trading Facility, and Global Exchange Market.

[14] They are also known in the literature under other terms such are the venture exchanges, new markets, SME boards, venues for SME listings, lower-tier markets, junior market segments, etc.
[15] However not all MTFs are SME markets.
[16] MiFID II, a European Union (EU) packet of financial industry reform legislation, came into effect in 2018, designed to protect investors and instil confidence in the financial industry: Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU.

Yet not one of the above MTF examples is an SME market. Article 33 of MiFID II regulates SME growth markets and defines that an MTF operator may apply to its competent home authority to have the MTF registered as an SME growth market. According to Article 33 of MiFID II, an MTF is granted SME growth market status if the following requirements are met:

- at least 50% of the issuers whose financial instruments are admitted to trading on the MTF are SMEs at the time when the MTF is registered as an SME growth market and in any calendar year thereafter;
- appropriate criteria are set for initial and ongoing admission to trading of financial instruments of issuers on the market;
- on initial admission to trading of financial instruments on the market there is sufficient information published to enable investors to make an informed judgment about whether or not to invest in the financial instruments; either an appropriate admission document or a prospectus;
- there is appropriate ongoing periodic financial reporting by or on behalf of an issuer on the market, for example audited annual reports;
- regulatory information concerning the issuers on the market is stored and disseminated to the public;
- there are effective systems and controls aiming to prevent and detect market abuse on that market as required under Regulation (EU) No 596/2014.

Among SME growth markets in Europe there are MTFs such as AIM (London), Nasdaq First North (Stockholm), NewConnect (Warsaw), and Nasdaq First North Baltic (Tallinn, Riga, Vilnius). The last two are described in greater detail in Chapter 3.

Source: Investopedia.com; euronext.com; world-exchanges.org; esma.europa.eu

To understand how these SME markets operate, one needs to be aware that these markets and segments focus mainly on young fast-growing firms that often fall into the definition of SME. This means that not all companies listed on growth markets would necessarily be regarded as SMEs, and not all SMEs are listed on alternative markets. The definition of an SME that can be present on growth markets differs between stock market operators around the world. The two key characteristics of an SME that alternative markets are always interested in are *young* and *fast-growing*. Such companies are often referred to as gazelles. The OECD defines gazelles as follows: "Gazelles are enterprises that have been employers for a period of up to five years, with average annualised growth in employees (or in turnover) greater than 20% a year over a three-year period and with ten or more employees at the beginning of the observation period" (OECD, 2010).

Data show that regulated equity markets are also largely utilised by young, fast-growing companies. Indeed, as the 2015 OECD report shows, in the period 2000-15, the percentage of companies choosing an IPO (Initial Public Offering) path within 3 years of their foundation has been consistently higher (in terms of % of total IPOs) than that of older companies in operation for 15 years or more (Nassr and Wehinger, 2015).

Using the above definition of gazelles, one should treat SME equity markets as equity financing opportunities that are suitable for SMEs rather than a general solution for the SME financing gap that covers risk finance applying to all SMEs. Public equity markets are therefore complementary, not competitive, to bank financing for SMEs. For instance, in a G20/OECD High-Level Principles on SME Financing[17] there is a statement that "Recognising the complementary nature of the role of banks and other financing channels, access to a sufficiently broad range of SME financing instruments is desirable in order to obtain the form and volume of financing best suited to SMEs specific needs and the stage of the firm life-cycle. Multiple and competing sources of finance for SMEs should be supported, and efforts should be made to increase entrepreneurs' awareness of the available financing options through targeted outreach initiatives. The development of alternative financial instruments for SMEs should also aim to attract a wider range of investors, including institutional investors, and to enhance their understanding of SME markets" (OECD, 2018).

Despite its relevance and appropriateness, capital market financing for SMEs remains underdeveloped, both for equity (public listings and equity private placements[18]), and for debt (securitisation, bond issuance, and debt private placements). OECD calculations show that the proportion of IPOs by the segment of small and medium firms in the total number of listings has dropped in terms of percentage from the mid-70s prior to the 2008–2009 financial crisis to the mid-50s thereafter (OECD, 2015).

At the same time, the share of SME financing provided through equity markets is currently very small. The most recent data from ECB show that the share of Euro area SMEs using equity financing is currently around 3%, and this has remained unchanged since 2015 (ECB, 2023).

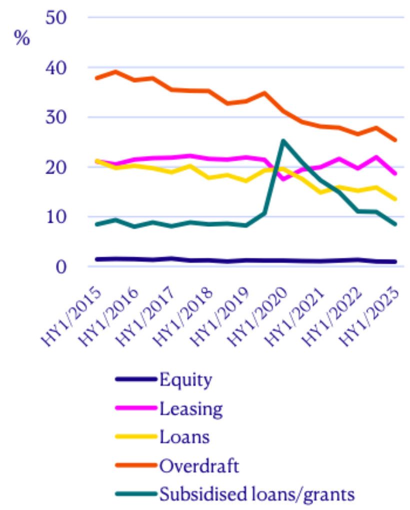


Figure 4: Share of Euro area SMEs using…

Source: ECB, 2023

Opportunities and advantages

Alternative markets can help SMEs avoid certain constraints associated with bank financing and the information asymmetries discussed above, and SMEs can then focus on sources of long-term financing that do not require repayment. As Šestanović (2016) puts it, equity financing increases SMEs' capacity to carry more debt financing on their balance sheets.

According to Pagano et al (1998), listing a company on a stock exchange offers a number of broader opportunities. We highlight three key benefits. First of all, it provides existing shareholders with a means for exiting the firm. Secondly, listing enhances the profile and prestige of the firm among potential employees, suppliers and clients. A public offering also facilitates the use of company shares for future acquisitions through the valuation process.

17 G20/OECD High-Level Principles on SME Financing were developed by the OECD, together with other relevant international organisations at the request of G20 Finance Ministers and Central Bank Governors (OECD, 2018).
18 A private placement is a sale of stock shares or bonds to pre-selected investors and institutions rather than publicly on the open market. It is an alternative to an initial public offering or public listing for a company seeking to raise capital for expansion.

Being listed on a public market brings several specific financing opportunities for SMEs. The WFE (2017) argues that the cost of equity capital can be lower than other forms of finance if there is access to a wider potential investor base. In the longer perspective, once listed, follow-on or secondary offerings would be easier to make.

Moreover, stock exchange financing has certain long-term benefits beyond the initial access to capital. According to Nassr and Wehinger (2015), it increases and diversifies the investor base, and increases SMEs' visibility and credibility associated with corporate governance standards. Public accountability, and the increased transparency and reporting implicitly or explicitly required by the markets, encourage better management practices, governance, and monitoring of performance. The requirements in terms of transparency and disclosures to investors and other stakeholders do incur costs, but they bring about significant improvements in processes, in the management framework, and in the company's risk culture. The management of a listed company quickly learns the important nuances of the legal and corporate systems they operate within. In addition, a listed company becomes better known to other market actors, its business partners, and even potential clients. Over time, being listed (conditional on some form of economic success) also opens more channels and alternatives for financing the company's further growth. Finally, it paves the way for listing on the main stock exchange. In the longer perspective, being a listed SME allows owners to realise their capital gains while enhancing the capital structure of their company and managing the costs of their capital.

One more opportunity related to the public equity market is that it can complement Private Equity (PE) and Venture Capital (VC) funding for start-ups, as well as equity and debt crowdfunding. Public equity offerings serve as important technical exit avenues for PE and VC investors, and provide opportunities for further rounds of capital raising rather than a complete exit.

Nassr and Wehinger (2015) make an important point that equity financing extends the investor base of a company, as it enables the purchase of company shares by both retail investors and institutional investors. Companies thereby have improved access to risk management instruments, and the risk can be distributed more efficiently. Gurrola-Perez, Lin and Speth (2022) argue that institutional investors may bring stability through long-term holdings, while retail investors are a source of liquidity. The WFE recently investigated the share of retail and institutional investment in SME markets across jurisdictions; their analysis was based on a survey of stock exchanges belonging to the WFE.[19] The majority of respondents (75%) reported retail accounting for over 70% of overall volumes in SME markets. The WFE research team concluded that the retail share of SME markets is higher than in the main markets, and that the number of SME markets with a high share of retail participation has increased.

The key practical advantage of alternative markets is their relaxed admission criteria compared to regulated markets. SME markets around the world offer more flexible listing criteria, less stringent disclosure requirements, and comparatively low admission costs in terms of legal and advisory fees, while their free float and investor dispersion requirements are also less strict. Table 1 provides key differences between SME markets and main markets.

19 https://focus.world-exchanges.org/articles/investor-types-sme-markets

Table 1 : Key differences between SME markets and main markets

SME board	Main market
Less extensive rulebook; usually regulated under rules of market operator, i.e. self-regulated	Strictly regulated by national securities (capital market) laws (and in EU relevant MiFID directives)
Publication of *information memorandum* (simpler than prospectus)	Obligatory publication of *prospectus*
Mandatory partners usually required (listing sponsor, certified adviser, market maker/liquidity provider)	Obligatory participation of investment company; on certain markets involvement of other agents and sponsors may be mandatory
Simpler and faster admission procedure and listing requirements; reduced administrative and procedural burden	More restrictive admission requirements and higher administrative and procedural burden
Less strict information requirements	Stricter information requirements
Lenient reporting requirements	Stricter ongoing reporting requirements
Shorter financial history and lower accounting standards	Longer financial history and higher accounting standards
Sometimes government tax incentives & other subsidies	Generally no government incentives
Smaller investor base with institutional and retail investors (on certain markets retail investors prevail)	Broad investor base, suited for regulated institutional investors such as pension funds, insurance companies, and other types of collective investment schemes
Perceived higher investment and liquidity risk	Perceived lower investment and liquidity risk
Aimed at potentially high-growth companies in the start-up or early stage (short track record), seeking to raise relatively smaller amounts (from few hundred thousands to a few millions euros)	Aimed at companies at an advanced stages of development, seeking to raise higher amounts of capital (from few million up to a few billion euros)
Firms operating in innovative sectors, mainly with intangible assets (e.g., IT, electronic media, telecommunication, biotechnology, environmental protection, alternative energy, etc.), although some markets attract broader set of companies from different sectors	Firms operating in various sectors

Source: Šestanović, 2016

Thanks to the easing of admission criteria, being listed on alternative markets opens up the opportunity for listed companies to prepare for listing on the relevant main markets. The public equity market thereby not only increases entrepreneurs' access to funding sources, but also improves their knowledge and ability to do business and raise funds in the future. In some SME markets, firms are encouraged to graduate to the stock exchange's main board once they satisfy certain criteria.[20] According to Schellhase and Woodsome (2017), the available data suggest that at least for older, more established SME boards in middle-income countries, such as Poland, South Africa and Thailand, such boards have indeed served as incubators for firms to eventually list on the main boards of their exchanges.

Challenges

An analysis of the literature reveals three key pillars of challenges for SMEs on public equity markets. The major obstacle in first place for impeding investor interest in SMEs is the issue of liquidity. Entry requirements (admission cost and listing requirements) are the second key challenge for the flourishing of markets dedicated to SMEs. Finally, the absence of an ecosystem that can cater to SMEs' specific needs in a particular country can reduce companies' willingness to go public.

[20] Criteria for graduation may include time spent listed on the SME board, as well as the attainment of specified thresholds for profitability, size, or number of shareholders.

Low levels of market liquidity represent one of the most significant obstacles to investment in public equities. Liquidity risk is reported by investors as one of the biggest challenges when it comes to small public equities (WFE, 2017). The lack of liquidity discourages investor participation and increases the costs of capital-raising for listed firms (Šestanović, 2016). According to the latest data available from the WFE, in 2017 turnover velocity ratios[21] were below 15% in 40% of the markets covered by (14 out of 33 markets). In 11 markets, however, the ratio exceeded 50%, and six exchanges (all in the Asia-Pacific region) had turnover velocity values of over 100% (WFE, 2018).

There are several reasons for lack of liquidity in the SME markets outlined in the report by the ESMA Securities and Markets Stakeholder Group (ESMA, 2012):

- SMEs are intrinsically of a smaller scale than blue-chips, which often reduces their attractiveness to large, institutional investors.
- The entry of high frequency traders tends to reinforce the attractiveness of blue-chips, sometimes at the expense of SMEs in terms of trading.
- Fragmentation of the trading landscape resulted in higher competition and pressure on the business model of trading venues, encouraging some to focus on the most profitable segments, such as blue-chips trading, at the expense of other less profitable segments, such as SMEs.

The lower liquidity of SME growth markets seems to be a fact one needs to accept. Although exchange groups are launching programmes to enhance the market's liquidity, financially rewarding market operators or brokerage houses for providing analytical coverage, the liquidity of SME boards is still and most probably will be lower than on the main boards. This is a retail market segment, with very limited analytical coverage and little engagement by investment firms. It can be seen as a junior market, a milestone of growth on the way to the main market, which obviously not every company needs to take – but which makes this journey much easier and more effective.

Despite the relaxed admission criteria, the admission costs and listing requirements present major entry barriers for SME issuers (Nassr and Wehinger, 2015). The challenge for marketplaces here is to maintain a proper balance between the adapted listing requirements designed for smaller companies on the alternative market and preserving investor protection and confidence in such instruments. Simply easing admission and information disclosure criteria for companies of smaller size is not always a good solution. As Nassr and Wehinger (2015) propose, just like in the US regulations, the qualification of a small company's listing in EU countries could be unified by size of offering and potentially the relative weighting of the company's market capitalisation, instead of by absolute company size criteria.[22] Keeping high standards of information disclosure throughout the life of an equity offering and listing seems essential for all issuers in order to attract and retain investors.

For a successful SME public equity market, the benefits for SMEs accessing capital markets must outweigh the costs. The cost of preparing and completing an offering of shares typically runs up to

[21] The turnover velocity is the ratio between the turnover of domestic shares over a year and their market capitalisation. For WFE definitions please refer to: https://www.world-exchanges.org/storage/app/media/work/statistics/WFE_Statistics_Definitions.pdf

[22] The heterogeneity and highly diverse nature of the SME population indeed represents a core challenge for SME policy frameworks (Raes, 2021).

several percent of the capital raised,[23] and depends mainly on the offering size, complexity, and procedure, as well as the responsibilities of project participants. SMEs' costs can be lowered by developing the SME market ecosystems, which include exchanges, platforms, brokers, investment banks, market-makers, advisors and equity research, and so on. More infrastructure players, coupled with broader dissemination of knowledge about alternative markets' benefits and admission requirements, would allow for more competition and lower costs in the long term. According to the WFE (2018), the ecosystem for SMEs is currently not wide-ranging enough, largely due to the lack of profitability, or in other words an economic rationale behind SME-related services provided by brokers and advisors in general. A larger number of participants in such an ecosystem would create a greater capacity to take SMEs public and support them in the longer term. Consequently, more IPOs could get executed when the "IPO window" is open, which in turn would create a willingness on the part of investors to invest in small quoted companies and lead other private companies or VC/PE investors to consider the IPO as a viable exit strategy.

Nassr and Wehinger (2015) made a pioneering attempt to show how a perfect SME equity offering ecosystem could look (Figure 5). In practice, however, some elements are missing because the fees are insufficient for covering the costs and the appetite for profit of all parties involved. The key institutional question today is how can the existing system function with some elements missing, and how can stimuli be created for the missing institutional players to exist.

Figure 5. SME equity offering ecosystem

Source: Nassr & Wehinger, 2015

One of the challenges that SMEs face when looking to raise capital on public equity markets is equity culture. Unfortunately, equity markets across Europe are much less popular than, for instance, in the USA. Nassr and Wehinger (2015) provide a striking comparison between the USA (50% of the

[23] Own estimation based on a review of practices of various alternative markets.

population has invested in equities) and continental Europe (roughly around 5% of the population has direct equity investments). There may be historical reasons for this, as family-owned and family-run firms in the EU prefer to retain control and a traditional business model. Entrepreneurs in Europe are thus unwilling to relinquish any share of ownership or control of their business. Nassr and Wehinger (2015) conclude that increased education on the SME equity market ecosystem is needed, while governments can induce further SME participation on public equity markets by bridging the educational gap of small companies when it comes to capital market financing, raising their awareness of public financing options available and appropriate to them, and equipping them with the skills necessary to tap the capital markets.

Equity market options for Belarusian SMEs in the EU

In this Chapter we consider two possible marketplaces that might be relevant for young and fast-growing SMEs with Belarusian owners to raise equity capital: NewConnect in Poland (part of the Warsaw Stock Exchange), and Nasdaq First North Baltic (part of Nasdaq Baltic).

NewConnect and Nasdaq First North Baltic are the key players in SME equity markets in Central and Eastern Europe. Based in Poland and in the Baltic countries, they perfectly match the main directions of Belarusian businesses' geographical relocation in the EU (see Chapter 1). Both provide opportunities for dedicated equity market offerings for SMEs, while their admission requirements differ. The key characteristics of the two marketplaces are presented in Table 2.

Table 2: Key characteristics of NewConnect and Nasdaq First North Baltic in 2023

	NewConnect	Nasdaq First North Baltic
Number of companies listed, as of December 2023	359	20
New listings in 2023	14	2
Delistings in 2023	34	2
Capitalisation as of 29 December 2023, € million	2,958	296
Turnover in 2023, € million	462	14.4
Turnover in 2023, %[24]	15.6	4.8

Source: newconnect.pl; nasdaqbaltic.com

NewConnect of Poland significantly outperforms Nasdaq First North Baltic in terms of size and liquidity, indicating that the Polish equity market has higher potential for SMEs than the Baltic one.

Table 3 describes and compares admission requirements for these two marketplaces. They are quite similar for both.

[24] For the matter of direct comparison, turnover is calculated as ratio of yearly turnover and capitalisation as of end of period.

Table 3: Admission requirements of NewConnect and Nasdaq First North Baltic

	NewConnect	Nasdaq First North Baltic
Required minimum companies' capital	PLN 0.5 million*	-
Required period of activity before entering the stock exchange	-	-
Public offering (prospectus approved by the regulator)	Yes[25]	Yes
Private placement (information document; simplified version of the prospectus) approved by the stock exchange	Yes	Yes
Free float requirement	At least 15% of the shares being introduced must be in the hands of no fewer than 10 investors, each holding no more than 5% of the company's voting rights	-
Authorised pre-debut advisor	Yes	Yes
Authorised post-debut advisor	Yes, in the first three years after going public	Yes
Publication of financial statements	Yes, quarterly and audited yearly	Yes, annual and semi-annual financial reports

*Source: newconnect.pl; nasdaqbaltic.com. *Above EUR 0.1 million*

Obviously, the basic requirement for a firm to enter the SME equity market is to be a publicly tradable company, which means Spółka Akcyjna (SA) in Poland, Akcinė Bendrovė (AB) in Lithuania, Akciju Sabiedriba (AS) in Latvia, and Aktsiaselts (AS) in Estonia. This might become a significant legal barrier for Belarusian businesses in the EU[26]. We estimate that currently the share of such businesses among the total number of firms with Belarusian shareholders in the EU is extremely low, at less than 0.01%.[27] Companies willing to use the equity market would need to change the company's legal form by opting for one of the legal options available in Poland[28] or the Baltic countries.[29] Going public requires some effort in terms of organisation, but it ultimately benefits its structure and operation. A young and fast-growing firm should therefore compare the costs and potential benefits of a legal transformation to a public company. Changing the legal form of a

[25] Smaller offerings may only require simplified documentation:
i) an offering, which raises (together with those offerings in the last 12 month) no less than EUR 100,000 but no more that EUR 1.0 million, requires no prospectus or information memorandum: it only requires the publication of a document containing details of the offering (including key information about the issuer, offered shares, planned use of cash raised, key risks),
ii) an offering which raises (together with those offerings in the last 12 month) no less than EUR 1.0 million but no more than EUR 2.5 million only requires an information memorandum which need not be approved by the Polish Financial Supervision Authority (KNF).
26 According to our discussion with a representative of the Warsaw Stock Exchange in May 2024, changing a company's status to a joint-stock company in Poland should be considered a technically feasible issue.
[27] In Poland, Lithuania, Latvia and Estonia we found only six such companies: four in Poland and two in Estonia.
[28] See, for instance: https://lawboxfirm.com/przeksztalcenie-spolki-z-o-o-w-spolke-akcyjna/
[29] See an example for Lithuania: http://www.invoco.lt/imoniu-pertvarkymas-reorganizavimas

business is challenging and costly, but it is an absolutely feasible and normal process when planning company development in any country around the world. The status of public company offers a range of benefits that are beyond the reach of many private companies, and they extend to the company, its shareholders, and its employees. Firms typically choose to become public companies and go public to raise capital for growth as a next step in the implementation of their development strategy and growth in shareholder value.

NewConnect

NewConnect was established in 2007 as a stock market operated by the Warsaw Stock Exchange (GPW) in the alternative trading system model. The market offers less strict formal requirements compared to GPW's regulated market, both in terms of the conditions for the introduction of shares to trading and the subsequent disclosure requirements for companies, as well as lower costs of floating and listing. It provides listed companies with access to investor capital and opportunities for brand promotion.

In July 2019, NewConnect was granted SME Growth Market status. As a result, listed companies can use regulatory facilitation with regard to requirements under EU regulations under MiFID II. The EU's efforts supporting the growth of SMEs suggest that further regulatory facilitation may be offered in the future to companies listed on SME Growth Markets, which would improve SMEs' access to capital.

NewConnect is a market suitable for the following companies:

- with large growth potential,
- looking for equity ranging from hundreds of thousands to tens of millions of PLN,[30]
- operating in innovative sectors, mainly with intangible assets (for example in IT, electronic media, telecommunication, biotechnology, environmental protection, alternative energy or modern services),
- with a vision and the likelihood of an IPO on the exchange market in the near future.

The process of going public at NewConnect consists of three key steps: i) preparation; ii) execution; and iii) new listing. Overall, the process of listing at NewConnect may take from 7 to 12 months.

In the preparation phase, a company needs to pick an Authorised Advisor. The Authorised Advisor will accompany the firm throughout the process of going public and thereafter, assisting with disclosure requirements and supporting the presence of the company's financial instruments on NewConnect. The next step in the phase of preparation is to conduct a due diligence and draw up a report. This will tell the Authorised Advisor whether the company meets the conditions necessary to go public on NewConnect, or what needs to be done to meet those conditions. Once the conditions necessary to go public have been met, the company should be valuated in order to determine the issue price of new issue shares at which investors will buy the company's stock.

[30] At the time of writing the policy-paper, the exchange rate was 1 EUR = 4.35 PLN.

Execution is typically the longest step in the process. It involves the drafting of the documentation required to offer shares, as well as the technical implementation of the process. The documents are prepared by advisors.

The final stage in going public with NewConnect is the new listing procedure, which involves several steps carried out by capital market institutions (the Warsaw Stock Exchange and the securities depository authority) in order to introduce shares to trading on NewConnect. The key part of a new listing is filing an application for the introduction of shares on NewConnect, usually prepared in collaboration with the Authorised Advisor. The introduction of shares to NewConnect is complete when the Exchange Management Board passes the relevant resolution. The Authorised Advisor helps ensure that the company's new listing is publicised and attracts positive investor interest.

Nasdaq First North Baltic

Nasdaq First North Baltic is a growth platform for ambitious small and medium sized companies from the Baltic countries combining the benefits of being public with simplicity. First North Baltic operates three separate stock exchanges, in Estonia, Latvia and Lithuania, under one Baltic roof, providing capital market infrastructure across the whole value chain, from listing, trading and market data to the clearing and settlement and safe-keeping of securities. Nasdaq acquired the OMX Group, the Nordic exchange group, and the owner of exchanges in Vilnius, Riga and Tallinn in February 2008.

The platform provides opportunities for two fundraising instruments: shares and bonds. The admission process is quite similar to that of NewConnect, and comprises four steps. First, the company's owners need to adopt a formal decision to list the company's shares or bonds on an exchange. Secondly, for a public offering a share prospectus – a document describing the securities to be offered to investors – needs to be drawn up and registered with the local financial supervisory authority. For private placement, a simplified version of the prospectus approved by the stock exchange needs to be prepared. Then, for new issues, an initial public offering or private placement of securities is carried out. Finally, a listing application can be submitted to the stock exchange.

An Agreement with a Certified Adviser is necessary for going public at Nasdaq First North Baltic. Information disclosure can be prepared either in the local language or in English.

The one-off shares admission fee is €7,000 for getting listed on Nasdaq First North Baltic, and the annual fee depends on the company's market value, and starts from €4,000.

Conclusions and policy proposals

There is a significant and constantly growing number of companies owned by Belarusians in the EU that contribute to the economies of EU member states, among others via taxes and tens of thousands of jobs. Their access to financing through traditional bank lending channels is very restricted, mostly because of the absence of collateral, partially due to frozen assets in Belarus (due to political persecution or regulatory limitation introduced by the authoritarian regime of Lukashenka), sanctions, and applicants' short credit history. However, there are alternative non-banking ways of funding businesses that are open to Belarusian entrepreneurs, including crowdfunding, private venture capital, and going public. We analysed opportunities of equity financing through initial public (or private) offerings and listing on organised SME growth markets for firms with Belarusian shareholders, and looked more specifically at the two leading SME growth markets in Central and Eastern Europe: NewConnect in Poland, and Nasdaq First North Baltic in Lithuania, Latvia and Estonia.

Going public has many short- and long-term benefits that this paper lists and explains. First of all, it provides a funding alternative to companies that do not currently have any access to bank credit. It can be seen as a segue to further growth as it enhances companies' governance frameworks, creates value in investor relations, and makes a company more transparent and therefore more credible to all types of business partner. For relocated Belarusian firms, going public not only broadens their funding alternatives, but can also open up access to bank credit, since listed equity can be a source of collateral.

There are, however, certain challenges involved with IPOs, or even drawbacks, including the costs, complexity, as well as the issue of comparatively low liquidity of SME markets. A fundamental legal barrier for Belarusian businesses relocated in the EU for going public is the requirement to change their legal form to a publicly tradable company. Currently, the share of such firms among all businesses in the EU with Belarusian shareholders is extremely low, at less than 0.01%.

Our first policy proposal is to launch a campaign for firms with Belarusian shareholders in the EU promoting the opportunity of equity financing through initial public (or private) offerings and being listed on NewConnect in Poland or Nasdaq First North Baltic in Lithuania, Latvia, and Estonia. The campaign could advertise specific benefits that an IPO can bring, while it should also explain in detail the process of going public, including changing the legal form to a publicly tradable company. Such a promotional campaign could be implemented via the Association of Belarusian Business Abroad (ABBA), with the usage of both private and public funds. Private funds could be raised from the market operators, the Warsaw Stock Exchange, and Nasdaq respectively to promote their SME growth markets among the relocated Belarusian businesses in the EU. Public funds could come from the European Commission's programmes for supporting the Belarusian private sector in exile.

Our second policy proposal is to dedicate a designated IPO fund that would assist relocated Belarusian companies in going public in the EU. The fund would cover a certain part of the costs of an IPO (for example legal fees, memorandum, advisors or audit costs, even the costs of changing the legal form to a publicly tradable company). Depending on the size of the fund, it could also participate in the IPO of relocated Belarusian companies by investing up to 20% of the public offering, and funding itself in part through successful investments. The fund could be partially financed from the European Commission's programmes related to the support of the Belarusian private sector in exile.

Going public requires some effort in organisation and investment, but it ultimately benefits companies and economies. Spurring IPOs of relocated Belarusian companies in the EU will further contribute to the economies of EU countries by accumulating new investment and creating new jobs in the companies concerned. Besides, it will also bring about two important benefits for the Belarusians and their aspirations for democratic change and economic reform in their country: (i) it can better integrate Belarusian entrepreneurs into the EU economies, strengthening their impact on the host economies as well as on the Belarusian diaspora; and (ii) the Belarusian business community will have a network of companies well established and connected in the EU that may bring significant experience and capital to enhance the economic transition process once Belarus gets on the path to democracy.

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