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The Characteristics of Young Companies quoted on the Unlisted Securities Market

by

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THE CHARACTERISTICS OF YOUNG COMPANIES QUOTED ON THE UNLISTED SECURITIES MARKET

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I INTRODUCTION

The major force underlying the establishment of the Unlisted Securities Market - USM - in 1980 was a recognition that the Stock Exchange was failing to meet the equity needs of small firms. (Davis and Pointon, 1984). It was argued, during the mid to late 1970's, that the absence of small firms seeking a Stock Exchange listing reflected the high costs of flotation, and that a consequence of this was that smaller growing companies were prevented from gaining access to equity so as to facilitate their further growth. In its own interest, the Stock Exchange felt that choking off the supply of new young companies seeking quotation would ultimately lead to a weakened market. For these reasons the USM was established to ensure that smaller companies could place equity on the market at lower cost than on the full market, and with fewer disclosure requirements. (Bannock and Doran, 1987).

The focus of the USM was therefore the fast growing small firm. The concept of growth in the small business sector is, however, particularly difficult to define (Storey, Keasey, Watson and Wynarczyk (1987)). For example a company which is fifty years old may have exhibited only very modest growth since start up. Nevertheless it may be of sufficient size to merit flotation on the USM if the owners wish to realise equity gains, particularly where the business has been successful in very recent years. For smaller companies it is therefore relevant to consider size by a given age as an indicator of growth.

We recognise this may be considered as a "one tailed test" since, whilst any company reaching the USM within ten years of start up is clearly a fast growth small firm, the definition excludes long established small firms which have only recently experienced very rapid growth. Even so, we have chosen to define our interest to be in young fast growth - YFG - small companies.
This paper examines the extent to which the USM is a homogeneous market, or whether the young fast growth companies differ significantly from their older counterparts. In particular it makes a distinction between "young" companies, defined as those which reached the USM within ten years of startup, and other more mature companies. It therefore attempts to offer additional insights on USM companies to those provided, for example, by Hutchinson, Meric and Meric (1988) or by Hall and Hutchinson (1988).

This paper attempts to test the following specific hypotheses:

i) YFG's are likely to prefer placement over introductions or offers for sale as a method of entry.

ii) YFG’s are more likely to have been floated in recent times, when the market has had an opportunity to develop, than in the recessionary conditions of the early 1980’s.

iii) YFG’s are more likely to move on to a full listing or be acquired than other USM firms. They are also more likely to fail, in the sense of having their trading suspended or cancelled.

iv) YFG’s are likely to be more strongly concentrated in the "modern" sectors such as electronics and leisure than in more conventional sectors.

v) YFG’s are likely to be generally larger than other firms.

vi) The profitability of YFG’s is likely to be higher than for other USM companies in the years prior to flotation, and also once floated on the market.

To test these hypotheses the paper is organised as follows:

It begins with a description of the data sources used. Section III then provides data on the age distribution of the companies on the USM.

Subsequent sections then use the age profile to test for significant differences in the two groups of firms. Section IV presents data on entry and exit and tests for age differences, whilst Section V presents data on sectoral composition. In Section VI data on market capitalisation is presented and in Section VII data on profitability and turnover is provided. In all these cases formal statistical tests are conducted to determine whether YFG’s differ significantly from more mature USM companies.
II  THE DATA

This paper uses two main sources of data viz. The Hoare Govett Unlisted Securities Market Directory, and Peat Marwick McLintock's USM Survey.

The Hoare Govett Directory mainly concerns itself with companies currently quoted on the USM, defined as at 28 September 1987. The Peat Marwick McLintock survey includes all companies which have at one time or another been quoted on the Unlisted Securities Market, as at the 31 December 1987. Because of the few months discrepancy in the dates, there are 357 "current Companies" in the Hoare Govett listing. Peat Marwick McLintock give data on a total of 604 companies, 370 of which are classified as "current". It is for this reason that the number of "current" companies in the tables presented in this paper varies according to the source used. The Hoare Govett directory is published annually, whereas Peat Marwick McLintock's survey now appears every six months.

For each of the 357 companies included in its directory, Hoare Govett give the current market capitalisation, together with issue data. The issue data includes the date and method of flotation, the amount raised, the percentage of capital issued, the issue price, yield and price/earnings ratio, together with new money and capitalisation. This data is also available in the Peat Marwick McLintock survey, but for all companies which have at one time or another been on the USM, rather than only currently quoted companies.

As well as flotation details, Hoare Govett provide summaries of financial data covering the past five years for each company. For each year, data on turnover, pre-tax profit, earnings, dividends, and net tangible assets are given. These short financial records, are based on figures provided in the prospectus, amended where appropriate by subsequent reported results. If a forecast is provided, this is also indicated in the data. Where little or no records are provided these are primarily start up and/or venture situations.

In the Hoare Govett Directory qualitative information is also provided. This includes, for example, details of how the company came to be founded, the company's current activities, major events in the life of the company, and future plans and prospects.

The Peat Marwick McLintock Directory provides five main tables together with an alphabetical index of all companies which have entered the market.
The alphabetical index of the 604 companies which had been quoted on the market at any time between 1980 and 1980 provides the first dealing date of the company, its industrial sector, and events and the date of occurrence. The events covered are: Acquisition, transfer to a full listing, cancellation, trading suspended, reorganisation, and change of name.

The first main table gives background information, by industrial sector, for companies floated since 1st January 1984. To obtain a full set of data on all companies quoted on the USM since its inception in 1980, this has been amalgamated with a similar table from an older directory. Basically, this table provides identical data to that given in the Hoare Govett directory, but Peat Marwick Mclintock also include companies which are no longer on the market as well as those currently quoted. It also provides data on the costs of flotation.

Table Two of Peat Marwick Mclintock lists the professional advisers used in each flotation, but this information is not used in the current paper.

The third table is 'Financial information at the time of flotation, since 1st January 1984'. This gives data for turnover and pre-tax profits, for each of the three years prior to flotation, as well as net and gross assets on flotation.

The final table contains share information for companies quoted as at 31st December 1987, but again this information is not used in the current paper.

To summarise, the main difference between the two directories is that Hoare Govett covers only companies currently quoted on the USM, but does provide a summary of the history of each company. Peat Marwick Mclintock's coverage is broader, encompassing not only the USM as it was at the end of 1987, but also the companies which have passed through the USM. This paper draws upon a data set which merges these sources.

III AGE OF USM COMPANIES

This paper compares companies which reach the USM within ten years of startup (young fast growers - YFG), and those which take longer (others - OTH), so as to test for key differences between these groups.

The age of USM companies varies considerably. Some, such as the Marina Development Corporation are only a few years old, whereas Kenyon Securities is one of the dozen or so companies which were established in the nineteenth century.
Unfortunately, identifying fast growth companies, using the criteria of age at time of flotation is not a simple matter given the data at our disposal. In particular, following flotation, the company may be acquired, reorganised, trading may be suspended, or it could continue successfully to a full listing. It is difficult to trace companies which have been acquired, suspended, or cancelled after flotation, and discover at what date they were founded since this information is not readily available. This means the current sample does not include ALL companies which reached the USM within ten years of startup, since it excludes those which had traded on the market, but had left before 1987. Foreign companies are also excluded from the Young Fast Growth group since it is inappropriate to combine what are effectively multinationals with UK owned independent companies developed from start up.

Given these limitations of the data, our analysis shows that 143 companies were known to have reached the USM within ten years of startup (young fast growth - YFG's). Of these, 115 continued to be quoted on the market at the end of 1987. These are then compared with the 235 companies which were quoted on the USM at the end of 1987, but which had taken more than ten years to reach the market.

IV ENTRANTS AND EXITS

(a) Method of Flotation

There are three methods of flotation on the USM: By introduction, a placing, or by offer for sale. In this section we examine whether "young fast growth" companies - (YFG's) appear to relatively favour different methods of flotation to that of other - OTH companies.

The cheapest method is an Introduction. For a company to gain an introduction to the market, at least 10% of its shares must be widely held by the public, and new capital must not be immediately required. This method has been used by 97 companies (16% of all entrants) for their flotations on to the USM. Table 1 shows that 48 companies quoted on the market at the end of 1987 used Introductions.

The most popular method of flotation is a placing. 431 companies (71.4% of all entrants) have used this method. For a company to be 'placed', the 10 per cent of shares which must be held by the public (if the company is to be admitted to the USM) are purchased by a sponsoring broker or merchant bank.
The sponsor then sells the shares to its clients, at the same or slightly higher price. Other restrictions placed on the company if it is to achieve a placing, are that market capitalization after the issue will not exceed £15m, and the total value of the shares placed does not exceed £3m.

The most expensive and least popular method of entry to the market, is the offer for sale or subscription. Only 76 companies (12.6% of all entrants) and 39 of those on the USM at the end of 1987 have used this method, which involves the familiar advertisements in the press. This method is used by companies who do not satisfy the criteria for an introduction or a placing.

**TABLE 1**

METHOD OF FLOTATION

<table>
<thead>
<tr>
<th>CURRENTLY QUOTED</th>
<th>ALL</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>OTH</td>
<td>YFG</td>
<td>604</td>
</tr>
<tr>
<td>174</td>
<td>89</td>
<td>431</td>
</tr>
<tr>
<td>31</td>
<td>8</td>
<td>76</td>
</tr>
<tr>
<td>30</td>
<td>18</td>
<td>97</td>
</tr>
<tr>
<td>TOTAL</td>
<td>235</td>
<td>115</td>
</tr>
</tbody>
</table>

Key: YFG = Young Fast Growth Company  
OTH = Other

Sources - 'Currently quoted': Hoare Govett  
'All': Peat Marwick McLintock

We can test for differences between YFG and OTH, in terms of method of flotation. To test for differences a Chi Squared statistic distributed with 2 degrees of freedom is calculated. This is found to be 3.416 which is only significant at the 20% level. There is therefore no reason to believe that YFG's quoted on the market at the end of 1987 preferred different methods of flotation to that chosen by OTH companies.
(b) **Time Series Analysis of Flotations**

We now examine the pattern of the year of entry for the 115 companies which reach flotation within ten years of startup - the YFG's - and which were on the market at the end of 1987, and compare them with OTH companies. Figure 1 shows the year of entry for the YFG companies. This is then compared with the year of entry for the 235 OTH companies.

Visual inspection suggests there is little difference between the two groups. We can calculate a Chi-squared statistic which is distributed with 7 degrees of freedom, to test for differences between the two groups. This was found to be 3.59 which has a very low significance of 90%. There is therefore no reason to believe that the year of entry differs between YFG and OTH companies.

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**FIGURE 1: YEAR OF ENTRY FOR CURRENTLY QUOTED 'YFG' & 'OTH' COMPANIES**

![Bar chart showing the number of companies floated each year from 1980 to 1987.](chart.png)

- Young Fast Growth (YFG) small companies
- Other More Mature (OTH) small companies
Time series analysis of companies transferring

FIGURE 2: NUMBER OF YEARS ON UNLISTED SECURITIES MARKET (USM)

Of the 108 Companies which transferred to a full listing, the arithmetic mean stay on the market was 29 months. Of those which went on to a full listing Figure 2 shows modal time to full flotation was two years, followed by one year. Nevertheless it has to be recalled that the USM has only been in existence for eight years, and so it is possible that the likeliest time for transfer to a full listing is, for example, six years after reaching USM. Currently the USM is not old enough to highlight this.
(c) Analysis of Exits

Of the 604 companies which have at some stage been quoted on the USM, only 370 were still on the market at the end of 1987. There is therefore a fairly high turnover of companies. As Table 2 shows there have been 234 exits, 38.7% of the number of entrants. The largest number of exits is attributable to the 108 companies which transferred to a full listing, followed by the 88 who were acquired. Only 28 companies have withdrawn from the market.

TABLE 2

EXITS FROM THE USM SINCE 1980 AND NUMBER REMAINING AS AT 31/12/87

<table>
<thead>
<tr>
<th>Category</th>
<th>Number</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Acquired</td>
<td>88</td>
<td>37.6%</td>
</tr>
<tr>
<td>Reorganized</td>
<td>10</td>
<td>4.3%</td>
</tr>
<tr>
<td>Suspended</td>
<td>28</td>
<td>12.0%</td>
</tr>
<tr>
<td>Transferred to full listing</td>
<td>108</td>
<td>46.1%</td>
</tr>
<tr>
<td>TOTAL EXITS</td>
<td>234</td>
<td>100.0%</td>
</tr>
<tr>
<td>Remaining</td>
<td>370</td>
<td>61.3%</td>
</tr>
</tbody>
</table>

Nevertheless it does seem likely that many of the YFG companies which entered the USM between 1980 and 1983 will have moved on to a full listing and so will not have been included in this study. Hence, although there are more YFG companies than would be expected in the later years, and fewer than would be expected in the 1980-83 period, this could easily reflect the movement of such firms to a full listing. Only with more complete data than we have available would it be possible to fully test this hypothesis but, intuitively, we feel that the proportion of YFG companies on the market is unlikely to have changed significantly.

ii) Time Series Analysis of Acquisitions

Turning now to the 88 companies which have been acquired, a somewhat different pattern emerges from those transferring to a full Stock Exchange quotation. Although the average length of stay on the USM is not very different from that of the firm moving on to full listing (32 months as opposed to 24), there are major differences in market capitalisation. For those leaving the USM for a full market quotation the average increase in market capitalisation at the end of 1987 was 980%. For those companies which were acquired, the mean increase in capitalisation was significantly smaller at +114%.

This points to a number of what are effectively distress and rescue acquisitions. In fact 23% of the companies have been purchased either at a discount to issue capitalisation or a premium of less than 10%.

Figure 2 also shows the distribution of time spent on the USM before acquisition. Acquisition seems most likely to occur two years after flotation, and in this respect is similar to those transferring to a full listing. Nevertheless the same provisos and reservations, which applied when interpreting data for transfers, also applies to data on acquired companies.

iii) Time series analysis of companies which cease trading.

The third, and last form of departure from the market, is through suspension of trading, or cancellation. Up until the end of 1987, only 28 companies had left the USM for this reason. Companies which get into difficulties, may leave the market, and re-enter shortly afterwards, following reorganisation. This applied to ten companies in all. Half of the companies suspended, cancelled or reorganised left the market in 1987.
As with companies acquired or transferred, it is possible to examine the time spent on the market by companies whose shares are ultimately cancelled or suspended. Figure 2 shows the distribution of time between flotation, and leaving the market in this way. Its most interesting feature is the uniformity in the number of departures of companies which have been quoted on the USM for between one and five years. As there are less companies which are four and five years old on the market, this suggests, that the mode of the distribution, when this is taken into account, would be greater than the two years indicated. It clearly demonstrates that firms exiting from the USM through suspension and cancellation of shares are substantially older than those exiting either through acquisition or those moving to a full listing.

V THE SECTORAL STRUCTURE OF THE MARKET

At the end of 1987 there were USM companies in most of the sectors included in the official list although, as we shall see, this has not always been the case. The purpose of this section is to provide a brief sketch of the way in which the sectoral composition of the companies on the market has changed in the period since 1980. It then examines whether there is any evidence that young fast growth companies - YFG's - are found in different sectors from those of other USM companies.

Table 3 gives a full sectoral breakdown for all companies currently quoted on the market, and for companies which have at some time or another been quoted on the USM.

The companies quoted on the USM at the end of 1987 are shown in the final column of the Table. The largest proportion (24.3%) comprises the 90 companies in the Industrials (miscellaneous) sector, followed by electricals with 61 companies (16.5%). The only sectors not represented on the USM at that time were Investment Trusts and Plantations, although companies in both these sectors have, at some stage, been present on the market.

In the early years of the USM the market was dominated by oil and gas companies. Later, financial and property companies and, later still, electricals (and especially computers) grew in importance. Prominent amongst more recent flotations have been service companies in the "people business" (design, consultancy, advertising). Diagram 1 shows how the sectoral distribution of USM companies has changed over the past 7 years.
### TABLE 3: ANALYSIS OF ALL COMPANIES WHICH HAVE ENTERED THE MARKET

<table>
<thead>
<tr>
<th>Industrial sector</th>
<th>Intro</th>
<th>Placing</th>
<th>Offer</th>
<th>Acquired</th>
<th>Regorg.</th>
<th>Suspended</th>
<th>Transferred</th>
<th>At 31.12.87</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Category</td>
<td>duction</td>
<td>for sale</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hire purchase</td>
<td>9</td>
<td>4</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>2</td>
</tr>
<tr>
<td>Building Industry, timber and roads</td>
<td>11</td>
<td>3</td>
<td>19</td>
<td>1</td>
<td></td>
<td></td>
<td>[1]</td>
<td>20</td>
</tr>
<tr>
<td>Chemicals and plastics</td>
<td>12</td>
<td>1</td>
<td>7</td>
<td>1</td>
<td></td>
<td></td>
<td>[2]</td>
<td>4</td>
</tr>
<tr>
<td>Drapery stores</td>
<td>13</td>
<td>4</td>
<td>30</td>
<td>7</td>
<td>[3]</td>
<td></td>
<td>[3]</td>
<td>33</td>
</tr>
<tr>
<td>Electricals</td>
<td>14</td>
<td>12</td>
<td>75</td>
<td>18</td>
<td>[17]</td>
<td>[2]</td>
<td>[4]</td>
<td>21</td>
</tr>
<tr>
<td>Engineering, machine tools</td>
<td>15</td>
<td>1</td>
<td>7</td>
<td>1</td>
<td>[1]</td>
<td></td>
<td>[1]</td>
<td>7</td>
</tr>
<tr>
<td>Food and groceries</td>
<td>16</td>
<td>1</td>
<td>18</td>
<td>7</td>
<td>[8]</td>
<td></td>
<td>[1]</td>
<td>2</td>
</tr>
<tr>
<td>Hotels &amp; caterers</td>
<td>17</td>
<td>2</td>
<td>11</td>
<td>[7]</td>
<td></td>
<td></td>
<td>[4]</td>
<td>2</td>
</tr>
<tr>
<td>Insurances</td>
<td>19</td>
<td>2</td>
<td>4</td>
<td>[1]</td>
<td></td>
<td></td>
<td>[1]</td>
<td>4</td>
</tr>
<tr>
<td>Motors, aircraft trades</td>
<td>21</td>
<td>1</td>
<td>9</td>
<td>1</td>
<td>[1]</td>
<td></td>
<td>[1]</td>
<td>9</td>
</tr>
<tr>
<td>Newspapers, publishers</td>
<td>22</td>
<td>5</td>
<td></td>
<td>[1]</td>
<td></td>
<td></td>
<td>[1]</td>
<td>3</td>
</tr>
<tr>
<td>Paper, printing and advertising</td>
<td>23</td>
<td>2</td>
<td>41</td>
<td>2</td>
<td>[7]</td>
<td>[1]</td>
<td>[17]</td>
<td>20</td>
</tr>
<tr>
<td>Textiles</td>
<td>28</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Investment trusts</td>
<td>29</td>
<td>1</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Trust, finance, land etc</td>
<td>30</td>
<td>6</td>
<td>10</td>
<td>2</td>
<td>[3]</td>
<td>[1]</td>
<td>[6]</td>
<td>8</td>
</tr>
<tr>
<td>Oil and gas</td>
<td>31</td>
<td>22</td>
<td>5</td>
<td>7</td>
<td>[7]</td>
<td>[1]</td>
<td>[2]</td>
<td>18</td>
</tr>
<tr>
<td>Plantations</td>
<td>33</td>
<td>2</td>
<td></td>
<td>[1]</td>
<td>[1]</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>35</td>
<td>1</td>
<td>21</td>
<td>5</td>
<td>[2]</td>
<td></td>
<td></td>
<td>25</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>97</td>
<td>431</td>
<td>76</td>
<td>[88]</td>
<td>[10]</td>
<td>[28]</td>
<td>[108]</td>
<td>370</td>
</tr>
</tbody>
</table>

Source: Pest Marwick McLintock
Note: Percentage of Market Capitalisation at 30th September in each year

Source: Hoare Govest
FIGURE 3: CURRENTLY QUOTED 'YFG' & 'OTH' COMPANIES BROKEN DOWN BY INDUSTRIAL SECTOR

- Miscellaneous (35)
- Oil and Gas (31)
- Trust, Finance, Land (30)
- Property (24)
- Paper printing, Advertising (23)
- Newspapers, Publishers (22)
- Motors, Aircrafts (21)
- Leisure (20)
- Insurances (19)
- Industrials (Misc) (18)
- Hotels, Caterers (17)
- Food, Groceries (16)
- Engineering, Machinery (15)
- Electricals (14)
- Drapery Stores (13)
- Chemicals, Plastics (12)
- Building, Timber, Roads (11)
- Beers, Wines, Spirits (10)
- Hire Purchase, Leasing (9)

Frequency
Figure 3 presents data on the sectoral composition of the 115 YFG's which have been identified, and are currently quoted on the market. It also presents data on the sectoral composition of the 235 currently quoted OTH companies.

Comparing the two groupings there appear to be some sectoral differences. For example none of the five 'Beers, Wines and Spirits' companies reached the USM within ten years of startup, nor any of the four companies in the 'Chemicals and Plastics' sector. Other sectors in which YFG's appear to be under-represented include Building, Timber and Roads, Drapery and Stores, Motors and Aircraft.

The absence of YFG's in the above sectors is balanced by an over representation in Electricals, Leisure and Property, all of which contain higher than expected numbers of YFG's.

A formal Chi-square test is, however, not possible for this data, because too many of the cell frequencies are less than 5.

VI MARKET CAPITALISATION

Although the USM includes primarily smaller quoted companies, there is in fact a wide range of company size. At one extreme Mrs Fields had a market capitalisation of £348m in 1987 whereas Swindon Private Hospital had a mc of only £1.9m. Recognising this considerable size variability of USM companies, this section of the paper examines whether young fast growth companies - YFG's - have a higher market capitalisation than other USM companies.

At the end of September 1987, the total capitalisation of the USM, was £9,052m, with an average market capitalisation of £25.4m. This compares with £11.8m, £11.2m and £10.6m for respectively 1986, 1985, and 1984.

During 1987 average capitalisation grew by +114% compared with an 82% increase in market price performance (as measured by the Datastream leaders index). In the preceding year, market size increased by 5%, and market price performance by 17%. This would suggest that, even accounting for market movement, there has been a marked trend towards increasing size of companies on the market.
Table 5 shows that at the end of 1987 only 8% of the market was represented by the 105 companies capitalised at £10m or less. 35% of the market and 231 companies had, however, been in this category in 1986. In 1987 the greater part (73%) was represented by the 130 companies capitalised at over £20m, figures for 1986 being respectively, 45% and 39%. Of the 130 capitalised at over £20m, 13 were capitalised at £100m or more.

**TABLE 5**

**MARKET BREAKDOWN BY SIZE IN SEPT 1987**

<table>
<thead>
<tr>
<th>Market Capitalisation</th>
<th>Mkt. Cap £m</th>
<th>Cap %</th>
<th>No.of Cos.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Below £2.5m</td>
<td>7</td>
<td>1</td>
<td>4</td>
</tr>
<tr>
<td>£2.5m - £10m</td>
<td>659</td>
<td>7</td>
<td>101</td>
</tr>
<tr>
<td>£10m - £20m</td>
<td>1761</td>
<td>19</td>
<td>122</td>
</tr>
<tr>
<td>Over £20m</td>
<td>6625</td>
<td>73</td>
<td>130</td>
</tr>
<tr>
<td><strong>TOTAL MARKET</strong></td>
<td><strong>9052</strong></td>
<td><strong>100</strong></td>
<td><strong>357</strong></td>
</tr>
</tbody>
</table>

Source: Hoare Govett

Sectoral analysis shows that Insurances have the highest market capitalisation, with an average of £71.4m per company, followed by Hire Purchase and Leasing companies, with £50.2m. Chemical and Plastics companies have the smallest average market capitalisation with £6.3m, the next smallest being Hotels and Caterers, with £9.9m.

Given these aggregate statements on capitalisation we again turn to our central purpose of making comparisons between young fast growth companies - YFG's and other companies quoted on the USM.

Average market capitalisation for the YFG's at the end of September 1987 was found to be £26.92, compared with £24.55m for other USM companies. Table 6 gives basic statistics on market capitalisation for the two groups.
TABLE 6
MARKET CAPITALIZATION IN SEPTEMBER 1987
FOR YFG AND OTH COMPANIES

<table>
<thead>
<tr>
<th></th>
<th>YFG companies</th>
<th>OTH companies</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>£m</td>
<td>£m</td>
</tr>
<tr>
<td>mean</td>
<td>26.92</td>
<td>24.55 (23.17)</td>
</tr>
<tr>
<td>std dev</td>
<td>26.10</td>
<td>34.26 (26.96)</td>
</tr>
<tr>
<td>minimum</td>
<td>2.4</td>
<td>0.8 (0.8)</td>
</tr>
<tr>
<td>maximum</td>
<td>127.1</td>
<td>348.0 (434.0)</td>
</tr>
</tbody>
</table>

KEY: YFG = Young Fast Growth companies
OTH = Other USM companies

Source: Hoare Govett

To determine if there is significant difference between the two groups, a t test is used. The t statistic is calculated to be 0.72 and so not significantly different from each other. There is therefore no support for the hypothesis that YFG's tend to have significantly higher market capitalisation than OTH companies.

VII PROFITS AND TURNOVER

This section examines data on profitability, normalised by turnover. As in the previous sections, data for all USM companies is provided initially, but then a distinction is made between YFG and OTH companies.

Table 7 shows profit as a percentage of turnover (p/t) initially for ALL companies and then separately for YFG and for OTH companies. Data for the OTH firms shows that in the 1984-7 period there was remarkably little change in levels of profitability, with this averaging at about 9%. The most striking feature is the increase in profit rates from the low point of 1983.

The profit/tturnover data for YFG companies for 1983 to 1987 follows a broadly similar pattern to that of the OTH companies. A t-test shows there is no significant difference between the mean profit/turnover for the two groups.
TABLE 7  
PROFIT/TURNOVER FOR FAST GROWERS,
VERSUS ALL USM COMPANIES, 1983-1987  

Profit/Turnover (%)  

<table>
<thead>
<tr>
<th>Year</th>
<th>ALL Companies</th>
<th></th>
<th>YFG Companies</th>
<th></th>
<th>OTH Companies</th>
<th></th>
<th>t</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>p/t</td>
<td>n</td>
<td>p/t</td>
<td>n</td>
<td>p/t</td>
<td>n</td>
<td></td>
</tr>
<tr>
<td>1983</td>
<td>6.9</td>
<td>314</td>
<td>6.3</td>
<td>105</td>
<td>7.2</td>
<td>209</td>
<td>0.54</td>
</tr>
<tr>
<td>1984</td>
<td>9.1</td>
<td>317</td>
<td>9.7</td>
<td>106</td>
<td>9.1</td>
<td>211</td>
<td>0.36</td>
</tr>
<tr>
<td>1985</td>
<td>8.7</td>
<td>322</td>
<td>8.8</td>
<td>109</td>
<td>8.7</td>
<td>213</td>
<td>0.05</td>
</tr>
<tr>
<td>1986</td>
<td>9.0</td>
<td>315</td>
<td>8.3</td>
<td>107</td>
<td>9.3</td>
<td>207</td>
<td>0.49</td>
</tr>
<tr>
<td>1987</td>
<td>9.6</td>
<td>286</td>
<td>8.7</td>
<td>92</td>
<td>10.0</td>
<td>194</td>
<td>0.68</td>
</tr>
</tbody>
</table>

Average  

KEY:  
ALL = All USM companies currently quoted  
YFG = Young Fast Growth companies currently quoted on USM  
OTH = Other companies currently quoted on USM  

Source: Hoare Govett  

We now examine whether, in years prior to flotation the 
YFG companies outperformed the OTH companies in terms of 
profitability. Data are available on profit and turnover 
three years prior to flotation, for most of the companies 
which have at one time or another been on the USM.  

Table 8 compares the three years prior data, for the YFG 
and OTH companies. A t-test shows that there is no 
significant difference between the mean profit/turnover 
for the two groups.
### TABLE 8

**PROFIT/TURNOVER FOR THREE YEARS PRIOR TO FLOTATION**

<table>
<thead>
<tr>
<th></th>
<th>ALL Co.s</th>
<th>YFG Co.s</th>
<th>OTH Co.s</th>
<th>t p/t n</th>
<th>p/t n</th>
<th>p/t n</th>
</tr>
</thead>
<tbody>
<tr>
<td>3 years prior to flotation</td>
<td>8.9 514</td>
<td>8.4 129</td>
<td>9.1 385</td>
<td>0.78</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2 years prior to flotation</td>
<td>10.3 523</td>
<td>10.5 133</td>
<td>10.2 390</td>
<td>0.34</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1 year prior to flotation</td>
<td>13.2 529</td>
<td>13.2 133</td>
<td>13.2 396</td>
<td>1.52</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Average</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Hoare Govett

Tables 7 and 8 show, that, in terms of profitability, there is also no significant difference between companies which take less than ten years to reach the USM, and those which take longer.

### VIII CONCLUSION

This paper has presented data on the development and characteristics of companies quoted on the USM. In particular it has attempted to distinguish between young, fast growth companies - YFG's - defined as those reaching the USM within ten years of start up, and other USM companies. The purpose of the distinction is to identify the extent to which the USM is serving the function of providing a relatively low cost source of equity capital for companies experiencing rapid growth and perhaps expecting to move on to a full quotation. The problems over defining growth in a small companies meant that it was appropriate to focus upon relatively young companies.
The paper concluded that whilst there were some differences between YFG companies and OTH companies, there were generally fewer differences than might have been expected. Our results provisionally suggest that:

- There are some differences in the sectoral composition of YFG and OTH companies. The YFG companies are more likely to be found in the newer industries such as electricals, leisure, advertising and property.

- Firms exiting from the USM through suspension or cancellation appear to be substantially older than those exiting through acquisition or those moving to a full listing.

In several respects we were unable to identify significant differences between OTH and YFG companies.

For instance:

- Both YFG and OTH companies prefer placements to either Offers or Introductions and although it might have been expected that young companies, marshalling their resources for growth might have been expected to favour the relatively inexpensive Introduction we could not find evidence to support this hypothesis.

- We could not adequately test whether there had been an increase in the proportion of YFG companies on the market over the period since the start of the market in 1980.

- Somewhat to our surprise we could find no evidence that the profitability of YFG companies was higher than that of OTH companies. This result applied both in the three years prior to flotation and whilst quoted on the market in the 1983-87 period.

- Finally we were not able to find any evidence of significant size differences between YFG and OTH companies.
REFERENCES


