Towards a European Capital Markets Union

Valerio Novembre, EUI

valerio.novembre@esma.europa.eu

Agenda

I. **EU vs. US capital markets: an overview**

II. The rationale for a European CMU

III. EU initiatives to achieve a CMU

IV. What's next? The CMU "elephants in the room"

V. Q&A session

I

EU vs US capital markets: an overview

Size and integration

An overview of EU financial structure

- EU capital markets-based financing is sizable but **European companies** continue to receive a significant share of their funding from **bank loans rather than from capital markets**.
  - When compared to the US, the world's largest and most successful CMU, the EU financial system remains considerably less market-based.
  - **Even listed companies** in Europe are substantially more bank-financed than in the US.
- In Europe, it can be observed that the levels of
  - the **financial market activity** and
  - **retail investor participation**

  are overall relatively **low and vary widely** across Member States.

Size and integration

An overview of EU financial structure

The **reasons** for this limited development **are deep-rooted in the features of our economy**.

(i) Financial market activity

- **In the EU, credit markets represent 80% of GDP (vs. 52% in US); stock markets represent 50% of GDP in EU and 154% in US.**
  - The EU financial structure indicator is in line with the levels observed in mid-90s and corporate equity and debt securities in EU are less than half weight than in the US.
  - Venture capital investments are 10 times higher in the US than in the EU
  - EU pension funds are smaller, generally less exposed to equity and mainly exposed to non-EU equity
- **Within the EU, there is significant financial structure diversity across members**, with countries such as NL, SE and DK on the one side and a few eastern and Baltic countries on the other side of the spectrum.

Link to graph 1

Link to graph 2

Link to graph 3

Size and integration

An overview of EU financial structure

(ii) Retail investor participation

- European households own substantial financial assets which have steadily increased in the last decade. However, their participation in capital markets is overall low, especially when compared to the US.
  - Equity and debt securities in Europe claim a share of 21% of total household assets compared to 40.7% in the US, on the contrary cash and bank deposit amount to 30% in EU vs. 21,3% in US.
  - In the last decade, while EU household assets have increased significantly (i.e. by almost a half), the various shares of asset classes remained relatively constant.
- Within the EU, the composition of households' financial assets is quite heterogenous, with deposits ranging from 14% (SW) to 61% (EL) CEPS (2019).

Agenda

II

The rationale for a European CMU

Structural issues

- The **post-2008 downturn** has highlighted the weakness of an economic system based on SMEs that are dependent on banking finance
  - In the US, capital markets absorbed 22% of shocks related to the Great Financial Crisis vs. 2% in the Euro area (cf. Milano, 2017)

- The underdevelopment of capital markets and in particular equity finance (including VC finance) has been proven to have negative consequences for **growth**.

- Equity-based financing is better suited than banks to finance the **twin transitions**: i) high-growth sectors such as digital and hi-tech where the role of intangible capital is higher (Beck et al. 2020), ii) less-polluting sectors (De Haas and Popov, 2019).

- Greater diversity of financing means better **stability** of the financial system
  - During a financial crisis, market-centered systems are more resilient, both on the demand and supply side (Gambacorta et al. 2014)
  - Systemic risk is higher in “bancocentric” systems (Langfield and Pagano, 2016)
  - Risk sharing among euro area countries is associated with the contribution of capital markets. (ECB, Financial integration in Europe, 2017)
  - More integrated capital markets can support smooth and homogeneous transmission of monetary policy (ECB, ibid.)

How to solve structural issues

- Capital markets and banking finance are complementary and should **go hand in hand**.
  - This calls for an evolved role for banks (less funding via balance sheet)
  - This requires increasing the attractiveness of EU markets for investors by reducing fragmentation

- In the past decade **Europe has progressed significantly in integrating some parts of its financial market, however there is room for improvement** especially in the equity market.
  - Clear examples of increasing market integration are trading venues and the market for clearing, which benefited from the adoption of milestone legislative reforms such as EMIR or Mifid.
  - Progress has also been made in areas such as asset management and non-equity issuances, where some member states have become specialists.
  - However, with the UK leaving, the biggest national capital market on which much of the EU economy was (and partly still is) dependent is now located outside the bloc

Current issues

- CMU is at the core of the European financial policy agenda, together with sustainable growth and digital finance.

- On the **demand side**, CMU is seen as a pillar of financing the twin transitions by channelling savings (especially in the form of equity) towards the real economy
  - Green transition expected to require €620bn of annual investment until 2030
  - Technological transition expected to require an extra €125bn per year

- On the **supply side**, increased retail investors' participation in capital markets is a key ingredient for a CMU
  - Households will more often need to look into their pension plans
  - Investor protection is essential in this regard

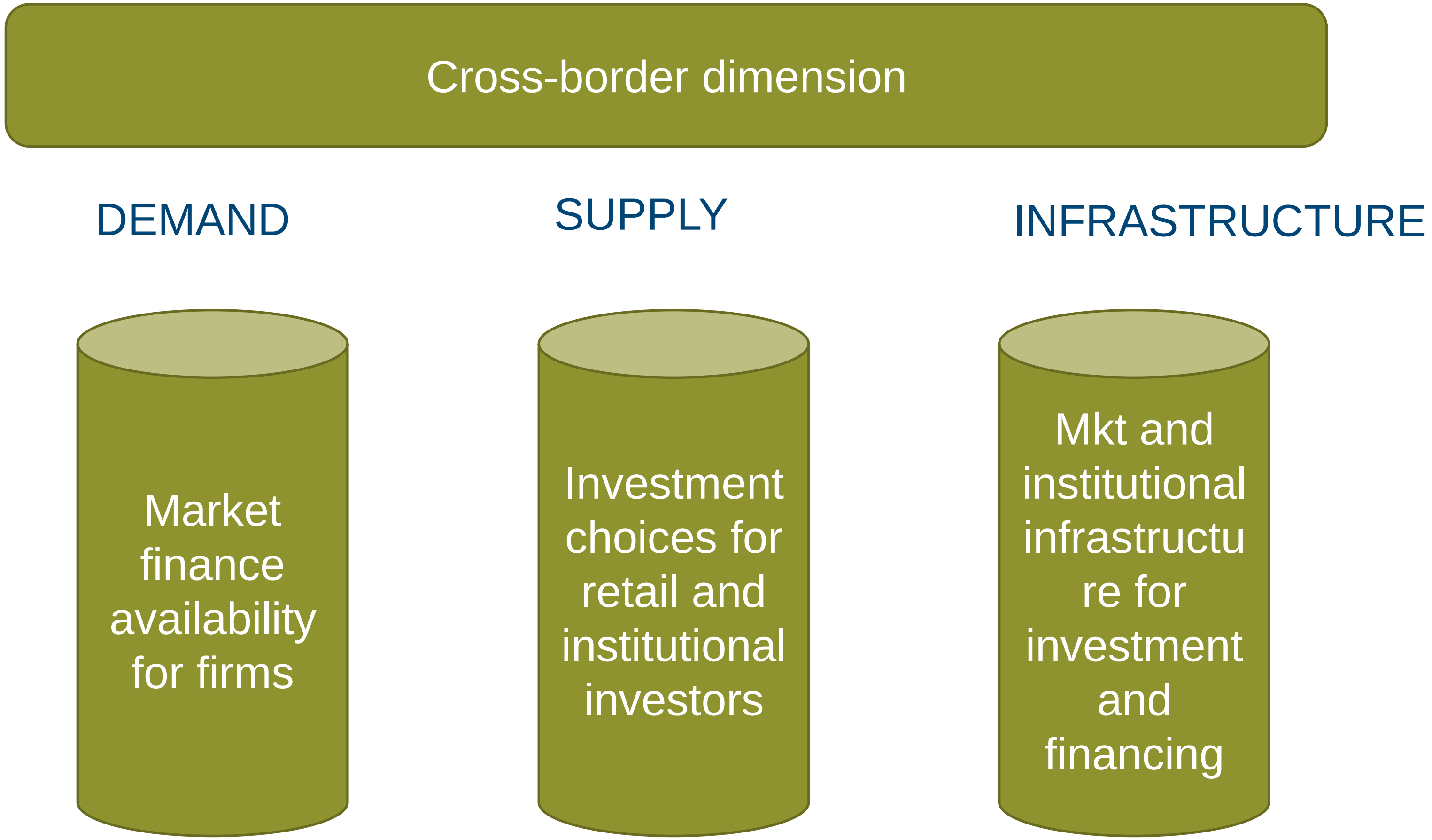
- Brexit was a game changer as London was a de-facto CMU. In the post-Brexit environment we have seen some trend towards increasing market concentration in the few EU-27 financial centres that benefit from a comprehensive ecosystem of finance professionals and services.
  - Certain EU-27 capitals have specialised and flourished in a certain different segment of the market. However, no EU capital seems able to replicate London's ecosystem.

Agenda

III

The pillars of a CMU and recent EU initiatives to achieve it

3 main pillars



The route to a CMU in the EU

2015 — Action Plan on Building a Capital Markets Union (CMU)

2017 — Mid-Term Review of the CMU Action Plan

2019 — 

Next CMU
Savings and Sustainable Investment Union

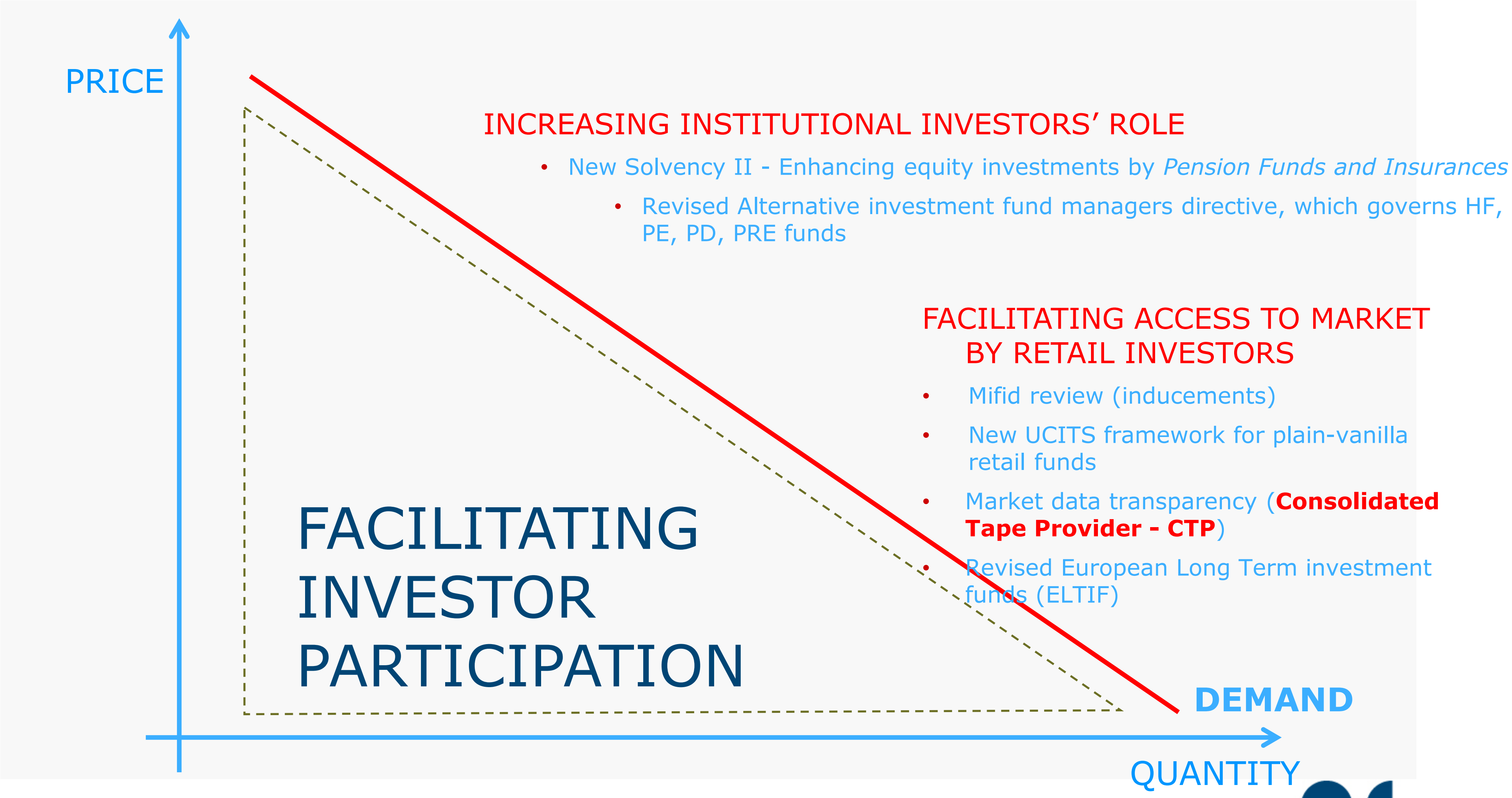
2020 (H1) — 

High-Level Forum
Final Report

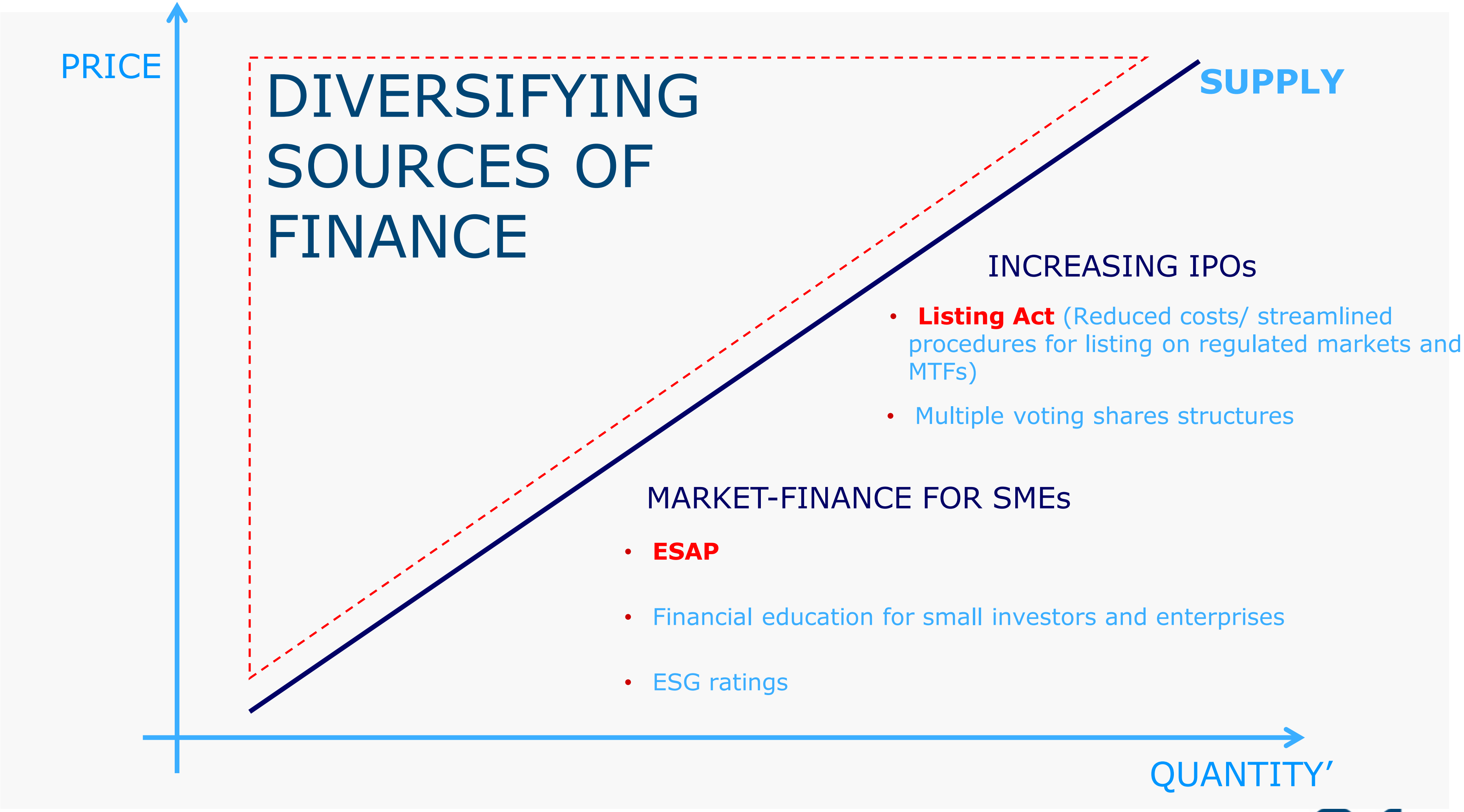
2020 (H2) — Second CMU Action Plan

2025? — Third CMU Action Plan?

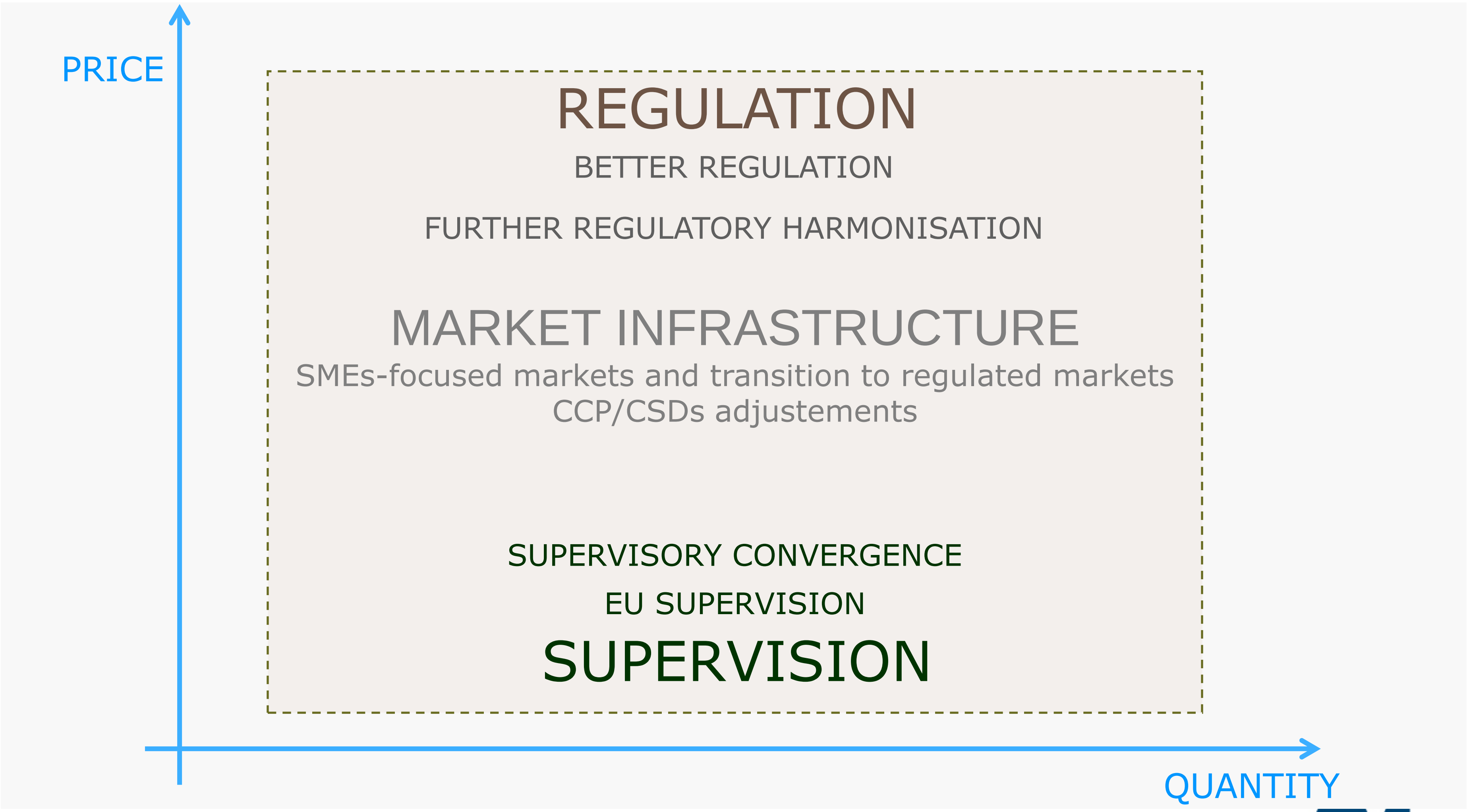
Demand: main areas of intervention



Supply: main areas of intervention



Market and institutional infrastructure: main areas of intervention



Agenda

I. EU vs. US capital markets: an overview

II. The rationale for a European CMU

III. EU initiatives to achieve a CMU

IV. What’s next? The CMU “elephants in the room”

V. Q&A session

IV

What’s next? The CMU “elephants in the room”

Ambitions vs tools

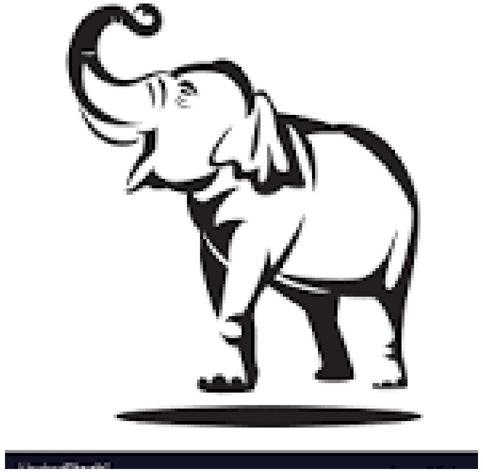
What's next?

The CMU

"elephants in

the room"

PRICE

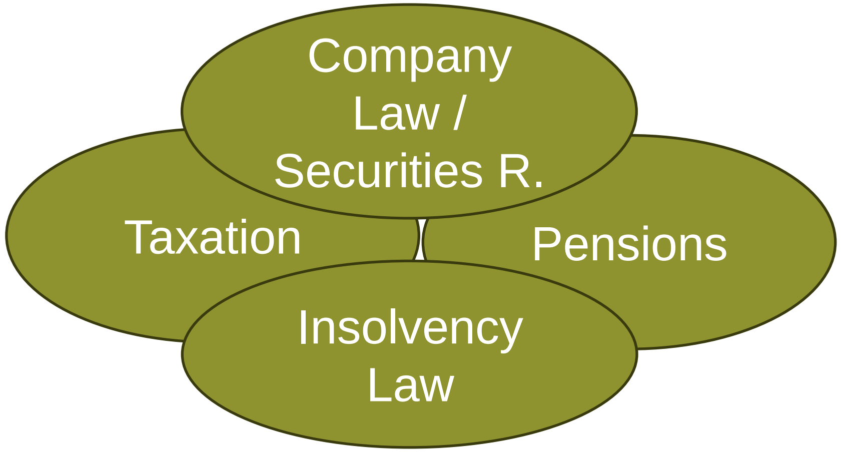


Market infrastructure consolid.

X-border M&As

X-border (equity) retail investm.

Securitisation



Supervision

QUANTITY

What's next?

The CMU "elephants in the room"

European Council
Council of the European Union

Home > Press > Press releases

Eurogroup Statements and remarks 11 March 2024 18:35

Statement of the Eurogroup in inclusive format on the future of Capital Markets Union

Vested interests must not block the EU's capital markets union

Europe's global economic standing requires progress on a project that has been in the works since 2015

MAIREAD MCGUINNESS + Add to myFT

What’s next?

The CMU

“elephants in

the room“

Insolvency

- Corporate insolvency / restructuring regimes are economically important because they support the optimal allocation of resources
- The European legal landscape in this area is diverse and efforts to reduce fragmentation are being put in place (cf. European Restructuring and Insolvency Directive, 2019/1023 and current proposed Directive 2022/702 on Insolvency)
- Overall, European insolvency systems are however less effective than the Ch.11 system in the US

What’s next?

The CMU

“elephants in

the room“

Securities regulation and company law

- Harmonisation of the national rules on company law has created some minimum standards and covers areas such as the protection of the interests of shareholders and their rights, rules on takeover bids, mergers and divisions, financial reporting and accounting, etc.
- Despite certain later efforts, such as the 2019 Company Law Package and the Regulation setting out the EU framework for screening foreign direct investment (EU 2019/452), cross border company mobility and the creation of a truly European market for corporate control seem still hampered by national political pressures
- The securitisation markets has been subject to complex regulation after the 2008 crisis: prudential treatment and reporting requirements could be reassessed, taking into account international standards

What's next?

The CMU

"elephants in

the room"

Taxation and Pensions

- "No taxation without representation"
- Withholding tax procedures still an issue
- Debt equity bias
- National EU pensions systems
  - pillar I prevalence
  - Limited role of pillar III
- PEPP effectiveness?

What's next?

The CMU

"elephants in

the room"

Supervision

- A key pillar of the European strategy for the integration of capital markets is the convergence of supervisory approaches
- ESMA set-up in 2011
  - Single rule book
  - Supervisory convergence
  - Direct supervision
- ESMA's governance

What’s next? The CMU “elephants in the room“

Towards an «EU SEC»?

European Central Bank + Add to myFT

Europe needs its own SEC, says Christine Lagarde

ECB president says consolidation among region’s exchanges would plug substantial funding gap

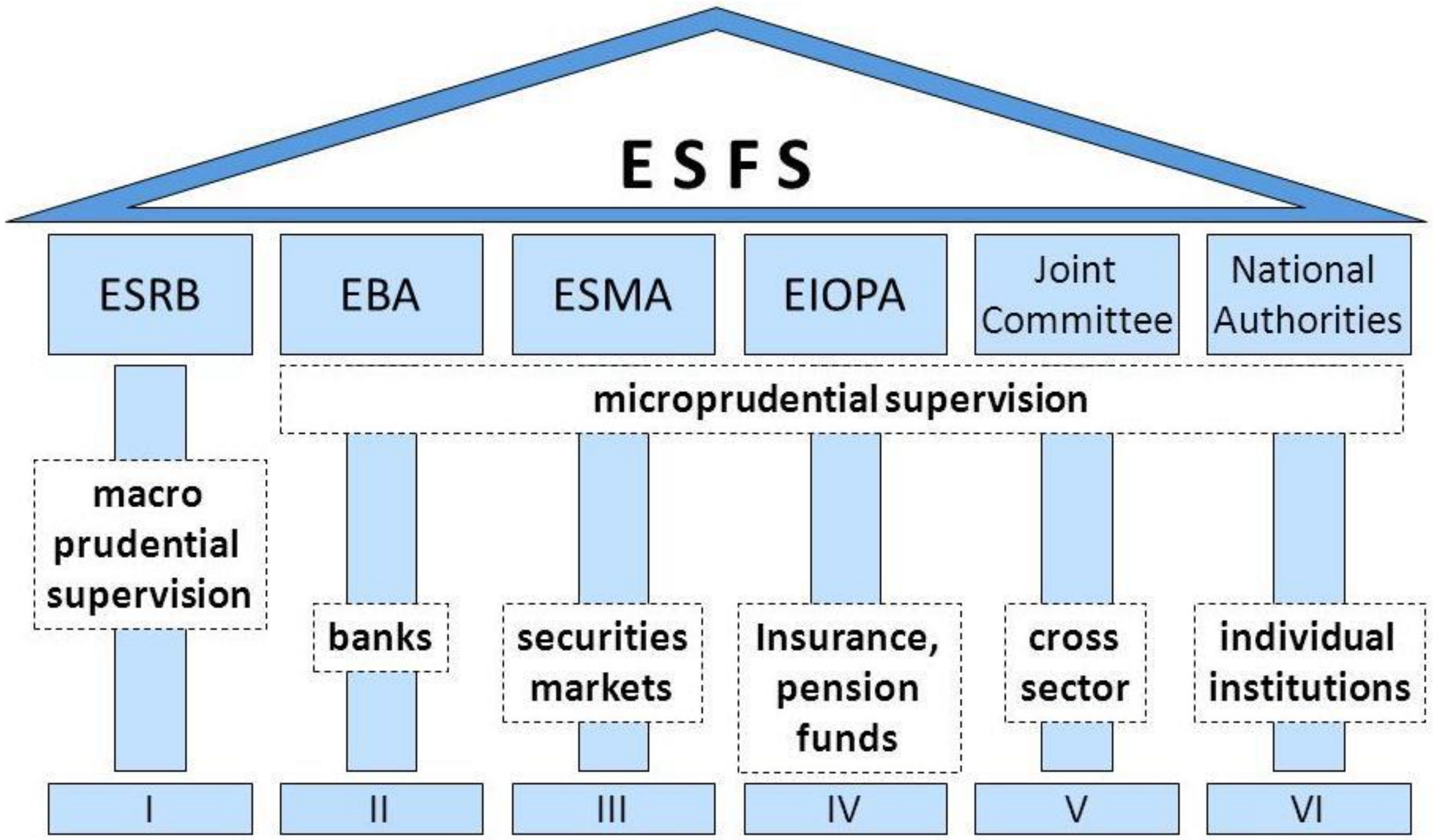
What's next?

The CMU

"elephants in

the room"

Towards an «EU SEC»?



What's next? The CMU "elephants in the room"

Towards an «EU SEC»?

Country	Banking	Securities	Insurance/Pension fund
Austria	FSA	FSA	FSA
Belgium	CB/FSA	FSA/CB	CB/FSA
Denmark	FSA	FSA	FSA
Finland	FSA	FSA	FSA
France	PA/IP	PA/IP	PA/IP
Germany	FSA	FSA	FSA
Greece	CB	S	CB/G
Ireland	CB	CB	CB/PF
Italy	CB/S	S/CB	I(CB)/PF
Luxembourg	FSA	FSA	I/FSA
Netherlands	CB/S	CB/S	CB/S
Portugal	CB/S	S/CB	I
Spain	CB/S	S/CB	G
Sweden	FSA	FSA	FSA
UK (macro FPC)	P(CB)/IP	P(CB)/IP	P(CB)/PF
EU (macro ESRB)	SSM/EBA/CA	ESMA/CA	EIOPA/CA
United States	B/CB	B/CB/S/S	Is/CB
Japan	FSA	FSA	FSA

CB (Central bank), PA (Prudential Authority on banks, securities and insurance, different from CB), B (Prudential Agency for banks), IP (Investor protection Authority for banks, securities and insurance), S (Securities Authority), I (Insurance Authority), PF (Pension Fund Authority), IPF (Insurance and Pension Fund Authority), FSA (Single prudential and investor protection regulator), G (Government department), CA (National Competent Authorities)

What's next?

The CMU

"elephants in

the room"

Towards an «EU SEC»?

- **Why**:
  - Single supervisor would be a key tool to build integrated and efficient capital markets in the EU
  - Remit should be on bigger entitites with broader international presence and with a higher systemic risk
  - Reduced regulatory and supervisory arbitrage

- **Why not**:
  - Markets are still too fragmented and regulatory harmonisation is still limited
  - National Authorities are better equipped to understand local market characteristics and specificities
  - Risk of duplications and inefficiencies
  - Size is not always a good proxy of systemic risk

What's next?

The CMU

"elephants in

the room"

Towards an «EU SEC»?

- **Why**:
  - Single supervisor would be a key tool to build integrated and efficient capital markets in the EU
  - Remit should be on bigger entitites with broader international presence and with a higher systemic risk
  - Reduced regulatory and supervisory arbitrage

- **Why not**:
  - Markets are still too fragmented and regulatory harmonisation is still limited
  - National Authorities are better equipped to understand local market characteristics and specificities
  - Risk of duplications and inefficiencies
  - Size is not always a good proxy of systemic risk

What to expect next?

Majority of EU states object to capital markets reform push

France led calls to revive financial integration project to help fund Europe's rearmament and green transition

Opinion **EU economy**

To really change the EU, the northern flank must take the lead

Nine like-minded member states would be enough to break the logjams on reform

MARTIN SANDBU + Add to myFT

Papers

AFM (2020), Working towards open and sustainable capital markets in Europe that serve the real economy - next steps for the CMU

Beck T., R. Dottling, T. Lambert and M. van Dijk (2020), Liquidity creation, investment and growth, CEPR Discussion Paper n.14956

Barata M.A., T. Beck and V. Novembre (2024), EU Financial Sector Priorities for 2030, Robert Schuman Centre Working Paper Series [EU financial sector priorities for 2030]

Demerzis M., Dominguez-Jimenez M., L. Guetta-Jeanrenaud (2021), Europe should not neglect its capital markets union, Bruegel Policy Contribution

De Haas R. and A. A. Popov (2019), Finance and carbon emissions, WP Series n. 2318, ECB

Micossi S. (2019), A new drive for the Capital Markets Union, LUISS Policy Brief.

Gortsos C. V. and W. G. Ringe (2020), Pandemic crisis and financial stability, EBI

Langfield S. and M. Pagano (2016), Bank bias in Europe: effects on systemic risk and growth, Economic Policy, 31(85)

Ringe W. G. (2015), Capital markets union for Europe – A political message to the UK, Legal Research Paper Series

Veron N. and G. B. Wolff (2016), Capital Markets Union: A Vision for the Long Term, Journal

Agenda

- EU vs. US capital markets: an overview
- The rationale for a European CMU
- EU initiatives to achieve a CMU
- What's next? The CMU "elephants in the room"
- **Q&A session**

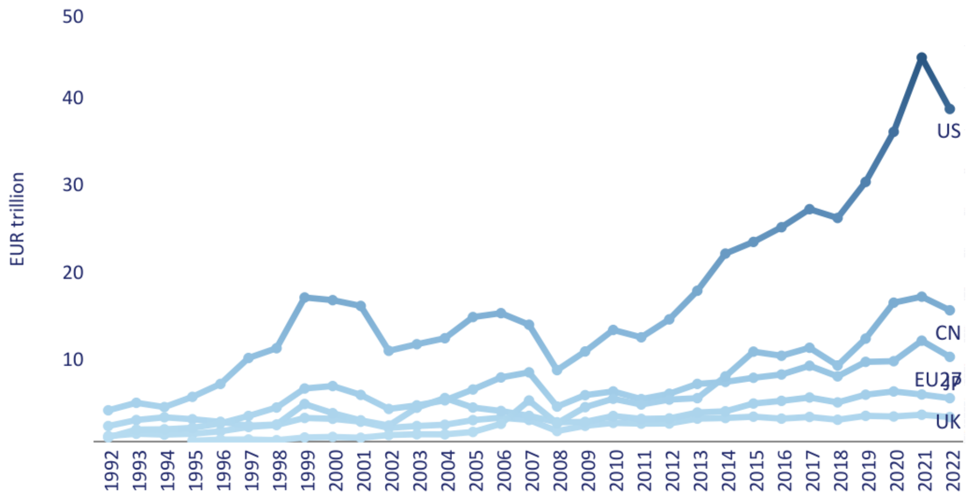
Any questions?

Annexes

The weight of capital markets in the main economies

Developments in market capitalisation

Market capitalisation (EUR trillion)



Market capitalisation (% of GDP)

Country
All

Year
2022

Market to equity

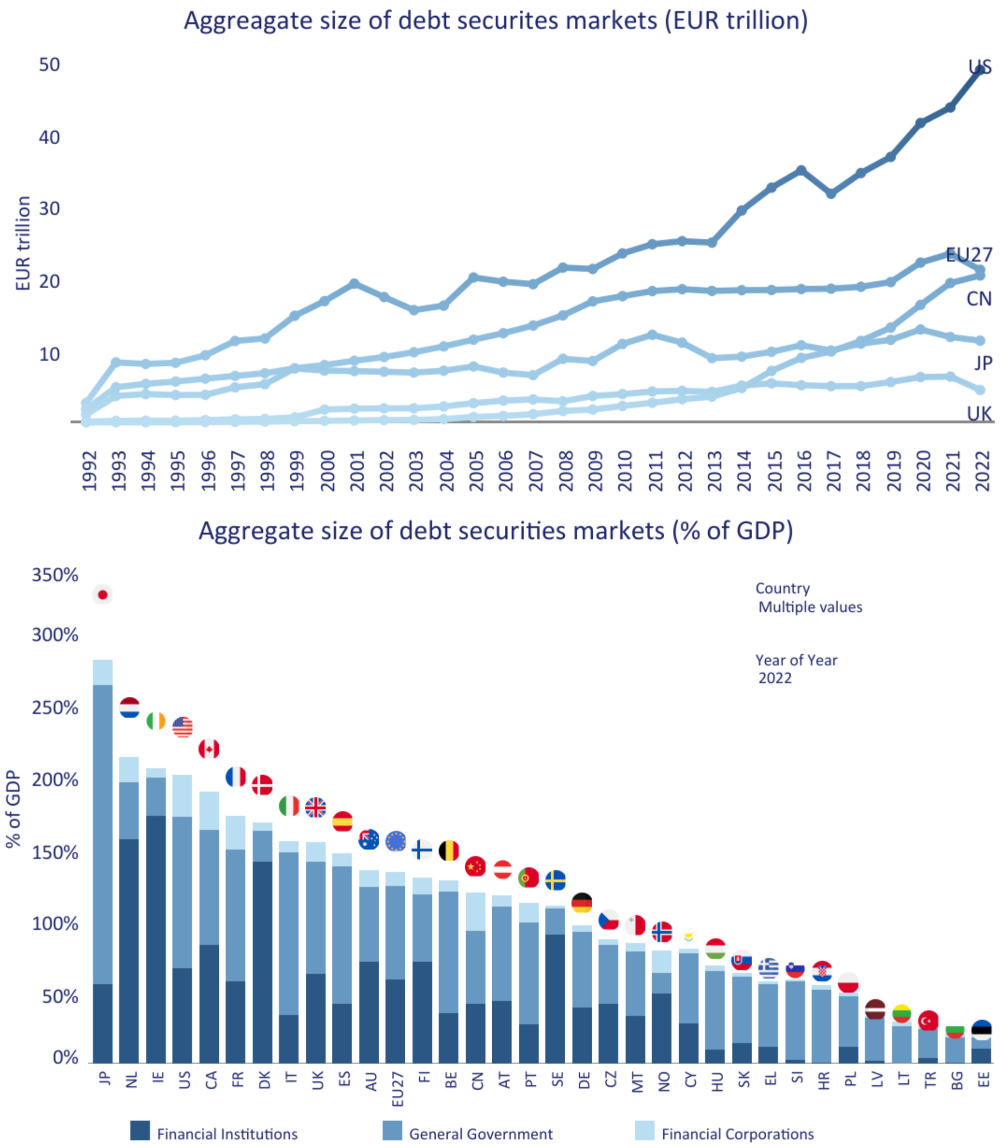
back

Source: ECMI Statistical Package, 2023

www.eui.eu

The weight of capital markets in the main economies

Developments in debt securities markets

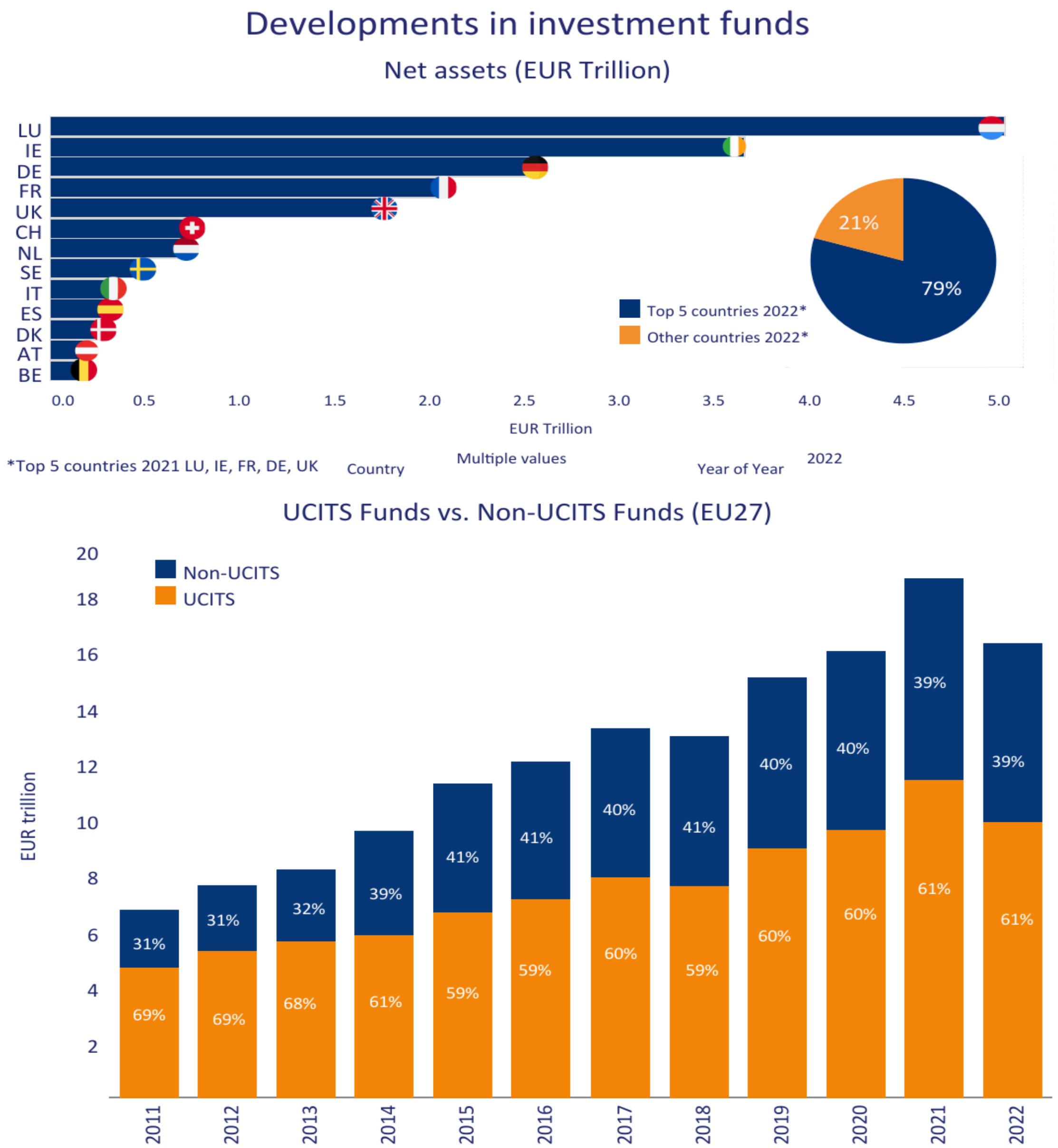


Source: ECMI Statistical Package, 2023

www.eui.eu

2023 ECMI STATISTICAL PACKAGE

The diverse role of investment funds in Europe



Source: ECMI Statistical Package, 2023