

Essential building blocks for a real Capital Market Union (CMU)

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CMU's key principles and challenges



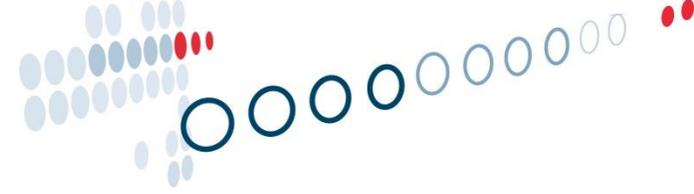
Key principles :

1. **Maximise the benefits of capital markets** for the economy, growth and jobs;
2. Create a **single market for capital** for all 28 Member States by removing barriers to cross-border investment within the EU;
3. Built on firm foundations of financial stability, with a **single rulebook** for financial services which is effectively and consistently enforced;
4. Ensure an effective level of **consumer and investor protection**;
5. **Attract investment** from all over the world and enhance EU competitiveness.

Key challenges:

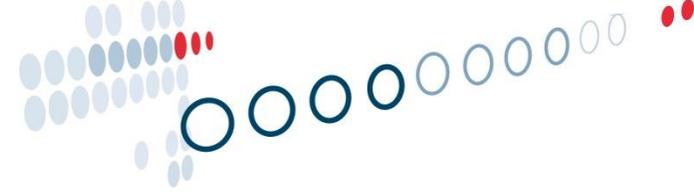
1. Supply side, to boost the flow of investment into capital markets and to enhance cross-border investment;
2. Demand side, to improve access to finance, including to risk capital.

Short-term - Five key areas



- To improve **securitisation** - Commission wants simple and transparent securitisation that works.
- To improve the **Prospectus Directive** – the Commission is not convinced that the current regime is ‘as friendly as it could be’. Administrative burdens probably deter SMEs from listing.
- To develop **private placement** market - the Commission is said to prefer a market-led approach (such as common guides and standardized documentation for private placement).
- To gather evidence about the economics of **SME credit information**.
- To boost **ELTIFS** which lack the incentives to attract institutional investors.
- To harmonise the **covered bond market**.

(1) Improving access to finance



The Commission's questions:

- Should measures be taken for greater liquidity in corporate bond markets?
- Should the EU support market-led development of 'green bonds' standardisation?
- Should the EU Adopt accounting IFRS style standards for SMEs listed on MTFs, as a feature of the SME Growth Markets?
- Are there barriers to the developments of crowdfunding platforms?

The Commission's analysis:

- for SMEs: diversity and scant credit information, preference to relationship based lending (hence banks);
- for start ups: there is a lack of tangible assets to be used as collaterals for bank finance, leasing and factoring;
- for mid-caps: access to public markets is costly;
- Corporate bond markets lack transparency and standardisation;
- Crowdfunding remains focused on national markets.

(2) Supply side - institutional investors

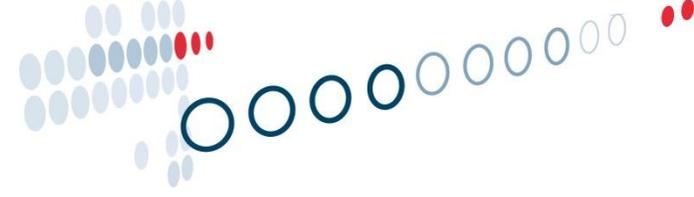


The Commission's questions:

- What policy measures could incentivise long-term investors to invest more in long-term projects, SMEs and high-growth start-ups and;
- How can we reduce costs to set up funds and market them cross-border? Commission asks which measures could be proposed to increase scale of venture capital funds both via public and private contributions, improve exit strategies and supply for investors and boost supply of venture capital to start-ups.

The Commission's analysis of current regulation and tools:

- **UCITS V and AIFMD** - still insufficient to reduce cost and diversify managed funds investment;
- **On pensions and insurance:**
 - There could be a review of Solvency II (and CRR) delegated acts, to adapt prudential rules for identified sub-classed of lower-risk infrastructure investment;
 - The Commission asks which sub-classes should be prioritised for.
- **On professional pensions:**
 - Commission suggests introduction of a standardised product, via a 29th regime to remove barriers to cross-border access.
- **Private equity and venture capital:**
 - EuVECA and EuSEF Regulations - the clause impeding managers with portfolio above €500 million to apply to set up and operate such funds or use these designations to market the funds in the EU is harmful.

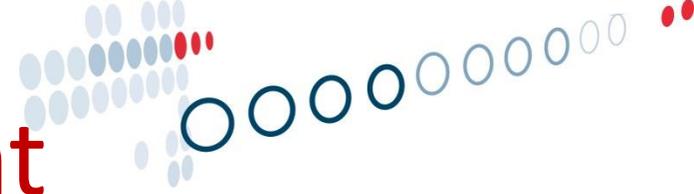


(2) Supply side – retail investors

Measures suggested to boost retail investment:

- Commission asks how to increase participation in UCITS by cross-border retail;
- Share national best practices in the development of simple and transparent investment products for consumers;
- The Commission suggests that in the review of the ESAs their mandate in consumer/investor protection could be enhanced. Commission announces vaguely it will begin preparatory work on the single market for retail financial services.

(2) Supply side – non-EU investment



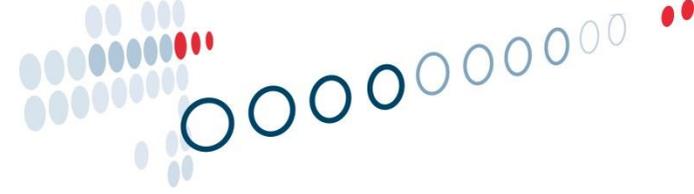
The Commission is asking the following questions:

- What more can be done to ensure that the EU is internationally competitive and attractive place in which to invest?
- What measures can be taken to facilitate market access of EU firms in third countries?

Attracting non-EU investment:

- The Commission notes that EU markets must be open and globally competitive to attract foreign investments.
- The EU has undergone a sizeable decline in the amount of gross capital inflows as a % of GDP, the gross capital inflows were lower in 2013 than in 2007.

(3) Improving the investment chain



Commission's questions regarding the single rule book, enforcement and competition include:

- Are there mechanisms to improve the functioning and efficiency of the investment chain?
- What areas in the single rulebook remain too divergent?
- Do we need changes to securities ownership rules that would help the integration of markets?
- Do the ESAs have enough power to ensure consistent supervisors?
- What additional measure relating to national or EU level supervision would help the CMU?

Commission's analysis regarding the single rule book, enforcement and competition includes:

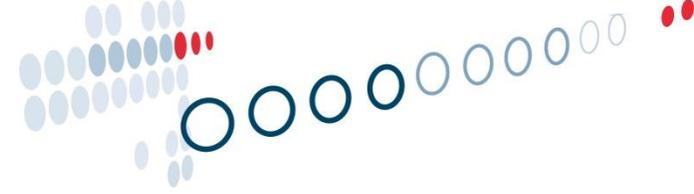
- The single rulebook is a major step forward to enforce EU regulation consistently but the single rule book's success depends on consistent implementation and enforcement.
- Supervisory convergence: the ESAs play an important role to ensure a level playing field. Active use of dispute settlement is needed – but more may be needed in a more integrated CMU.
- Common Data and reporting across the EU will help the CMU – common IT approaches for reporting requirements would help the CMU.
- Market infrastructures are regulated by CSDR, EMIR and T2S. The Commission is working on CCP recovery and resolution. The fluidity of collateral across the EU is currently restricted. Where there may be potential to make further improvements.

CMU's key principles and challenges



What is new:

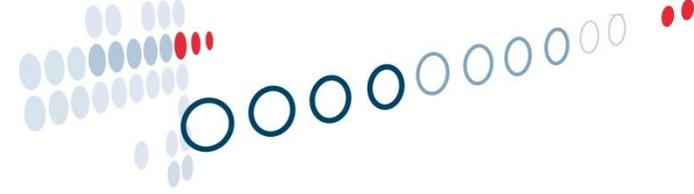
- The Commission believes that the case for a Capital Market Union now is obvious despite the fact that the EU has been trying to create a capital single market for a long time!
- There is a new focus on incentives for demand (i.e. investors) whereas in the past, the Commission focused primarily on the regulation of banks.
- There is a fresh awareness that 'one size does not fit all' and that the US capital market is not necessarily the benchmark for an EU capital market.
- The Commission somewhat reluctantly admits that some of its previous regulations were counterproductive in terms of growth and access to bank loans and capital.
- The Commission is ready to look at new ways of achieving its objectives such as working with the industry (ex. private placement, market-led development of 'green bonds' standardisation) and working with the Member States (to tackle the Giovannini barriers).



CMU – The key questions

Some of the key questions that we should discuss:

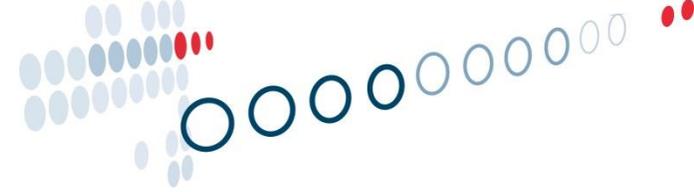
- Diagnosis - do we agree with the Commission on what needs to be fixed and why? What is the problem?
- Solutions: do we agree with the Commission on how to fix the problem?
- Ownership - who owns the project ?
- The method - did we use the wrong methods in the past (i.e. we obliged the Member States rather than cooperating with them)?
- What will be the scope? What is the perimeter? What is the level of granularity of our standards and how will they fit in with the rest of the world?



CMU – The key questions

Ownership: Who owns the project? Do we need a pilot?

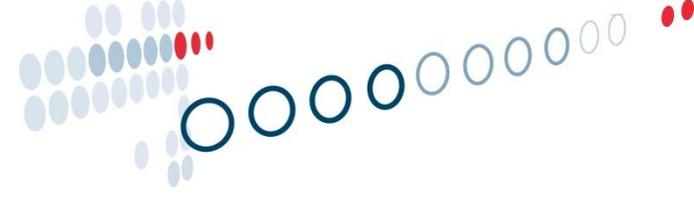
- Banking Union has succeeded due to the leadership of ECB and because a cross-border market already existed. The new bit was to add the SSM. But CMU is not BU!
- Who stands to win from the CMU project?
- Do we need a federal, independent and legitimate supervisor to drive this project? Could ESMA do this? But what would then be Member States' incentives to act?
- How to avoid hijacking by vested interests?



CMU – The key questions

Diagnosis: What is the problem? What needs to be fixed and why?

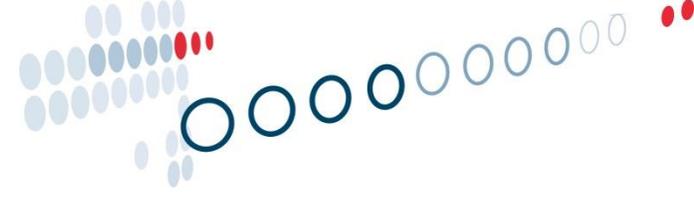
- Commission's Green Paper: merely a shopping list?
- What are the problems: access to bank loans? Access to equity markets? Lack of investor appetite for risk? Fixing the plumbing? Unemployment in Europe?
- Is Europe over-regulated? Is regulation too complex? Do no harm!
- Importance of taking stock, e.g. with Giovannini barriers.
- Is it realistic to expect a pan-European capital market? Don't we already have one (London)?



CMU – The key questions

Solutions: Do we agree with the Commission on how to fix the problem?

- Maximise the benefits of capital markets for the economy, growth and jobs.
- Build on firm foundations of financial stability, with a single rulebook for financial services which is effectively and consistently enforced.
- Create a single market for capital for the EU-28 by removing barriers to cross-border investment within the EU.
- Ensure an effective level of consumer and investor protection.
- Help attract investment from all over the world and enhance EU competitiveness.



CMU – The key questions

Method: What went wrong in the past and what could work better now?

- Did we use the wrong methods in the past?
- What can we learn from the Giovannini process? Why it has not delivered fully?
- Top-down blueprint or bottom-up approach, or a combination of both?
- Is it realistic to initiate the CMU project at the level of 28 Member States in one go?
- Is a ‘one size fits all’ approach appropriate in this context?



CMU – The key questions

Scope: What is the geographical perimeter?

- CMU is a single market project but it cannot be conceived as an EU project only. CMU should not be seen in isolation!
- CMU is about removing barriers, not erecting them.
- Market openness and greater cooperation should also therefore contribute to its success.
- But then, how granular EU standards should be to fit in with the rest of the world?
- What is the trade-off if the EU wants to attract investment from abroad?