European Capital Markets Union: Strengthening Capital Markets to foster growth

Restoring European competitiveness with joint efforts

On 18th February 2015, the European Commission published its Green Paper “Building a Capital Markets Union”. Along with its paper, the Commission opened the consultation phase, inviting all interested parties to contribute to the conceptual framing of a future Capital Markets Union. Deutsche Börse Group welcomes the Commission’s initiative.

The aim of integrating European financial markets has long been in the focus of policy makers; with the Customs Union, the Monetary Union and, most recently, the Banking Union. A Capital Markets Union can be seen as the next step on the way to fully integrate European financial markets in all 28 Member States.

Europe has gone through a severe financial and economic crisis in recent years, with much of the region still struggling to make meaningful headway on reducing unemployment and stimulating economic growth. A shift in political priorities from years of crisis solving towards sustainable growth and job creation is therefore decisive.

The concept of a Capital Markets Union should provide part of the solution, with its main objective to enhance the efficient allocation of capital throughout the EU by developing non-bank sources of funding. A strong economy needs strong capital markets to finance its growth.

This is especially problematic for small- and medium sized enterprises (SMEs) in Europe, which rely heavily on bank funding. Enhancing capital market financing will allow for companies of all sizes to benefit from alternative methods of funding. Ideally, bank and non-bank funding exist in parallel.

With regard to a broader picture, Deutsche Börse Group proposes following six core principles at the heart of achieving the objectives of a functioning Capital Markets Union:

1. Revive investor trust in financial markets

Since the global financial crisis in 2008, trust in financial markets has dramatically decreased. The loss of trust combined with a lack of properly understanding the complexities of the financial system have also led to a decline of confidence in capital markets. It takes convincing initiatives to restore the trust of investors and spur the demand for new sources of funding. Through communication and education the informed investor will be more willing to invest into European companies; and the informed company will be capable of better choosing its right source of funding.

2. Improving access to non-bank funding sources

Compared to Asia and the U.S., Europe still has a lot of room to foster non-bank financing. For example, while in the U.S. only 30 percent of general funding is covered by bank loans and 70 percent via capital markets, exactly the opposite is true for the European Union. In order to bridge the gap that emerged as traditional sources of bank funding have become increasingly constraint, non-bank funding provides alternatives through equity and debt funding. A well functioning Capital Markets Union would provide investors and companies with choices, market infrastructures, in this regard, play an important role. There is not just one method through which to increase access to funding i.e. for SMEs in Europe. Fostering a stable, positive environment and incentivising companies through attractive and diverse funding options is essential.

3. Promote financial stability

Reducing risk in the system is an indispensable condition for growth and employment. A lack in financial stability translates into economic instability as has been demonstrated during the financial crisis. In order to mitigate systemic risk and create well-functioning markets, safety and integrity must be ensured. In recent years, regulators have clearly understood and strengthened the vital role of market infrastructures: exchanges, central counterparties (CCPs) and central securities depositories (CSDs) in achieving this objective via permanent market supervision, efficient post-trade processes and collateral management. An important aim of the Capital Markets Union should thus be to realise the G20 goals and to continue implementing and truly applying the European regulations (e.g. Emir, CSDR).

4. Increase transparency
Ensuring transparency for investors as well as supervisors is an essential prerequisite for increasing financial stability, as increased transparency in terms of execution, both pre- and post-trade, improves the quality of price discovery and reduces investment risk. The Capital Markets Union should look to improve upon existing initiatives, ensuring transparency for functioning price discovery mechanisms, while keeping in mind that different data users, like retail investors, institutional investors or regulators, have different transparency needs.

5. Foster harmonisation and remove barriers
Harmonising different rules and standards within the European Union is a fundamental effort in order to eliminate costly barriers and reduce complexity for investors and companies. Significant fragmentation still exists in the public domain, for instance in securities law, insolvency law, accounting standards for SMEs as well as tax procedures. Initiatives in this area, building on the single rulebook as a harmonised regulatory framework, will increase the attractiveness of European financial markets and returns on investment, thereby stimulating growth. The Capital Markets Union can serve as an efficient vehicle to dismantle some of the cross-border barriers that still prevent the development of truly integrated European markets.

6. Shape the supporting regulatory and supervisory environment
Last but not least, shaping the supporting regulatory and supervisory framework, not only within the European Union but worldwide, is vital to create an environment in which the proposed initiatives for growth can fully prosper.

A Capital Markets Union represents an ambitious joint vision for policymakers as well as industry and societal stakeholders to integrate and further deepen European financial markets. Spurring the dialog between the different parties is an indispensable part of turning ideas into concrete actions that can flourish.

Deutsche Börse Group therefore highly appreciated the Conference of the Institute for Law and Finance of the Goethe University in Frankfurt to have offered a platform that brought together the various views on the initiative, with the common aim to revive Europe's competitiveness.

Alexandra Hachmeister
Chief Regulatory Officer
Deutsche Börse Group