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Finance for Europe

Integration, Sustainability and Competitiveness

Reflections and recommendations for banking and capital markets policy ahead of the next EU legislative cycle

November 2023

Association for Financial Markets in Europe
www.afme.eu

/ About us

The Association for Financial Markets in Europe (AFME) is the voice of Europe's wholesale financial markets, providing expertise across a broad range of regulatory and capital markets issues. We represent the leading global and European banks and other significant capital market players. AFME's members are the lead underwriters of 89% of European corporate and sovereign debt, and 75% of European listed equity capital issuances.

We advocate for deep, integrated, and sustainable capital markets which serve the needs of companies and investors, supporting economic growth and benefiting society.

AFME works to promote a robust, connected and competitive financial system, in the EU, UK and globally.

- **Advocating for deep and liquid secondary markets.** Placing greater focus on the role of well-functioning, diverse and competitive secondary market ecosystems, to build a highly liquid, market-based funding capacity, which can support businesses in raising funds and cost-efficient transactions for investors.

- **Pursuing changes that enable the green and digital transformations Europe needs.** The scale of the transitions economies need to undertake demands large-scale mobilisations of capital. Policy makers can help to create the right conditions across Europe's capital markets so that businesses and investors can benefit from technological developments and decarbonise supply chains.

- **Supporting the completion of the Banking Union and Capital Markets Union.** These have the potential to improve financial stability, ensure alternative funding sources are available to finance economic recovery & transformation independently of the economic cycle, and aid in reducing the costs of local ring-fencing facing EU banks.

- **Ensuring, in the EU and the UK, the connectivity of financial markets to the rest of the world.** Open, competitive, resilient financial systems thrive, and improve stability through the development of integrated global markets, enabling the provision of efficient services to end-users. Regulatory fragmentation undermines the benefits that come with cooperation and coordination across jurisdictions.

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1. Introduction

Context and challenges ahead

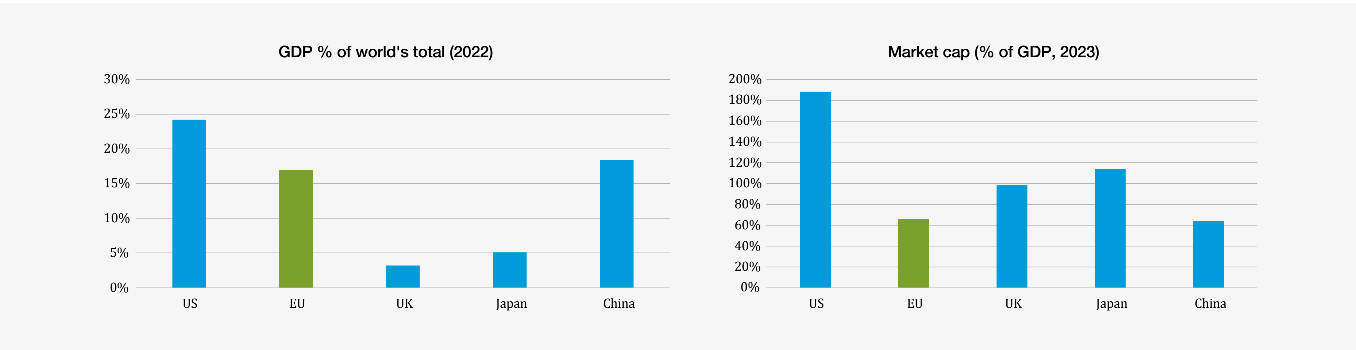
As the 2019-2024 EU legislative cycle draws to a close:

- European countries face a demographic challenge that will put pressure on public budgets and state pension systems, with citizens increasingly needing to find investments that achieve suitable returns and an income for their retirement. The inflationary environment has the potential to further erode purchasing power and compounds the urgency.
- We are less than seven years away from the milestone the EU set to reduce its greenhouse gas emissions by 55%. The European Commission estimates that the EU will need additional investments of c. EUR 700 billion annually to meet the combined objectives of the Green Deal, REPowerEU and the Net Zero Industry Act, with the majority from private financing.
- The concept of open, strategic autonomy permeates several policy domains, including financial services. It requires policymakers to balance factors such as international partnerships, which are important for the EU to remain open and part of the global economy, with concerns about the EU's competitiveness and independent capacity to navigate shocks.

Open, deep and integrated capital markets can help address some of these fundamental challenges because they:

- Provide opportunities for retail investors to manage their pensions and achieve a better return on their savings.
- Offer additional sources of funding, including solutions which are well suited to financing net-zero transition needs.
- Improve risk-sharing and enhance financial stability.

However, despite efforts under the EU's CMU Action Plans and advances in specific areas such as green bond issuances, EU capital markets remain underdeveloped in comparison to the size of the EU economy and the EU's global counterparts.



Source: AFME research based on multiple sources, see annex for further information

This paper therefore suggests avenues for EU policymakers to explore when considering their next steps to develop the EU's capital markets to serve its economy and citizens. While many of the issues it raises are well known, it attempts to recontextualise these and offers specific proposals for action.

2. Summary of AFME recommendations

Enhance the competitiveness of EU banking markets, increasing their capacity to support the economy, directly and indirectly (Chapter 3)

- Assess any future regulatory change in the context of the global competitiveness of EU banking and capital markets
- Consider the EU banking and capital markets more holistically – a fully functional and integrated banking market would help to achieve an integrated capital market
- Remove local capital and liquidity requirements for banking groups
- Streamline the macroprudential framework
- Ensure a level playing field when it comes to international standards, particularly when relevant for global activities such as markets (e.g. align timing of new capital requirements for market risk with other jurisdictions)
- Ensure that long term solutions are developed to address the ‘unratedness’ of corporates in the EU

At EU level, focus efforts in areas where rapid progress in implementing CMU measures could be transformational (Chapter 4)

- Establish consolidated tapes and enhance the equity tape with additional levels of order book depth
- Implement the European Single Access Point
- Make targeted changes to civil liability to help issuers provide forward-looking information to investors
- Adopt changes to corporate insolvency rules and harmonise withholding tax procedures to support cross-border investment
- Complete the single market for depositaries to promote participation in funds

Encourage Member State initiatives to develop their markets and seek to integrate so that European capital markets can develop at scale (Chapter 4)

- Promote the scale benefits of an integrated European capital market to Member States, corporates and citizens
- Encourage best practice sharing among Member States to develop domestic markets and investment, especially in areas where EU-level action cannot be as efficient (in particular in relation to the pensions challenge

Ensure that the sustainable finance framework achieves its objectives (Chapter 5)

- Focus on establishing roadmaps and incentives for the real economy transition, which will in turn facilitate sustainable finance, including transition finance
- Address usability challenges in the current framework, such as those associated with the do no significant harm criteria in the Taxonomy, the Sustainable Finance Disclosure Regulation, banks’ Green Asset Ratio and other disclosures
- Ensure that regulation is promoting investment and does not adversely impact the competitiveness of financial institutions or companies operating in the EU and internationally
- Enhance international coordination and improve international interoperability with other key jurisdictions
- Continue to work to strengthen the EU Emissions Trading Scheme and increase the policy and regulatory support for the role and development of voluntary carbon markets in the EU, while enhancing cooperation with other jurisdictions

Make markets more efficient for the benefit of corporates and investors (Chapter 6)

- Harness technology to improve liquidity in certain asset classes, provide access to a broader range of opportunities to investors and reduce operational costs to the benefit of end-users
- Maintain global competitiveness by continuing to improve settlement efficiency in the EU and assessing the potential to shorten the settlement cycle
- Monitor the impacts of transparency requirements on market-makers' ability to provide liquidity in fixed income instruments
- Raise the prominence of improved liquidity in secondary markets to a core, stand-alone EU policy objective in order to attract domestic and international capital pools and grow listings on EU public markets
- Review the financing toolkit, including new EU-wide hybrid instruments and public/private partnerships, which allow for scaling up market-based finance at pace
- Adjust the regulatory framework for securitisation to combine the advantages of efficiently deploying bank lending and market-based financing of the real economy
- Ensure that the rule-making process, based on the Better Regulation principles, can be responsive to the changing economic environment

3. Banking market integration

Since the GFC a decade and a half ago, European banks have continued to strengthen their capital and liquidity and made major strides in improving their balance sheets, as is evidenced by the significant reduction in non-performing loans (see table below).

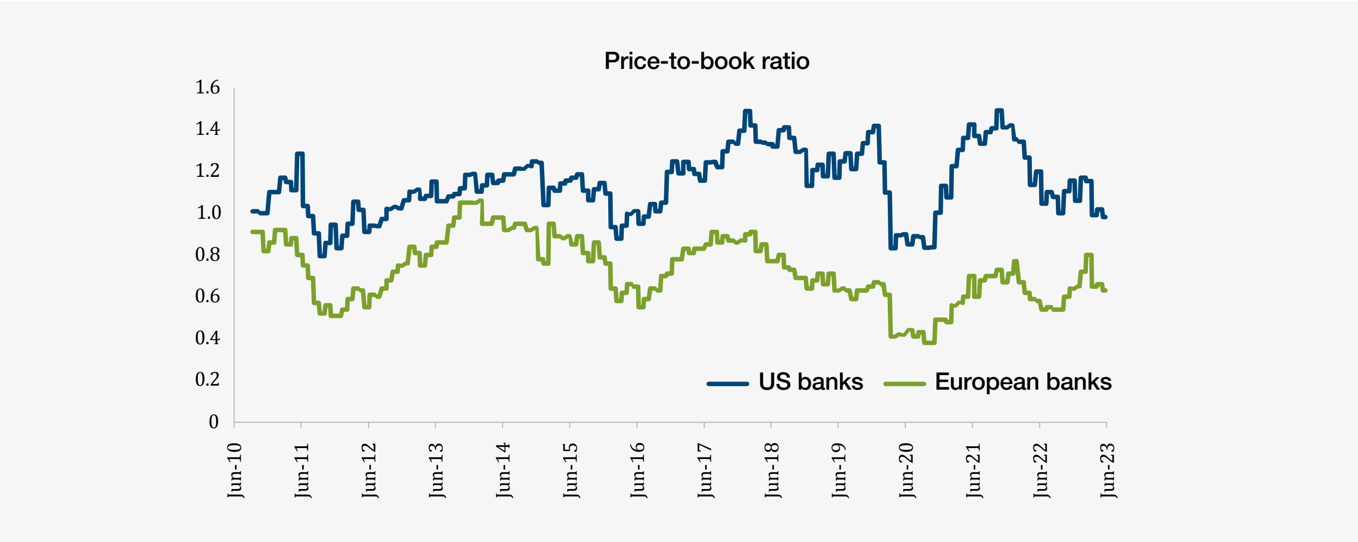
Figure 1: **Evolution of key EU banking sector regulatory ratios**

	CET1 ratio	Leverage ratio	Liquidity Coverage ratio	NPL ratio
2015 Q4	13.5%			7.0%
2016 Q4	13.8%	5.0%	136.1%	6.2%
2017 Q4	14.6%	5.4%	143.6%	4.9%
2018 Q4	14.4%	5.3%	145.0%	3.8%
2019 Q4	14.9%	5.6%	145.9%	3.2%
2020 Q4	15.7%	5.8%	171.3%	2.6%
2021 Q4	15.6%	5.9%	173.4%	2.1%
2022 Q4	15.3%	5.5%	161.5%	1.8%

Source: ECB

They have demonstrated they are well positioned to weather a variety of shocks and support the economy through periods of stress. Yet, despite these advances, European banks continue to lag behind their international peers, with market valuations below those in other jurisdictions.

Figure 2: **Price to book ratio of US banks and European banks**



Source: Refinitiv Eikon

Unsolved challenges in the single market for banking

The European banking sector has struggled with low profitability for more than a decade. While this has improved somewhat since 2022[1], average returns remain below the cost of capital. There are multiple reasons for this, including longstanding regulatory barriers which continue to hamper EU banking market integration. Direct cross-border lending within the EU also remains relatively low[2], and banking consolidation remains limited, particularly cross-border.[3]

As a result, European banks lack the scale and scope of their international peers, particularly US banks, which benefit from deeper and more efficient home markets.

It is important to recognise the tremendous transformation of the European regulatory and supervisory environment over the past decade. We have witnessed major advances in the Banking Union, such as the creation of the Single Supervisory Mechanism together with the Single Resolution Board and the implementation of a European recovery and resolution framework, with the latter currently under review to ensure it can apply to a broader range of (mid-sized) banks and avoid losses, in the case of a failure, being borne by taxpayers.

However, despite this progress, EU banks still cannot reap the benefits of a single market in banking, which impacts their scale and ability to compete globally, particularly in those areas where scale matters, such as capital market activities. For the EU to meet its investment needs of coming years, it is critical that it considers the competitiveness of its banking system and banks' ability to provide direct lending as well as capital market solutions to the real economy[4].

If persistent obstacles to the free flow of capital and liquidity (see Box) are addressed, internal capital allocation within banks operating across the EU would be significantly more efficient and resources would flow to where they are most in demand. Individuals, companies of all sizes, as well as sponsors of green and/or innovative projects, would all benefit from cheaper funding. The removal of these hurdles would not only enable more efficient capital allocation across the EU; it would have the benefit of further building on the foundation for sustainable economic growth achieved via post-GFC financial reforms, ensuring funding of the real economy throughout the cycle and further improving banking sector resiliency. This is the virtuous cycle that EU policy makers should strive for.

"EU banks still cannot reap the benefits of a single market in banking, which impacts their scale and ability to compete globally, particularly in those areas where scale matters, such as capital market activities"

1 Due notably to a combination of increasingly diversified revenue sources and the higher interest rate environment

2 ECB financial integration indicators

3 Bank mergers and acquisitions in the euro area: drivers and implications for bank performance: ECB Financial Stability Review, November 2021

4 Unrated corporates are another example of an issue that needs to be tackled. While the transitional arrangements included in the EU banking package for unrated corporates in the Output Floor are welcome, it is important that longer term solutions are found. A potential solution could be to establish a platform for banks to pool their data, or for credit bureaus to be approved as external ECAIs and develop a mechanism to map their assessments to risk weights.

Within the confines of their respective mandates and legislative frameworks, various authorities have sought partial remedies to improve the current situation. For instance, to facilitate the implementation of today's limited cross-border waivers, ECB Banking Supervision has encouraged the exploration of including contractual intragroup guarantees to support subsidiaries in supervisory approved recovery plans. They have also promoted reflection within banks on how to further digitalise their services and have clarified their supervisory approach to business combinations to remove areas of market uncertainty.

Additionally, the ECB has raised the question of why EU banking groups do not (or cannot) make greater use of branches to directly provide services across the EU, rather than relying on subsidiaries. Since the UK's exit from the EU, international banks have significantly scaled up their EU presence. In contrast to EU banks, international banks have taken advantage of European structures such as "branchification" and the EU company status (societas europaea). This raises the questions as to why incumbents are not able or willing to do so.

Nevertheless, international banks increasing their EU footprint still face the complexity of having to operate across multiple jurisdictions, with the associated differences in regulatory frameworks including, and going beyond, prudential requirements.

Differing domestic legal, taxation and AML requirements increase the cost bases of all banks operating across the EU. Proposals are on the table to create a single rule book for AML/CFT and to address certain tax and legal obstacles. Negotiations in these areas are protracted, with uncertain outcomes. Yet, they are also essential to reducing operating costs for banks and enhancing their competitiveness.

Capital and liquidity continue to be trapped inside national boundaries within the EU banking market

Banks remain confronted by an absence of meaningful cross-border waivers, including within the Eurozone. The ECB's ability to grant limited cross-border waivers from the LCR remains, to the best of our knowledge, unused some seven years after the formulation of its policy, with a similar situation with respect to the NSFR. The issue is exacerbated by the persisting complex approach to large exposure exemptions, creating an unlevel playing field and, in some cases where limits are applied via national law, acting as a direct legal impediment to the cross-border flow of funds.

Internal MREL requirements also apply at the level of all subsidiaries and cannot be waived across Member States, even if these entities are not material subgroups and are all within the scope of a single resolution authority, i.e. the SRB in the Banking Union. This EU application goes beyond the internationally agreed TLAC standard. Finally, cross-border waivers for capital (whether risk-based or under the leverage ratio) are not available and the recent agreement on the implementation of the final Basel 3 standard in the EU has compounded the situation by requiring the application of one of its key features, the so-called output floor, at the legal-entity level.

A macroprudential framework lacking in clarity and coordination

In addition to the minimum (so-called Pillar 1) requirements of the prudential framework, banks operating across the EU are subject to a complex set of additional micro and macroprudential buffers originating from different sources that partially target the same types of risk.

These include Pillar 2 requirements and guidance, set by microprudential authorities but in practice also used, in part, to address macroprudential risks. A combination of other buffers including a fixed capital conservation buffer (CCoB), a countercyclical buffer (CCyB) and various systemic buffers (including SyRB, G-SII and O-SII) are determined by the macroprudential authority of each Member State in which a bank operates. While the ECB can require additions to these national measures should it deem them insufficient, it lacks the symmetrical power to be able to loosen such requirements if they are duplicative.

The relatively opaque and complex design of the macroprudential framework, combined with a lack of coordination between the various authorities, contributes to overlapping requirements and capital accumulation within EU banks which in turn weighs on their ability to generate revenue and remain competitive, with impacts on pricing.

"[…]In the absence of cross-border liquidity waivers […], the combination of European and national provisions prevents around €250 billion of high-quality liquid assets from being moved freely within the banking union. Even if a "complete" liquidity waiver (100% of the individual requirement) were to be granted, around €140 billion of high-quality liquid assets would still not be transferable at the system level. The overall amount of risk-weighted assets resulting from individual non-waivable requirements of cross-border subsidiaries in the banking union is around 25% larger than the amount of consolidated risk-weighted assets attributable to those subsidiaries at the consolidated level."

ECB Banking Supervision Chair, Andrea Enria, **September 2021**

Reframing the debate to benefit EU corporates and competitiveness

Member States' views on many of the above issues often appear irreconcilable but the need for progress remains.

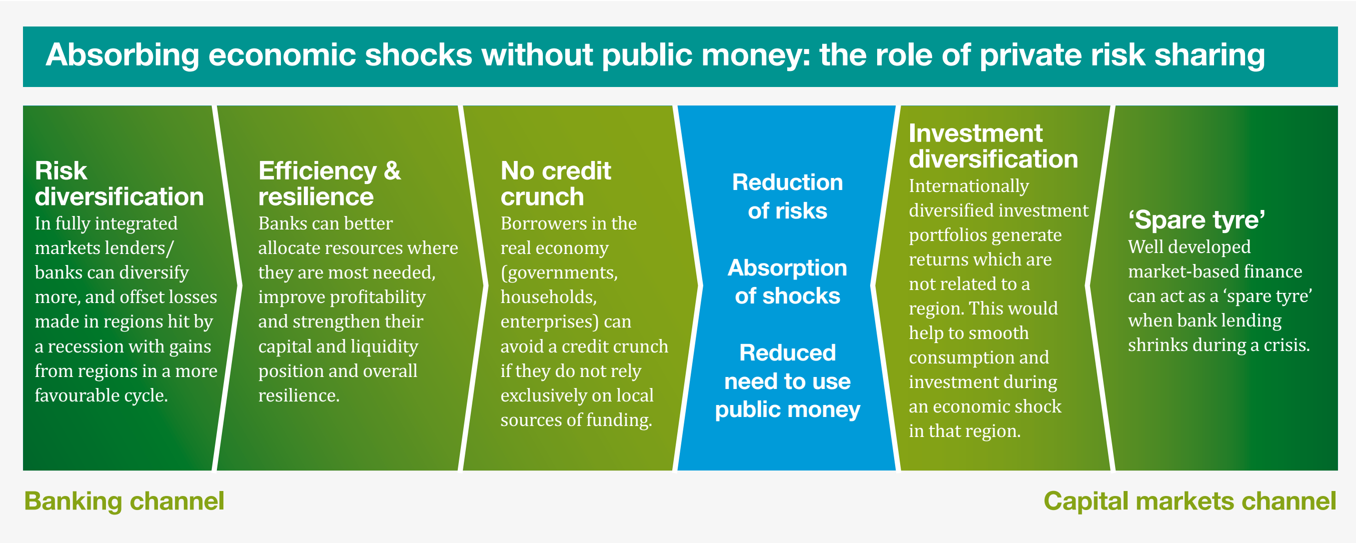
These questions should therefore be revisited at the earliest opportunity, reframing future discussions away from the risk-mitigating focus of the previous decade to placing a greater emphasis on achieving common goals related to EU corporates' financing needs and the bloc's competitiveness.

Considering banking and capital markets development more holistically from a policymaking perspective may also help in moving forward:

- A fully functional and integrated Banking Union will help to achieve a more integrated EU capital market. The development of an integrated Capital Markets Union will provide European corporates and governments greater access to finance and European investors a broader range of investment opportunities.
- Capital markets, particularly public and private equity capital, tend to be more suitable funding sources for higher risk investments – for example, innovative start-ups or frontier technologies. Meanwhile, bank loans tend to be more appropriate for medium-to-low-level risks, consolidated industries and more traditional investments. However, both are necessary to support Europe's diverse financing needs.
- This system would also provide a powerful shock-absorbing mechanism.

These objectives are intrinsically linked and mutually reinforcing. Banking and Capital Market Unions must be pursued in tandem over the next legislative cycle to promote the EU's competitiveness, ensure it can meet its sustainability goals and maintain the welfare of its citizens.

Figure 3: **Reinforcing benefits of banking and capital market unions**



AFME recommendations:

Enhance the competitiveness of EU banking markets, increasing their capacity to support the economy, directly and indirectly

- Assess regulatory change in the context of the global competitiveness of EU banking and capital markets
- Consider the EU banking and capital markets more holistically – a fully functional and integrated banking market would help to achieve an integrated capital market
- Remove local capital and liquidity requirements for banking groups
- Streamline the macroprudential framework
- Ensure a level playing field when it comes to international standards, and in particular those which are relevant for capital market activities given their global nature (e.g. align timing of capital requirements for market risk with other jurisdictions)
- Ensure that long term solutions are developed to address 'unratedness' of corporates

4. Capital market integration

The Commission has delivered all the legislative and non-legislative measures in its 2020 CMU Action Plan and EU leaders have committed to completing negotiations on open files before the next European elections[5].

While these are strong, positive signals to be welcomed, the data shows that there has not yet been a transformational shift in the funding mix of the EU economy[6].

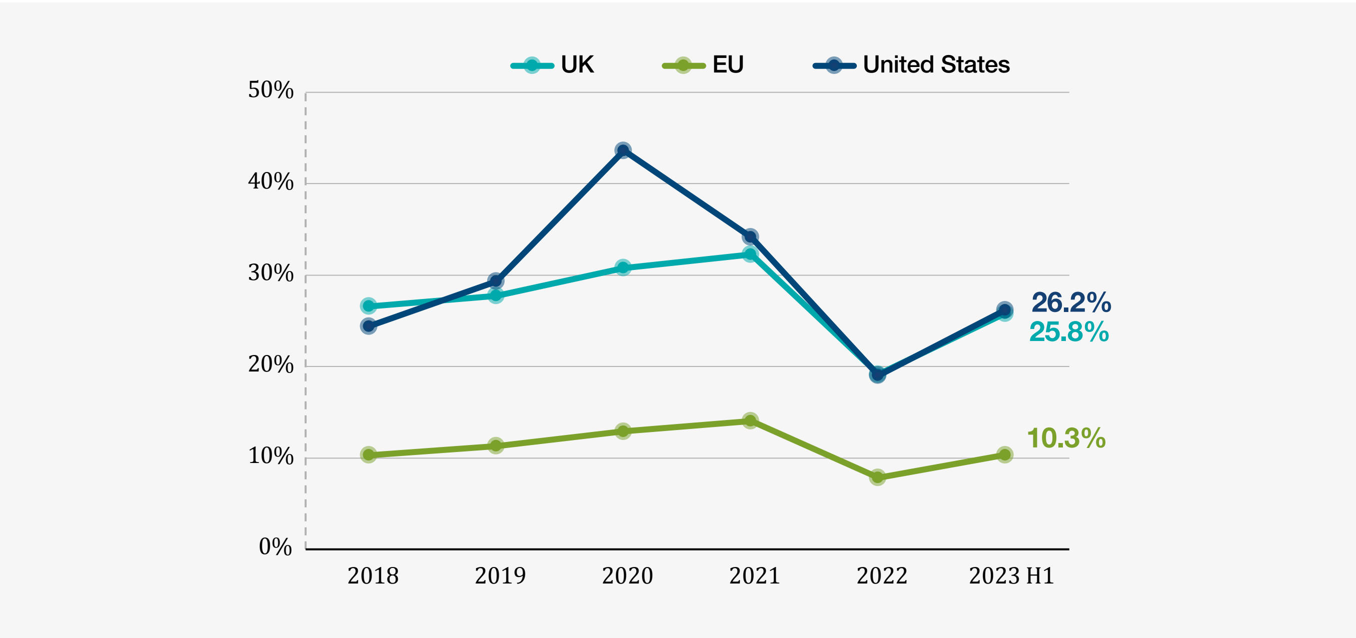
Of those CMU measures which have already been finalised, or are close to completion, a large number will only be implemented, and their impacts felt, years down the line. At this stage in the policy cycle, it is therefore challenging to undertake a meaningful assessment of what has been achieved via the CMU Action Plan. It is clear though that the financing structure of the EU economy will need to adapt, and at pace, if it is to support the EU's significant transformative investment needs, including the fast-approaching climate goals of 2030, as well as its demographic and competitiveness challenges.

The development of the EU's capital markets to support the economy therefore needs to remain at the forefront of the policymaking agenda during the next legislative cycle.

In our view, this needs to involve a combination of EU and domestic level initiatives and that EU focus is given to the implementation of some of the more potentially transformative measures already included in the 2020 CMU Action Plan.

Our views on the most impactful potential changes are set out below.

Figure 4: **Market-based financing of non-financial corporates**



Source: Market-based finance indicator, AFME's 6th CMU KPI Report (non-financial corporates' equity and bond issuances as a % of total annual financing)

5 In April 2023, the then current and incoming presidencies of the Council, the Commission and the Parliament renewed their commitment to further integrating and developing the capital markets union and to finalising the work on legislative proposals before the next European elections.

6 See for instance AFME's 6th CMU KPI Report

EU and domestic initiatives need to work together to integrate and scale capital markets

Member State initiatives can be extremely valuable, particularly in areas which fall beyond EU-level competences such as pension systems, financial education initiatives and tax incentives designed to encourage targeted investment. Member States should be provided with a platform to share their successful experiences in these areas to see if and how they can be adapted for other markets.

However, it is also important that bottom-up approaches are designed to support the growth of the EU's total market capacity, to avoid impacts remaining localised and investment being sourced predominantly from local investors. Put another way, if not coordinated with the perspective of the European economy and its competitiveness in mind, bottom-up initiatives risk maintaining or introducing further fragmentation. This could put a limit on the size of the overall EU market, ultimately also limiting the potential contribution that markets can make to funding investment needs at the scale needed to address the challenges described above.

To scale up, it is necessary to attract more investors and issuers from across the EU and abroad. Even the largest most sophisticated institutional investors continue to report that they do not consider the EU to be a homogenous market, given the degree of difference between domestic markets[7].

To reduce these differences, strengthen cross-border market integration and to scale EU capital markets up to a size which is more commensurate with the EU economy, we recommend that complementary EU and Member State level measures be taken forward in parallel, building on what will have been achieved in the present legislative cycle.

Importantly, European policymakers *also* have the responsibility to carry on promoting the advantages that the scale of a single capital market can unlock for the public good of all EU Member States, corporates, investors and citizens so that efforts are channelled to this purpose, rather than diffused by individual EU markets competing against each other.

"If not coordinated with the perspective of the European economy and its competitiveness in mind, bottom-up initiatives risk maintaining or introducing further fragmentation"

7 See for instance ECMI's **Feasibility study for the creation of a CMU equity market index family**, July 2020

Integrated European Capital Markets – a public good

Benefits of integrated European capital markets include:

Efficient allocation of capital to support growth

By enabling the efficient allocation of capital to where it is needed, a larger, more integrated European capital market would foster economic growth in the EU. Integrated capital markets enable the funding, trading, hedging, and pooling of risks, providing investors with opportunities to finance potentially profitable but inherently risky investments that might otherwise be overlooked. This implies increased financing of innovation, the development of productivity and enhanced competitiveness.

Increased market liquidity

By enabling the free flow of capital across borders, greater integration of capital markets increases liquidity. Liquidity enables companies to access funding more easily and at lower costs on primary markets because it also enables investors to buy and sell securities more easily and at better conditions on secondary markets. Greater liquidity in a market attracts investors by helping them to achieve higher and more sustainable returns over the medium to long term.

Diversification opportunities

Integrated capital markets provide investors with a broader range of investment options, allowing them to diversify their portfolios across countries, sectors and different types of financial instruments, thereby reducing their risk.

Access to larger pools of capital

Integration allows issuers to tap into a broader pool of investors, including institutional investors, pension funds and other asset managers, as well as retail investors. In particular, smaller corporates, high growth potential firms and companies operating in smaller markets benefit from increased visibility in integrated markets, as they can attract funding from investors who specialise in specific sectors or have a higher risk appetite.

Enhanced financial resilience across the EU

The risks associated with localised or asymmetric economic shocks can be spread across a larger and more diversified investor base. This private risk-sharing mechanism helps to mitigate the impact of shocks on individual markets or countries, enhancing the ability of businesses to withstand economic downturns and adapt to changing circumstances. When shocks do occur, recovery also happens more quickly in economies with well-developed capital markets.

The pensions challenge - channelling savings into productive investments

The EU's household savings rate is high relative to other developed regions but a large portion of those savings are invested in cash and deposits and not in capital markets instruments or long-term savings products. Japan has a similar savings allocation profile. This contrasts with the US where households have a more prominent participation in retail investment.

There is a strong relationship between savings invested in capital market instruments and the capacity of corporates to raise finance in markets. That is why it is important for retail investors in the EU to be offered attractive capital market investment products.

The structure of the pension system is an important driver of retail investment in capital markets. Building pools of private retirement savings not only contributes to develop capital markets but also results in lower overall public spending on pensions, freeing up public resources otherwise needed to finance pay-as-you-go pension systems. Funding pressure of such schemes due to demographic changes and rising life expectancy is a concern in several Member States.

We believe that it is necessary for Member States to act quickly with respect to the EU's "pensions' challenge". We suggest they consider all the main policy options available, for example auto-enrolment and tax incentives, though we acknowledge that the tax angle can sometimes be challenging in the context of stretched national budgets.

We therefore see this issue as a prime candidate for sharing best practices among Member States. Pension investments themselves should in our view be a mix of domestic and cross-border options, thereby increasing the level of cross-border integration and securing diversification benefits for investors.

Integration through centrally accessible market information

Here, the idea is to provide investors with straightforward access to high-quality and comparable data, to enable them to evaluate investment and trading opportunities across the EU. One of the practical advantages of this approach is that it can leverage existing data and is not dependent on integration of the underlying (physical) market infrastructures. Instead, technology is harnessed to provide an overall view of individual markets.

Having EU-wide data for investing and trading is critical to maintaining and reinforcing a virtuous circle between primary and secondary markets. Well-functioning, diverse and competitive secondary market ecosystems provide deep pools of liquidity for investors and issuers and reduce the cost of primary funding for corporates. Liquid secondary markets play a role in asset valuations (i.e. liquidity premia), influencing issuance in the primary market. Likewise, an active primary market is necessary to encourage the trading of a range of assets to satisfy investor demands for instruments with differing risk profiles.

Two important examples of this are the consolidated tapes and the single European access point and the next legislative cycle should focus on delivering their implementation.

Access to trading data through consolidated tapes

The consolidated tapes will facilitate investors' access to EU markets with a comprehensive and standardised view of equity and fixed income trading environments. The clearer picture provided by the consolidated tapes will contribute to making EU markets more competitive and attractive to all investors (including retail investors) regardless of their resources, sophistication or location. With the EU's upcoming needs for private capital sources, this is a critical objective.

These tapes will make cross-border investments easier through the creation of a truly (albeit virtually) integrated pan-European market, which will ultimately benefit corporates when raising capital and investors when allocating their savings. This will contribute to the ultimate goal of increasing capital flows within the EU and defeating retail investors' existing home bias[8]. Over time, setting up tapes could also facilitate the creation of pan-European indices, which would provide additional non-domestic investment opportunities.

8 i.e. their tendency to hold a significant share of domestic assets in their portfolios

We therefore welcome the requirement for ESMA to assess the effectiveness of the consolidated tape for shares by no later than 30 June 2026, including the appropriateness of adding additional features to the pre-trade tape, which we would strongly support.

We specifically recommend that at an appropriate time the pre-trade tape is expanded to include five levels of depth of the order book. This is technically possible and would be the most valuable option for the future subscribers to the tape, providing them with a wide range of non-latency sensitive use cases. Importantly, this would also ensure the commercial viability of the consolidated tape provider.

Access to EU corporate data through the European Single Access Point

We are supportive of the establishment of the European Single Access Point (ESAP) and commend the European Commission for launching such a broad and ambitious project. The ESAP is likely to make a strong contribution to enhanced European capital markets by improving the accessibility of key information on EU corporates for current and potential investors. Importantly, "ESAP will contribute to further integrating the financial services and capital markets in the single market, to allocating capital more efficiently across the EU and promoting the development of smaller capital markets and economies by giving them greater visibility."[9]

We think this is a strategically important project and if implemented successfully, it will provide a long-term benefit to the integration and competitiveness of EU markets.

The inclusion of sustainability information will be an important function of the ESAP, because it will facilitate investment in sustainable projects and activities, supporting the transition of the EU economy.

Given the complexity of the project, we are supportive of a pilot implementation phase, to allow time for the ESAs to develop and test the relevant IT infrastructure on information disclosed under a limited number of specified regulations, such as the Prospectus Regulation.

Integration through removal of longstanding barriers

These include differences between civil liability regimes, insolvency frameworks, withholding tax procedures and completing the single market for depositaries. Meaningful progress on these topics has been slow, even though there is widespread recognition of these barriers.

Targeted changes to civil liability regimes to help issuers provide forward-looking information to investors

These regimes relate to the liability of an issuer (or other person such as an adviser) for the information disclosed to investors and are therefore important to ensuring suitable investor protection. Targeted changes could to these regimes could be impacftul.

Investors find forward-looking information, such as profit forecasts, useful. Issuers however may be reluctant to provide this type of information if they are worried about litigation risks if the information (which is inherently uncertain) proves to be inaccurate.

One solution would be to modify the liability regime in the Prospectus Regulation, so the issuer would only be liable if they *knew that the forecast was incorrect or intentionally misleading*. The US currently follows this approach. In particular, this approach would help high-growth companies (which may not have a long track record) to tell their story to investors and thereby to raise capital.

9 ESAP Proposal, Explanatory Memorandum

4. Capital market integration

Targeted harmonisation of insolvency rules to support cross-border investment

The European Commission has proposed a directive harmonising certain aspects of insolvency law. The impact assessment notes: “The empirical analysis undertaken by the IMF identified that convergence in insolvency regimes would yield the *largest contribution to three key metrics of financial integration*: higher cross-border asset holdings, a reduction in cross-country differences in funding costs and improved risk sharing across EU Member States.”

It also notes: “Different insolvency regimes are not only an obstacle for intra EU capital flows. Non-EU investors are equally facing a fragmented insolvency regime when they intend to invest in the EU, which creates incentives for them to invest in larger national markets where they can realise scale effects. The fragmentation of insolvency systems disadvantages the catch up of smaller local capital markets.”

We are strongly supportive of the Commission’s initiative, due to the anticipated benefits for corporates and investors, and developing a more integrated market.

In relation to maximising the recovery of value, we support the introduction of an EU framework for pre-pack proceedings (where the sale of a business is negotiated before the formal opening of insolvency proceedings). This mechanism already exists in some Member States. Extending the mechanism across the EU would be a good example of an approach inspired by national measures.

The pre-pack rules would rightly include safeguards to ensure transparency and equal treatment of creditors. The proposal includes a requirement for court authorisation, which would however make the process longer and less certain. While court intervention would be appropriate in some cases, there should be flexibility for the parties to agree without it. In such cases, the process could be left in the hands of the appointed insolvency official, with oversight by the court where necessary.

Harmonising withholding tax procedures to promote cross-border investment

The Commission has proposed a Directive for faster and safer relief of excess withholding taxes. The explanatory memorandum states: “The proposed initiative will lead to costs savings for investors, *estimated approximately at EUR 5.17 billion per year*. This owes to the fact that investors will incur less compliance costs, will face less instances of double taxation and will be able to reinvest the refunded money in a timely manner. This initiative will thus tackle a structural, longstanding obstacle to cross-border investment and will help EU companies raise capital from a wider base of investors, which is a core CMU objective.” It also notes that the proposal *complements the Retail Investment Strategy* to empower consumers to take full advantage of EU capital markets.

These proposals have our strong support given the expected benefits for investors and for EU companies raising capital. In particular, the introduction of a common digital tax residence certificate and common reporting obligations for financial intermediaries will significantly streamline withholding tax refund procedures and help to ensure fair taxation.

In light of the important role of certified financial intermediaries in initiating relief or refund procedures on behalf of investors , we suggest that a greater emphasis be placed on achieving a consistent approach across the EU to the due diligence obligations placed on these intermediaries. To *achieve maximum benefits* from this proposal, Member States should therefore work towards an approach that provides clarity on key concepts such as beneficial ownership, financial arrangements and holding periods, ensuring the FASTER system will work in practice for investors as well as intermediaries.

“Having EU-wide data for investing and trading is critical to maintaining and reinforcing a virtuous circle between primary and secondary markets”

Completing the single market for depositaries to promote participation in funds

One of the EU's greatest assets is the single market. Similarly to the obstacles to a true single market for banking described earlier, more can be done to complete the single market for capital, for instance to encourage the establishment of funds such as ELTIFs across the EU[10].

The amount of capital invested via ELTIF products (estimated at around EUR 11bn at end 2022 by Scope Ratings) currently represents only a minor portion of the net asset value of all EU Alternative Investment Funds. Moreover, the ESMA ELTIF register shows that ELTIF products are domiciled in only four EU Member States (Luxembourg, 57; France, 21; Italy, 13; and Spain, 2).

This leads to the *question of what is holding back the development of ELTIFs* across the EU. Part of the answer can be found in the European Directives. A fund manager authorised under AIFMD or UCITSD is required to appoint a depositary for each alternative investment fund (AIF) or collective investment scheme (UCITS) it manages. This is entirely appropriate. However, there is an additional localisation requirement that the depositary should be in the same location as the fund. The localisation requirement is holding back the development of ELTIFs because the local depositaries (for example, in the CEE region today) may not be capable of providing the services. Depositaries in other Member States have these capabilities. The solution is straightforward – extend the single market by allowing depositaries from other Member States to passport their services.

AFME recommendations:

Encourage Member State initiatives to develop their markets and seek to integrate so that European capital markets can develop at scale

- Promote the scale benefits of an integrated European capital market to Member States, corporates and citizens
- Encourage best practice sharing among Member States to develop domestic markets and investment, in areas where EU-level action cannot be as efficient, in particular in relation to the pensions challenge

At EU level, focus efforts in areas where rapid progress on implementation could be transformational

- Establish consolidated tapes and enhance the equity tape with additional levels of order book depth
- Implement the European Single Access Point
- Make targeted changes to civil liability to help issuers provide forward-looking information to investors
- Adopt changes to corporate insolvency rules and harmonise withholding tax procedures to support cross-border investment
- Complete the single market for depositaries to promote participation in funds

10 ELTIFs are collective investment vehicles that can raise capital from both retail and institutional investors willing to invest in projects that require long-term capital, such as infrastructure, real estate, transport and energy, as well as in smaller and mid-sized businesses.

5. Sustainable finance

Five years from its publication, the Action Plan on Financing Sustainable Growth has seen significant progress in its implementation. This has been marked by the adoption of flagship initiatives such as the EU Taxonomy, the Sustainable Finance Disclosures Regulation (SFDR), the EU Green Bond Standard and the Corporate Sustainability Reporting Directive (CSRD), as well as technical standards and guidance further specifying certain key concepts and methodologies. This has also been supported by integrating ESG risk considerations into prudential regulation and supervision.

Thanks to this intense regulatory activity, the building blocks for sustainable finance are now either in place or in the process of implementation. At the same time, the need to pursue further decarbonisation efforts will still need to be high on the policy agenda of the next Commission. The next mandate will cover a vital period for advancing real economy transition, as its end will coincide with the 2030 climate milestone. By then, the EU will need to have defined its 2040 climate goals and approached questions as to which potential new measures, or revision of existing ones, are needed to set the EU on track to meet its new objectives.

We believe that the foremost priority is for the EU institutions and Member States to continue to focus on putting in place the policies, roadmaps and incentives for *real economy businesses to be able to adapt.* This will in turn facilitate finance which will be available to support companies' investment and financing needs throughout the transition.

Transition finance

Transition finance, on a significant scale, will be vital to achieve the EU's climate and environmental commitments. We welcome initiatives on transition finance both in the EU and internationally, including work of the European Commission[11], G20 Sustainable Finance Working Group, OECD and others.

As these initiatives indicate, the importance of transition finance is increasingly recognised by policymakers. Banks and investors are also keen to scale the provision of transition finance and AFME members see the availability of credible and comparable transition plans as crucial in providing clearer signals in favour of transition financing.

We therefore encourage policymakers to continue to focus on providing guidance on decarbonisation trajectories and roadmaps for different sectors of the real economy. Clarity and consistency in the concepts and expectations underpinning different transition plan frameworks are key to this task.

Ensuring the existing framework is achieving its objectives

The Sustainable Finance Package, released in June 2023, combines the emphasis on transition finance with the need to ensure the usability of the current framework in practice and the coherence of its components. We welcome the work of the Platform on Sustainable Finance to review the usability and coherence of the regulatory framework. This workstream resonates with our views on the importance of assisting market participants in the implementation of the key pillars of the EU Sustainable Finance framework and of measures to clarify the existing toolkit, along with targeted changes to promote its effectiveness.

Any evolution of the sustainability reporting framework (including any simplification) should be considered alongside the regulatory framework for banks, including with regard to the prudential framework.

"It is crucial that the EU institutions and Member States focus on putting in place the policies, roadmaps, incentives, mandates and investments for the real economy to have the information, the tools and incentives to adapt their businesses"

11 Commission Recommendation on facilitating finance for the transition to a sustainable economy, June 2023

Carbon pricing

As Commission President von der Leyen has recently highlighted[12], carbon pricing is one of the most effective tools to drive decarbonisation in a way that nudges polluters to pay for their pollution and encourages participants to innovate. AFME welcomes the steps taken to broaden the scope and ambition of the EU Emissions Trading Scheme and encourages the Commission to continue to consider opportunities for its further strengthening.

Alongside compliance carbon markets, voluntary carbon markets have an important role to play in supporting the transition. We encourage the Commission to explore the development of voluntary carbon markets with international partners to allocate investment towards low-carbon projects, renewable energy and energy-efficiency initiatives, among other sustainable practices, including in jurisdictions where there is no compliance market for carbon pricing.

International coordination

While the EU continues to lead in many areas, we have seen a significant increase in other jurisdictions establishing their own regulatory sustainable finance frameworks. This trend increases the relevance of efforts to maximise the interoperability of existing frameworks and emerging issues, such as transition planning, leveraging international standards where possible. It is also important to ensure EU regulation does not unintentionally decrease the international competitiveness of EU companies and financial institutions. We encourage EU policymakers and regulators to increase their cooperation with other jurisdictions, including through fora such as the G20, IPSF, NGFS and ISSB Jurisdictional Working Group, among others.

AFME recommendations:[13]

Ensure that the sustainable finance framework achieves its objectives

- Focus on establishing roadmaps and incentives for the real economy transition, which will in turn facilitate sustainable finance, including transition finance
- Address usability challenges in the current framework, such as those associated with the do no significant harm criteria in the Taxonomy, the Sustainable Finance Disclosure Regulation, banks' Green Asset Ratio and other disclosures
- Ensure that regulation is promoting investment and does not adversely impact the competitiveness of financial institutions or companies operating in the EU and internationally
- Enhance international coordination and improve international interoperability with other key jurisdictions
- Continue to work to strengthen the EU Emissions Trading Scheme and increase the policy and regulatory support for the role and development of voluntary carbon markets in the EU, while enhancing cooperation with other jurisdictions

12 **Speech at the Summit for a New Global Financing Pact**, June 2023

13 These recommendations are further elaborated in AFME's separate publication "Sustainable Finance in the EU: Priorities to unlock financing and investment", November 2023

6. Efficiency and competitiveness

The integration and scale benefits of a single European capital market discussed earlier will contribute to improving the competitiveness of the EU economy. This is why they require full political support at the highest levels as the current context likely demands that an even greater emphasis be placed on the policy goal of strengthening the attractiveness and competitiveness of the EU.

In this section, we highlight additional areas which we think could help boost competitiveness.

Harnessing technology to provide more liquidity in certain asset classes and reduce costs for end-users

DLT and tokenisation in capital markets

From the perspective of end-users of capital markets, the development of Distributed Ledger Technology ("DLT") holds promise for driving growth by making it easier for a broader range of real economy actors to access capital markets.

For investors, tokenisation can increase the liquidity of traditionally illiquid assets, and through the "fractionalisation" of ownership of such assets, provide access to a wider range of investment opportunities.

From an operational perspective, payments, settlement and securities lifecycle events could be accomplished with greater safety, more efficiency and improved liquidity. Recognising this potential, in addition to its well-known work on developing a retail CBDC, the ECB together with industry is investigating the application of DLT in wholesale markets.

At scale, these developments could have significant benefits for the real economy and increase the ability of the financial system to allocate resources more efficiently. The recent GFMA Report on "*The Impact of Distributed Ledger Technology in Global Capital Markets*", highlighted that through the tokenisation of illiquid assets DLT could unlock transformative benefits including c. €18 billion annually in global clearing and settlement costs as well as innovation, through establishing a global market for tokenised illiquid assets which could be worth c. €14.5 trillion by 2030.

Other technologies

Cloud services and Artificial Intelligence are among the new technologies having the main transformational impacts on capital markets and both are expected to yield cost savings that can be passed on to clients as adoption becomes mainstream.

DORA has introduced an effective regulatory framework for banks' use of cloud services. Recognising that access to the most advanced technology and geographical diversification are key factors in ensuring competitiveness and resilience for banks operating in the EU, policymakers rejected any approach imposing strict localisation requirements for cloud providers. It is crucial this is not undermined by introducing alternative forms of digital sovereignty requirements, for instance in the context of the EU cloud certification scheme (EUCS).

Maintaining global competitiveness by improving settlement efficiency

Settlement is a critical step in the securities trade lifecycle, representing the point contractual obligations agreed at the time of trading are discharged. Although the vast majority of securities transactions settle on time, it is generally accepted that settlement efficiency is lower than in other jurisdictions such as the US. There are more settlement fails, which introduce additional risks, costs and inefficiencies.

Improving settlement efficiency was a core objective of the Central Securities Depositories Regime and this aspiration is shared by AFME and its members. AFME has established a Market Settlement Efficiency Task Force to report on inefficiencies and provide recommendations to address them.

Recommendations can be broadly divided into three categories:

- Reducing exceptions by addressing known data quality issues and expanding use of common platforms and standards for exchanging trade and settlement information.
- Expediting resolution of exceptions through increased transparency throughout the chain of intermediaries, including eventual adoption of a unique transaction identifier, and ensuring consistent matching criteria, thresholds, and static data.
- Optimising settlement of available inventory by increasing the availability and usage of partial settlement functionality, and where necessary increasing the frequency and timing of CSD settlement batches.

AFME considers that progress in these areas would facilitate the potential adoption of a shorter settlement cycle in the EU. The US will adopt a "T+1" default cycle in May 2024, which the US industry believes will reduce counterparty risk across the ecosystem, resulting in lower margin requirements and therefore cost savings. US participants anticipate T+1 will serve as a catalyst for increasing levels of post-trade automation and standardisation. They anticipate several challenges due to the compression of core processes into a much shorter window, and impacts on supporting processes such as securities lending, foreign exchange, and corporate actions.

Many of the benefits and challenges articulated by the US industry would also be applicable if the EU were to adopt T+1. However, given the unique nature of European markets – which, in comparison to the US, have a multitude of currencies, market infrastructures, and distinct legal frameworks – AFME considers implementation could be more complex. There is more to consider, more to change, and more actors to coordinate. Moreover, different implementation dates between the EU and connected jurisdictions such as the UK and Switzerland would create additional complexities, and therefore it may be beneficial to aim for a harmonised implementation date.

Accordingly, AFME has established an industry task force on T+1 settlement to assess the potential to shorten the settlement cycle in the EU.

Liquidity is key to closing the (public) equity gap

Home grown unicorns and their exits on public markets within the EU

As noted, the size of EU equity markets does not compare favourably to other global capital markets, and is small in comparison to the size and breadth of the EU economy.

The Commission has proposed a package of measures to make it easier for companies to list in the EU. We are supportive of introducing multiple vote share structures, which can provide an effective way for all innovative high-growth companies (not only SMEs) to access the market.

The package also includes changes to the content and format of prospectuses to reduce the burden on issuers. The Commission has a difficult balancing act to make it easier to access markets while ensuring investor protection. We have proposed that issuers continue to have the flexibility to provide a full explanation of their business to potential investors.

We are also not convinced that changes to disclosure requirements are addressing the underlying problem. EU corporates are seeking initial public offerings ("IPOs") outside the EU (see Box below), despite disclosure, accounting and reporting obligations being significantly more demanding and costly than the existing EU requirements.[14] When admitted to trading in EU markets, EU corporates tend to also pursue an additional listing on a foreign market to access bigger pools of liquidity.

14 "Primary and secondary equity markets in the EU – Final report", Oxera Consulting LLP, November 2020.

EU company IPOs in third countries

Although the number of cross-border listings within the EU has been decreasing, the number of EU companies seeking to list outside the EU has been increasing. Since 2010, there have been 40 IPOs of EU-27 companies in the US compared to only one US firm conducting an IPO on an EU-27 exchange. Over the same period, 110 EU companies sought a UK IPO.

There have also been some highly publicised examples of EU-27 companies seeking direct listings on US exchanges in recent years, including some of the most innovative and globally successful EU corporations.

Ferrari completed its IPO on the NYSE in 2015 and Spotify listed on the NYSE through a direct listing in 2018. The US market is also very attractive to EU biotechnology companies. BioNTech successfully completed its IPO in the US in October 2019 and it is now one of the biggest German listed companies by market capitalisation. Another German biotechnology company, CureVac, IPO-ed in the US in August 2020 despite German development bank KfW investing EUR300m in a 23% ownership stake and the massive EIB investments in its development.

More than 100 EU companies have a primary or dual listing in the US. Issuers state that access to capital, and specialised and knowledgeable investors, drives listing in the US.

One of drivers of this trend is the potential for higher valuations in markets that benefit from international pools of capital and highly liquid secondary markets.

The European liquidity landscape is concentrated on national trading venues[15] and therefore remains fragmented along national lines, acting as a drag on the attractiveness of its markets. Its complex structure is difficult for investors to navigate and keeps trading costs high, which negatively impacts returns. The EU should seek to break this cycle and create a more virtuous one.

The EU is not lacking in R&D and innovation capabilities, whether measured by its talent pool (STEM graduates), number of patents or unicorns. However, to scale up and build future corporates we also need to attract significantly larger pools of investors and liquidity. The role of liquidity – in making the EU's markets attractive to investors and the location of choice for growing businesses – should not be neglected in upcoming policy conversations. It will be a determining factor in attracting capital to the EU for its investment and innovation needs and will contribute to building its financing capacity and overall competitiveness.

Fostering the development of a pan-European ecosystem of market infrastructures supporting secondary equity markets will help achieve this. Several options exist, including promoting open access and interoperability links between equity CCPs, facilitating cross-border mergers at the market infrastructure level[16], or putting technology in place that could overcome the costs of fragmentation.

Moving into the next legislative cycle, we invite European policymakers to map existing European market infrastructure and establish a new vision for improving efficiency and other measures in support of improving liquidity.

"To scale up and build future corporates we also need to attract significantly larger pools of investors and liquidity"

15 According to Oxera report "Understanding the Liquidity Landscape in European Equities Markets" for the first six months of 2020, 81% of addressable liquidity was executed on-venue, 13% on systematic internalisers and 6% over the counter (OTC).

16 Along similar lines, Oxera on "Primary and secondary equity markets in the EU – Final report", Oxera Consulting LLP, November 2020

IPOs can be for many, but not for all

The bar is rightly high for taking a company public and should remain so to meet investors' informational needs and ensure public companies are subject to the highest corporate governance standards. IPOs are an important route for European corporates, but other financing solutions are also necessary (e.g. when a company is not large enough to list) for the European economy to transform at the scale required to meet its climate goals and remain globally competitive.

The public sector can play a role in attracting private capital to finance certain projects and corporates that may be deemed too risky without some level of co-investment or enhancement. With stretched public finances, it will be critical to review EU and Member State funding programmes to ensure they achieve their full potential. Policymakers could also review Member States' pandemic-related recapitalisation programmes to see if they could be redeployed to face the new financing challenges.

Policymakers may also wish to revisit the development of an equity-like hybrid EU-level instrument to cater for corporates that cannot access capital markets. The scale and liquidity of such a market would be significantly enhanced by an instrument with standardised contractual terms, features and tax and accounting treatment at the EU level. AFME has offered a blueprint for creating an EU-level programme of this nature, which could be revisited.

Individual listing is unlikely to be cost effective for most SMEs, and investors would be more likely to invest in a diversified pool of SMEs. Again, to achieve scale, the instrument would benefit from being coordinated across the EU. The securitisation market could play an important role.

Securitisation as a tool to bridge bank and market funding

Securitisation can make a vital contribution to Europe's substantial financing needs in the coming years, including those arising from the green and digital transformations. It is the only financial technique which enables financial institutions both to recycle capital and finance additional lending to households and small businesses.

Securitisation (either by transferring assets or risk) can be used to finance SMEs' working capital and leases of essential assets, such as low-emission vehicles, solar panels and energy-efficient manufacturing equipment. It can be a powerful tool to scale up ESG transition financing, especially as 44% of the funding required to meet the Paris 2°C requirements will be required in the form of loans to businesses and households[17].

The absence of a well-functioning securitisation market is a strategic loss to the European financial system. It is undermining the competitiveness of European financial institutions and limiting their ability to recycle capital to support new financing. It has encouraged institutional investors to shift towards products that do not offer the same protection, transparency and liquidity advantages.

Securitisation rightly constituted one of the elements in the second CMU Action Plan, as part of the 2019-2024 Commission mandate (after featuring prominently in the first CMU Action Plan). Despite an active policy agenda and several regulatory milestones, the work programme in this core pillar of the EU capital markets strategy arguably remains incomplete.

We therefore consider that securitisation should be a central aspect of the next policymaking phase. We base this assessment on (1) the unique contribution that well-functioning securitisation can provide to meeting the most important challenges facing the European financial system, and (2) the need to undertake further targeted work on aspects of the regulatory framework. Further recalibration is needed to enhance risk sensitivity, proportionality and usability in specific regulatory areas.

17 GFMA-BCG Report "Climate Finance Markets and the Real Economy" (December 2020) – available here.

6. Efficiency and competitiveness

Banking framework

We strongly welcome the transitional measures agreed in the EU's CRR3 package, which will support the economic viability of the risk transfer securitisation that will play a fundamental role in financing large and small European businesses. Following the review clauses included in CRR3, the next mandate should work towards a stable and better calibrated capital and liquidity treatment for securitisation in the banking framework at the European and international levels.

Solvency 2

The coming policy period should prioritise further work on the prudential treatment of insurance companies investing in securitised assets. A recalibration of the Solvency 2 capital charges on assets to levels that are proportionate to risks is a condition for the return of the insurance sector as investors in securitisation. Without a more risk-sensitive calibration of Solvency 2, there is no economic rationale for this non-bank industry sector to invest, despite the many advantages that securitisations could offer.

Review of the Securitisation Regulation

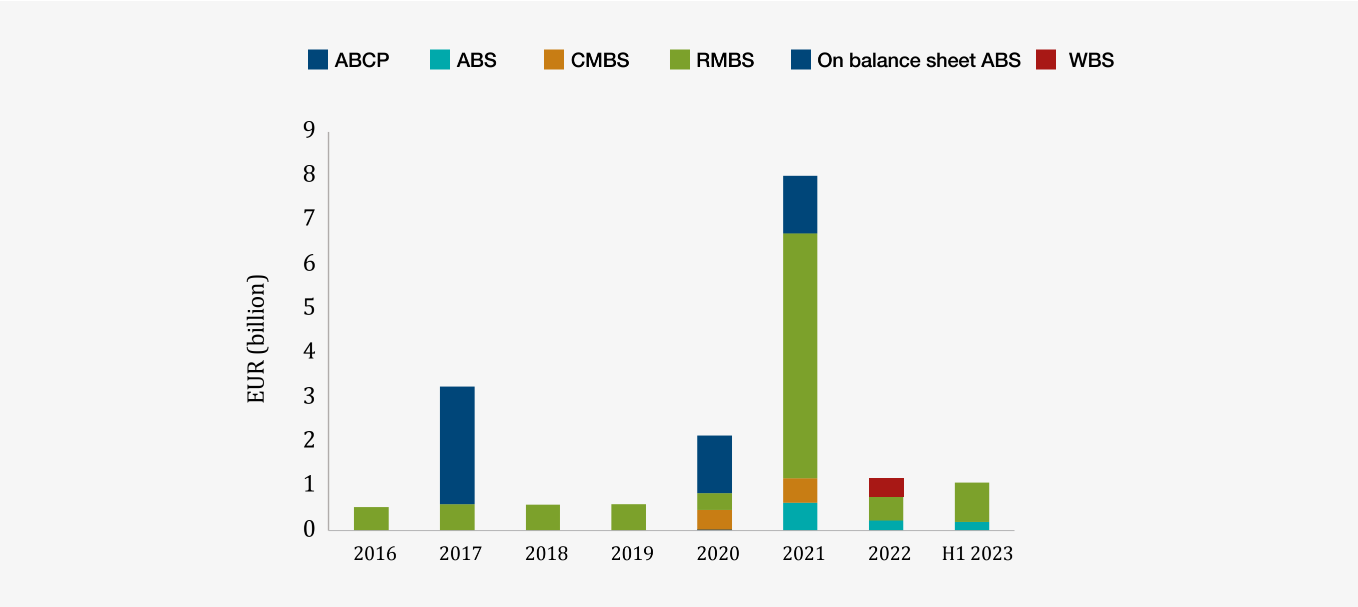
While the Commission decided not to undertake a general review of the Securitisation Regulation Level 1 requirements within the 2019-2024 mandate, we believe such a review is fundamental to support investors' return to the product. Specific aspects of the framework continue to pose major challenges to existing market participants and act as a fundamental barrier to new entrants. The proportionality of investor due diligence requirements should be among the areas for consideration, as discussed in this AFME **paper**.

We welcome the Commission's invitation to ESMA to streamline disclosure requirements, which are widely seen as burdensome for issuers and unhelpful for investors. This should continue to be a priority. An appropriate differentiation between disclosure and due diligence requirements for public and private securitisations should be a central component of this work.

Support the nascent ESG securitisation market

Following the adoption of the EU Green Bond Standard, the next legislative cycle should maintain a strong focus on supporting the nascent ESG securitisation market. One priority should be to support the development of a green framework for synthetic securitisation, which is the most cost-effective way of securitising project finance for green assets that cannot be easily securitised via true-sale securitisations. Their appropriate integration into the framework for ESG-related securitisations is therefore a priority.

Figure 5: **European ESG securitisation issuance**



Source: AFME

Ensuring that EU rule-making processes are fit for purpose

The current context requires that a greater emphasis be placed on the policy goal of strengthening the attractiveness and competitiveness of EU capital markets, making assessments in line with existing Better Regulation principles.

While the process of rule-making itself is by far not the sole contributor, it does play a role in the competitiveness of capital markets. In particular, well-functioning markets which attract capital and liquidity tend to be characterised by rule books which can evolve rapidly in line with market developments. Importantly, such rule books are capable of being adapted as needed to cater for stress situations, Successive external shocks have characterised the current EU legislative cycle. and, while pandemic-related "quick fixes" for instance have been put forward as a good example of the ability of the EU's legislative making process to address such situations, continuing to rely on the full mechanism involved in a level 1 process at EU level in its present set up could hold back some of the progress desired.

The current framework provides for strong democratic control and, arguably, legal certainty once a level 1 process is concluded. However, there may be other means by which the same goals can be achieved. Greater delegation of powers to the Commission and other European regulatory bodies who are accountable to the co-legislators within the context of mandates designed by the latter is a path forward which, although likely to be controversial, merits reconsideration before the next legislative cycle begins. In turn, this also implies that the regulatory community will need to have the right expertise, monitoring tools and regulatory powers at its disposal to discharge its responsibilities. Finally, for such a system to be effective, the existing governance arrangements of the ESAs would also need to change, for instance by including independent members on the Board of Supervisors.

AFME recommendations:

Make markets more efficient for the benefit of corporates and investors

- Harness technology to improve liquidity in certain asset classes, provide access to a broader range of opportunities to investors and reduce operational costs to the benefit of end-users
- Maintain global competitiveness by continuing to improve settlement efficiency in the EU and assessing the potential to shorten the settlement cycle
- Monitor the impacts of transparency requirements on market-makers' ability to provide liquidity in fixed income instruments
- Raise the prominence of improved liquidity in secondary markets to a core, stand-alone EU policy objective in order to attract domestic and international capital pools and grow listings on EU public markets
- Review the financing toolkit, including new EU-wide hybrid instruments and public/private partnerships, which allow for scaling up market-based finance at pace
- Adjust the regulatory framework for securitisation to combine the advantages of efficiently deploying bank lending and market-based financing of the real economy
- Ensure that the rule-making process, based on the Better Regulation principles, can be responsive to the changing economic environment

7. Annex: Global capital market development metrics

	US	EU	UK	Japan	China
Macro					
GDP ($tn, 2022)	23.3	17.1	3.1	4.9	17.7
GDP (% world's total)	24%	17%	3%	5%	18%
Banking					
GSIB pre-tax RoE (3Y avg)	11.2%	8.7%	7.7%	7.2%	13.1%
Total bank assets (% GDP, 2022)	98%	193%	323%	231%	305%
Total bank assets (% global, 2022)	14%	18%	4%	6%	29%
Primary markets					
IPOs (3Y avg, % GDP)	0.3%	0.1%	0.2%	0.1%	0.3%
Corporate bond issuance (%GDP, non-financial, 2022)	2.5%	1.5%	2.3%	1.6%	3.2%
Green bond issuance (% GDP, 2022)	0.1%	1.4%	0.4%	0.4%	0.6%
Securitisation issuance (% GDP. Ex-US agency, 2022)	4.0%	0.3%	0.9%	1.1%	1.8%
Secondary markets					
Equity turnover ratio (annual turnover/market cap, 2022)	3.5	1.5		1.4	2.6
FX trading ($tn per day, 2022)	1.9	0.8	3.8	0.4	0.2
Market cap (% GDP, 2023)	188%	66%	98%	114%	64%
% world's market cap (2023)	50%	13%	4%	6%	13%
Pools of capital					
Household savings rate (pre-covid)	8%	13%	6%	4%	35%
Household financial assets (% GDP, 2022)	490%	221%	324%	411%	30%
% HH financial assets saved in cash & deposits (2022)	14%	32%	27%	55%	57%
Digital					
FinTech Unicorns (number, 2023)	107	20	20	1	9
FinTech Unicorns valuation (% GDP, 2023)	1.6%	0.3%	3.8%	0.02%	0.1%

Sources: AFME research based on data from World Bank, Eikon, ECB, NYFed, UK Finance, US Fed, BoJ, Dealogic, SIFMA, JPM, BofA, S&P, JSDA, BigXYT, WFE, FESE, BIS, Eurostat, CEIC, Japanese Cabinet Office, OECD, Seafarer, CBinsights, Chinese Centre for National Balance Sheet. Bank assets and household savings for China are the latest available (2019).

Notes

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