AFME's 15th Annual Spanish Capital Markets Conference

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Good afternoom

First of all, I would like to thank AFME for the invitation to this conference devoted to Spanish Capital Markets. I think that the reflections that are being developed here today are specially relevant given the situation of our markets.

Precisely these weeks we are in the process of elaborating the 2023 CNMV Annual Report and I have to admit that these last years it has been a bit of a not very optimistic task. The numbers about IPOs, issuances of equity and fixed income as well as of volumes traded in secondary markets are getting lower and lower and we should not, we cannot just accept this situation. We have to react.

Nevertheless, I am afraid that this situation is not only applicable to Spanish markets but, until a certain degree, also to all of Europe.

In this sense, an European course of action to try to revitalize our financial markets is more than necessary. This leads me to talk about the main European project in this regard: the CMU. Given the importance of this project and the massive consequences it has, or it can have, on Spanish capital markets, I would like to use this time to deepen a bit into this plan.

I) WHY NOW

Firstly, let me start by asking "Why now".As we all know, the CMU is not a new project. It may cause a bit of melancholy but the truth is that we have been discussing the way to foster capital markets for, at least,more than 15 years.

However, the problems which led to its creation still persist today and achieving a stronger European capital market is now more important than ever.

Besides the normal function of markets and the need to have a diversified funding mix that can fulfil companies' needs, contribute to economic growth and foster financial stability, capital markets are an **essential piece in the access to long-term finance** that European companies will require in this decade. The unprecedented levels of additional investment needed for the de-carbonization of our economies and other strategic priorities like the digital transformation cannot be financed with recourse to public budgets or bank loans alone.

European companies (including the Spanish ones) will have to **increase significantly their equity in order to strengthen their balance sheets and also to be able to absorb new loans for those massive investment projects**. Therefore, the provision of equity and long-term debt by capital markets is a must and should constitute a strategic priority for the European Union. Without much deeper capital markets, our economies will fail to transform on time.

Besides that, a bigger participation of european citizens in capital markets would undoubtedly imply an improvement in the long term profitability of their savings. It is clear that we are currently in a suboptimal situation in this regard.

However, as I was saying, the problem is that despite the efforts made**, capital markets have not developed sufficiently in the EU in the last decade.** This leads us to the second question: What has been done so far and which problems persist.

II) WHAT HAS BEEN DONE AND CONSEQUENCES

As you know, the Capital Markets Union (CMU) was launched in 2015 as a plan to create a single European capital market. The aim was to get money – investments and savings – flowing across the EU so it could benefit consumers, investors and companies, regardless of where they were located.

Among other aims, a capital markets union would provide businesses with a greater choice of funding, offer new opportunities for savers and investors, reinforce the EU's global competitiveness and autonomy and make the financial system more resilient. While progress has been made since its launch, some of the fundamental problems persisted.

Since then, around 61 measures have been included in the different action plans. So far, the EU has delivered all 12 out of 13 legislative measures from the first CMU action plan as well as 13 actions from the second action plan.

Some of them stand out such as: the MiFID revision, the approval of the ELTIF Regulation or the introduction of the pan-European personal pension product (PEPP). And since the 2020 Action Plan has been implemented, a lot of really important initiatives as the amendments in MiFID/MiFIR, EMIR, AIFMD/UCITS, the Listing Act or the RIS have just been approved or are even still in the pipeline.

So I think that it is important to emphasize that we need to wait some time before we can actually see their impact on markets. After all, this is a long-term plan, which will take time to materialize in terms of market momentum. In connection with this, I think it could be a good moment to perform some **diagnosis about the current situation of capital markets** in Europe and analyze the problems that persist.

Firstly: European capital markets are still underdeveloped

In terms of capitalization over GDP, we can observe that we are far away from for example the US or other areas (we are talking about figures of 65% vs more that 150%).

Regarding primary markets, especially equity markets, they are not providing a large-enough share of the funding that EU companies need. The number of new companies taping markets (IPOs) has declined in the EU since 2008. If we add this fact to the exclusions from trading, the consequence is a sharp decline in the number of listed companies in the EU (from more than 12,600 in 2008 to 7,000 in 2023).

Secondly: some cross-border investment barriers persist

The CMU Action Plan has not resolved the main barriers identified as potential impediments to cross-border capital flows. These barriers are often caused by national laws, such as those in the fields of insolvency and fiscal rules or from a lack of financial education.

Nevertheless, despite these existing barriers, capital markets in the EU are already quite integrated. Way more than banking markets.

Using Spain as an example, the proportion of ownership of listed companies by non-residents is more than a 50% and holdings in Spanish sovereign bonds by investors in other countries represents more than 40%.

Cross-border competition in investment funds is also high: close to half of UCITS bought by Spaniards are not manufactured and managed in Spain. And more than half of fixed income securities of Spanish companies are issued out of Spain.

Therefore, it can be observed that **there is a high degree of cross border financial flows** even though there are many voices claiming that we have a serious problem of fragmentation in our markets.

If we look at secondary markets, specifically to equity trading venues, it is true that we have national markets and also trading platforms with a big share of the total volumes traded in almost every stock in the EU. This could be considered a problem but, on one hand, **competition among trading venues has brought benefits to investors**, in the form of diminishing execution costs and improved service. And, on the other hand, many other economic areas with more active primary and secondary markets, including the US, show **high trading fragmentation and competition** and, still, impressive depth of capital markets. In any case, experiences of consolidation in this area have not proved to have a direct impact in terms of growth of markets.

Having said that, an area in which there could be more potential benefits from a higher degree of integration or at least from a better linkage between infrastructures is the field of post-trading (CCPs and CSDs). In the EU we have a really big number of CCPs and CSDs and this fact does not compare well with the situation in the US where they have just one CCP for equity and just one CSD.

Thirdly: there are structural features that hinder market development

It is also very obvious that there are structural features like the size of companies, with a predominancy of SMEs in Europe (even more in Spain) or the risk profile of investors, pretty conservative in many countries in the EU, that imply constraints to the development of markets.

And finally: we still face a supervisory model issue

A number of proposals recently issued or published put this matter in the centre of the CMU debate. And, more specifically in the idea of ESMA centralizing supervisory powers in the EU.

ESMA assuming even more tasks is a relevant and pertinent debate. First we have to acknowledge that the creation of this authority in 2011 and all the impressive work that it has developed since has implied a big step in the good direction of having a single rule book and a high degree of supervisory convergence in the field of capital markets.

Although there is still significant room for a bigger use of ESMA's tools and powers, centralization of supervision in ESMA in some additional areas of EU financial markets could bring some relevant benefits, but it is hardly a silver bullet to attract companies in large numbers to capital markets or foster investment and should not be the main policy driver if our objective is the growth of markets. The potential benefits of this course of action are more focused in investor protection or financial stability.

The main case for centralization would be located on market segments where we have few systemic participants with significant cross-member State presence, that are regulated only or mainly by EU regulations, with little connection to local legal specificities or, more generally, where there is a high risk of regulatory arbitrage.

This is not typically the case of the rules applicable to locally listed issuers or to the retail distribution of financial products, where national supervision could be more effective.

But it could be the case of other segments like CCPs, manufacturing and product governance, some relevant securities' issuances or services around cryptoassets.

Nevertheless, EU markets have been more active in the past, even with the same supervisory structure as of today, and some national EU markets (take Sweden as an example) show excellent dynamism in spite of fragmentation or the supervisory structure in the EU.

Taking all this analysis into consideration, **what can be done to really promote capital markets?**

III) POSSIBLE SOLUTIONS

First, a **re-branding towards Capital Markets Growth (CMG) would probably help to put the focus where the problem lies**. As I was saying what is missing from European capital markets is sufficient growth and weight of markets.

Too few EU companies choose capital markets to obtain finance and too few Europeans choose financial instruments to invest their savings. Those two dimensions should be the main focus of EU policies. There is a need to identify the right incentives to attract more companies and more investors to capital markets.

In this sense, there is a number of proposals that are being published these days. Just as examples I could mention the recent Eurogroup statement or the report led by former Italian prime minister Enrico Letta that was published yesterday. I think that many of these proposals could deserve consideration and I would highlight some of them.

A) TO ATTRACT COMPANIES TO CAPITAL MARKETS

Lets start by looking into how we could attract companies to capital markets.

1) **Addressing tax asymmetry:** Addressing tax asymmetry is paramount for encouraging companies to choose equity financing over debt.

   By providing a more favorable tax framework for equity financing, policymakers can create incentives for companies to strengthen their balance sheets through equity, contributing to a more resilient and well-rounded financial ecosystem.

2) **Promoting markets among companies:** European companies, and specially SMEs tend to have less recourse to capital markets financing. This can partly be explained by cultural factors. Unlike the US, European companies have traditionally tended to finance themselves through loans and feel safer by doing so.

   Public institutions should actively communicate the merits and advantages of engaging with capital markets, encouraging more individuals and companies to view participation in markets as a strategic financial decision.This would also incentivize long term companies growth.

3) **Reducing Costs and Harmonizing Access Rules:** To further lower barriers to entry, it is necessary to reduce costs associated with access to capital markets.

   Additionally, harmonizing access rules, particularly regarding information provided to supervisors and advertising materials, can simplify the process for companies and create a more streamlined and accessible capital market environment.

4) **Creating Equity-Qualified Segments:** The creation of equity-qualified segments, with less reporting and trading obligations could attract companies seeking to enter the public domain without being or feeling overwhelmed by strict reporting and free float requirements.

B) ATTRACT INVESTORS TO CAPITAL MARKETS

But actions also need to be taken in order to attract investors to capital markets. There are a number of proposals in this direction that could be useful. For example:

1) **Establishing tax incentives for investors:** We could get some inspiration from successful experiences like the U.S. 401(k) or the Swedish IPA, to make

investment in capital markets more appealing by providing financial benefits to investors.

One potential idea inspired on the previous ones would be to have an European investment account with which investment would be possible in a wide range of financial products differing taxation to the moment of exit.

Another fundamental step in the taxation area would be to simplify and make more agile all related to tax withholdings across the EU and the different financial products.

2) **Encourage pension funds to play a more active role as long-term investors in capital markets** would also be a key element. By aligning the interests of pension funds with the growth and stability of capital markets, policymakers could ensure a reliable source of long-term capital, contributing to the sustainability and resilience of the financial ecosystem.

3) **Enhancing investor knowledge and facilitating investment recommendations.** An educated investor base could contribute to a healthier and more resilient market. It is important to improve financial literacy but also to try to change investors' culture making them understand and consider investments of which they have sufficient information and analysis.

4) **Boosting a more diversified distribution model**
We could also make a reflection about the potential benefits of having a more diversified distribution model in terms of a wider variety of financial intermediaries, avoiding the risk of conflicts of interest or oligopolic behaviours and enhancing the offer available to investors.

CONCLUSION

I will conclude now.

From the CNMV we call to **shift the narrative from consolidation and centralization to fostering growth of markets.** We definitely advocate for targeted policies that incentivize both companies and investors. By addressing the causes of the underutilization of capital markets by companies and the lack of investor participation, this shift aims to create a more dynamic and resilient market.

I hope you will have an excellent conference and I thank you for your attention.