“Deeper capital markets in a new context"
AFME 14th Annual Spanish Capital Markets Conference

RODRIGO BUENAVENTURA, CHAIRMAN OF THE CNMV
18 April 2023

Good morning to all and thank you for your kind introduction. And thank you again to AFME for inviting me to participate, another year, in the event’s inauguration.

Last year I spoke about the relevance of the scenario we are experiencing where we are facing high macroeconomic uncertainties. After Russia invaded Ukraine thirteen months ago, there have been other factors which have influenced the economic situation in Europe such as high inflation rates, slower economic growth and a very stark shift in monetary policy, with significantly higher rates.

We continue to have very high investment needs (especially on green and digital); an ageing population; public finances in need of consolidation. In this context, deep capital markets, and especially equity ones, appear more important than ever. And, yet, they have been continuously shrinking in relative terms in the last 10 years. AFME has a very revealing graph in their CMU KPI report about the path of the percentage that EU GDP and EU market cap represents of the world. And the path is, to say the least, a bit depressing.

The relevance of the current moment along with the key role of capital markets was properly understood by the European Commission through its Capital Market Union initiative, which I will refer to later. In the same way, the Spanish legislator acted to stimulate markets with its recent modification of the Spanish Securities Market Law, now called the Securities Market and Investment Services Law (LMVSI for its abbreviation in Spanish) and which came into force a week ago. First, I would like to address this last issue.

One of the main objectives of the new text is to increase the Spanish securities market’s competitiveness. The regulation is improved, and the regulated matters are simplified and rearranged, adapting the national law to recent developments in European law that needed to be transposed.

Improving the competitiveness of our securities market requires greater simplification while maintaining investor protection. This is the reason why the new text incorporates several measures.

Admission to trading of bonds is simplified to the extreme: from now on, when a bond is issued in a program with a base prospectus, you don't need to come anymore to CNMV to admit it for trading. The reporting obligations of participants in Spanish post-trading infrastructures are also adjusted: in particular, the Spanish peculiar obligation of Central Securities Depositories to have an information system to supervise settlement, and registration, widely known PTI, is removed. We also have a new regime for the regulation of SPACs.

We have new measures to improve the competitiveness of the collective investment and investment services industry (introducing a new category of investment services firm called national advisory firm).

In terms of investor protection, the new text takes a step forward in its ongoing fight against financial fraud, introducing measures to prevent unauthorised entities to provide investment services in the European Union. From now on, internet search engines, social networks and media in Spain will have to actively check that the firm seeking an advert is properly licensed before publishing that advert.

The new law also allows Spanish markets to adapt to technological developments by introducing the possibility for financial instruments to be represented by distributed ledger technology (DLT).

Lastly, regarding the governance and effective independence of the regulator, the new text introduces improvements such as the establishment of six-year non-renewable mandates for Board members of the CNMV.

All these changes are aimed at making Spanish securities markets more competitive. And this same objective is shared by the Capital Market Union, led by the European Commission since 2015.

The European initiative was born with a twofold goal: on the one hand, to achieve greater market integration and, on the other, to make European stock markets larger and more attractive to companies and investors.

Throughout these years we have worked mainly on the first goal, to achieve the union and integration of the markets, but the time has now come to focus on growth because this objective is to my mind the real priority.

The regulation and supervision of securities markets is not at all as fragmented as it could be in 2015. Today, Member States have a harmonised regime by means of the European regulations in places where we used to have directives (or nothing). This is the case in matters such as registration and settlement (CSDR), prospectus (prospectus regulation), derivatives, registration, and central counterparties (EMIR), and trading and reporting (MiFIR). We have a single point of settlement in the Eurozone (T2S) and we have progressed towards real convergence in the supervision of securities markets by means of the new powers of the European regulator, ESMA. European issuers provide information to the market and develop their prospectuses in a very similar and aligned way in all EU countries. It is quite possible that further progress is needed in some areas, such as the development of a single point of access of issuer and product information or pending developments regarding consolidated tape, but these issues are more related with the information rather than market integration or structural changes.

However, the concept behind "Union", as applied to securities markets, bears a false resemblance to the concept of banking union, whose goal was to centralise supervision of the most relevant and systemic banks in response to past financial crises and the link between banking risk and sovereign risk. This has nothing to do with capital markets today. In fact, EU capital markets are way more integrated today than EU banking markets. All you need is to compare where investors place their savings (in funds investing across Europe) versus where depositors place their savings (in domestic bank deposits). Or compare the origin of shareholders of companies going public (a global origin) versus the origin of the bank financing of companies (almost exclusively a local origin). There is no such thing as an EU banking market, except for the top tier of very large corporates.

In stock markets, companies and investors are already free to choose the market in which they want to operate. Any European or Spanish company can issue and list bonds and shares in its own market or that of other European countries (and is not only that they can: they do that, freely). There are also companies of European origin listed in the Spanish stock exchange, and we have CSDs and CCPs from other Member States offering services in different countries. Spanish savers invest half of their assets in funds from other member states. There is no such thing as home bias in securities markets, at least in Spain: only 2,5% of the portfolio of Spanish investment funds goes to the Spanish equity market. The Spanish market is mainly serving EU and international investors, not Spanish ones.

In any case, if fragmentation was the problem, does it mean that we should reduce competition between execution venues, to concentrate liquidity in the main ones and eliminate Sistematic Internalisers and competing execution venues? I do not think so.

To me, it is all about incentives to go public. In terms of cost (as compared with debt and private equity), in terms of taxation, in terms of access to capital pools unavailable elsewhere, in terms of ways to maintain control by the founders and in terms of extra regulatory requirements (as opposed to not going public). And some countries, like Sweden, who face the exact same regulation as any other EU Member State and the exact same fragmented or non-fragmented trading environment, have managed to have vibrant primary equity markets in the last few years. We should probably take stock of those success cases.

I am convinced that our problem is not fragmentation or integration, which is reasonably high in the regulatory side, but the small size of the market and the lack of a strong linkage with the financing structures of companies. For this reason, the current objective should not be to achieve a perfect and complete integration, but rather develop deeper and larger markets. The concept of "growth" should take precedence over the concept of "union" and thus lead to measures that will make markets more attractive to companies.

The solutions to make securities market cheaper, simpler, more agile, and more attractive for companies and retail investors are on the table. Now it is time to apply them. Initiatives such as the Listing Act, AIFMD/UCITS reform, ESAP or the Retail Investment Strategy initiative are part of the solutions and must also accompanied by the balanced, intelligent, innovative and ground-breaking use of tax incentives (such as DEBRA).

Focusing on “g” of growth quickly, boldly and effectively is our only chance to revitalize this absolutely vital part of our economies. We need to triple the amount of market-based finance if we want to have balance structures as robust and resilient as US corporates and diminish the dependence of bank financing that EU companies still show and suffer.

On this effort, we should be very careful when adopting regulation of a non-financial nature. If we address non-financial rules (like sustainability disclosure, gender diversity or alike) only to listed companies, we will be creating a bigger divide between going public or not, but not linked to the interests of shareholders. If some matters (like GHG emissions, diversity or equality) are important for society as a whole, and they are clearly very important, let’s not regulate those only for listed companies. We will get smaller impacts in our societies, and we would create disincentives to go public.

Nonetheless, the development of securities markets, and therefore an increase in non-bank financing, should not be viewed as a problem but rather as a blessing for the Spanish and European economy. I say this because in recent months, we have been witnessing, more or less regularly, statements from various sources that identify non-bank financing with a growing source of systemic risk. Some of these statements are based on liquidity tensions on constant-value money market funds in March of 2020 or on recent events with liability-driven pension funds in the UK.

To me, it is remarkably striking that, with all that has been going on in the banking side in the last 5 weeks, some are still pointing at the investment funds as the source where risks will come from.

Of course, collective investment can generate risks. It would be foolish to deny that. For those of us old enough to have lived the crisis of LTCM, it is pretty obvious. But we have a decent understanding on where those lie: too much leverage, too little collateral posted, promises of re-payments (like CNAV MMFs of defined-benefit funds), poor liquidity management or poor supervision. And these risks are nowhere near universal. Some countries have acted decisively on those fronts.

Let me take Spain as an example. There are hardly any monetary funds in Spain, or at least none with a constant value. We do not have defined benefit pension funds, and the industry's leverage is certainly low. We have a strict liquidity management framework in place, with guidelines issued by CNMV last year. Since 1991, we have been receiving monthly information on a fund-by-fund basis for every individual asset they hold, which enables us to do proper preventive supervision, carrying out regular liquidity stress tests at both mutual fund and fund manager level.

The solution to the alleged systemic risk would not be to impose extraordinary liquidity buffers or capital buffers because funds should not be regulated as if they were deposits offered by banks. The solution lies on four key elements: (i) appropriate liquidity management tools available to managers and supervisors, (ii) a strict match between the liquidity of underlying assets and the fund liquidity windows, (iii) leverage limits and controls, (iv) and adequate monitoring and supervision of all those elements, based on transparency, reporting and supervisory data.

The European Union follows most of these approaches in the amendment of the AIFMD and UCITS directives, introducing liquidity management tools, like swing pricing or redemption windows, thus ensuring effective responses to liquidity pressures in times of market stress. They also impose a regular reporting regime to the supervisors to be developed by ESMA through technical standards, which I hope will benefit from the experience of the Spanish model.

Let me conclude now. Non-bank financing and the growth of securities markets must be fellow travellers, partners involved. And both are today, more than ever, necessary if we really want our companies to access deeper capital pools and broaden the investor base. The stakes are so high for our economies that we should make capital markets growth a strategic priority. I hope that in the upcoming AFME conferences in Spain, looking at how fast things change recently, we can celebrate a turning point on this.

Thank you very much.