FINANCIAL OBSERVATORY
Focus: investment and new trends

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Good morning.

I would like to thank El Español and Invertia for inviting me to participate in this event. It is a good time to debate, discuss and listen to the stakeholders in the sector in such an exceptional situation as the one we are living through.

The CNMV, as the supervisory of the financial markets, must always act with the three objectives assigned to it by the Law: investor protection, transparency of information and orderly functioning of the market. But in the current context, we must also facilitate financial markets as one of the tools to drive a sustainable and digital economic recovery.

The main lines of our strategy for the 2021-2022 biennium are based on this idea. Recently, we presented our Activity Plan to the public. We have defined four strategic lines of action:

- Firstly, implementing rigorous supervision based on investor protection and greater use of data.
- Secondly, boosting capital markets as a source of funding for economic recovery.
- Thirdly, facilitating the role of the stock market in the transition to a more sustainable economy.
- And fourthly, promoting technological developments in securities markets, and preventing their risks.

In our view, the above four lines of action outline the three major trends driving the securities markets, which I would like to discuss later, and explain the activities that the CNMV is carrying out in each of them. These three major trends are determined by:

1. Technological development and digitalisation processes as a factor of change.
2. The unstoppable transformation brought about by sustainability.
3. The road to a European Capital Markets Union and increasing retail investor participation and protection.

1.- Technological development and digitalisation

Over the last few years, we have witnessed an intensive application of new technologies in financial services that have led to the establishment of new lines of business, new products and new operators. Developments such as massive data processing and analysis, the use of artificial intelligence systems, cloud storage, robotisation of analysis, new transaction recording tools (blockchain) and tokenisation are causing significant changes in the financial sector and also in supervisors. This trend brings with it a cultural change that affects companies - which can improve their services for greater efficiency - and investors, who need to be better educated to understand the new approaches.

While new technologies allow investors a wider range of options, they are not without risks that need to be understood and monitored. The key is to strike a balance between promoting innovation, technological development and maintaining the integrity of securities markets and investor protection. The forthcoming implementation of European regulations (MICA and DORA) will cover these risks both in the area of so-called cryptoassets and in the increasingly important area of cybersecurity.

The CNMV is no stranger to this trend and is involved in promoting technological advances, in driving innovation applied to the securities markets and in its own digital transformation. In fact, our Activity Plan focuses on objectives such as, among others:

- The launch of the sandbox together with the Bank of Spain, the Directorate-General for Insurance and Pension Funds (DGS) and the Treasury through which, in a controlled test environment, disruptive technological projects will be developed.
- A three-year strategic information system plan to determine the CNMV's medium-term needs.
- Review of the security of market infrastructures and supervised entities against cyber-risks.
- A digital CNMV, with greater use of artificial intelligence and supervisory algorithms to enhance the institution's role.

One area that is generating supervisory and regulatory attention is cryptoassets. As you know, in February of this year the CNMV and the Bank of Spain issued a joint public statement warning of the risk derived from this type of asset, especially when offered as an investment. These are complex products with high risk and may not be suitable for small savers. Products whose price formation process is not transparent and involves a highly speculative component that can even lead to the total loss of the investment. Products as yet not covered by European regulation providing guarantees and protection similar to those applicable to financial instruments.

In recent months we have witnessed an increase in massive advertising campaigns, both in digital and physical media, about cryptoassets that include concepts typical of financial products such as "investment" or "profitability". The risk of this massive publicity and its effects on investors has led to a Government initiative to control the advertising of cryptocurrencies when they are offered as an investment, which, in my opinion, is appropriate and timely. As a result, at the beginning of March, a provision (Article 240 bis) was added to the SMA by which the CNMV "may subject to authorisation or other forms of administrative control (including the introduction of warnings) the advertising of cryptoassets or other assets and instruments presented as investment objects".

Article 292(4) has also been amended to consider as a serious offence the carrying out of advertising without respecting the requirements established. This reform, which is urgent and necessary, grants the CNMV the power to implement it through a Circular and we are already working in order to have a clear regulation for this advertising activity as soon as possible. We will therefore conduct a broad public consultation, consult our Advisory Committee and submit it to the Council of State prior to its adoption. **It is certainly important to act quickly, but it is more important to adopt the appropriate regulation**.

It is also necessary to emphasise that it is not the instruments (cryptocurrencies), nor the providers, nor the transactions that are subject to CNMV control, but only their advertising when they are offered as an investment alternative.

2.- Promoting sustainability

The European Commission has already detailed in its action plan for financing sustainable growth that it is necessary to promote the reorientation of capital flows to facilitate the achievement of this growth, to manage the financial risks arising from climate change and to foster transparency and long-term vision in financial and economic activities.

Many paradigms that were axioms in economics textbooks in the 1980s are now fading. For example, we were taught that interest rates were always greater than zero and macro textbooks had to be reprinted in the last decade. We also learned that investment theory was based on a risk-return spectrum. More and more institutional and retail investors are now including impact as a third axis of their management. What used to be the risk-return spectrum is now the risk-return-impact spectrum. We will probably see financial economics textbooks also being reprinted in the next few years.

This paradigm shift means that we are probably witnessing the beginning of the largest re-allocation of investment portfolios in the history of our markets.

The CNMV cannot be oblivious to this trend, and we must incorporate it into our planning. It is up to us to implement the framework to be developed in the EU for green emissions and other sustainability-labelled investment products and instruments, as well as for benchmarks that take into account the carbon footprint. All of the above must be done without discriminating against any sector, activity or participant.

Similarly, in order to promote transparency and the dissemination of non-financial information by issuers, there must be a clear and homogeneous legal framework that facilitates the comparability of such information and avoids fraud or greenwashing practices. In addition, financial market professionals and institutions are already incorporating ESG (environmental, social and governance) factors into their organisational requirements. All this will favour the channelling of capital flows towards sustainable investments.

In line with this trend, the CNMV will carry out various actions this year, including the following:

- A study on the issuance and marketing of sustainable financial products will be conducted.
- We will enhance financial education activities on sustainability, thereby improving investor education. A study on the integration of climate risk monitoring into prudential conduct and macro-prudential supervision will be carried out.
- We will improve the Sustainable Finance Portal in order to facilitate the dissemination of information and have greater capacity for interaction with the sector.

3.- The Road to a Capital Markets Union

The Capital Markets Union is an essential element for improving investment options and a more diversified financing of European companies. The basic idea is to increase the weight of stock markets in equity financing of companies (as opposed to bank financing via loans). This will bring three benefits: greater resilience of European companies in the face of future crises, greater growth possibilities for these companies (we have a problem of the average size of European and Spanish companies in particular) and greater opportunities for investors' savings.

Two recent factors illustrate and qualify this argument. On the one hand, the effects of the pandemic we are experiencing and the importance for issuers as a whole to have sufficient capital to cope with times of global uncertainty and for investors to build diversified portfolios. And on the other hand, Brexit itself, and the relevance of an adequate diversification of financial centres. It is important to understand that the capital markets union will be more robust based on several national financial centres rather than a single one. And all this is compatible with polycentric supervision, based on several national financial centres rather than a single one, but coupled with stronger coordination mechanisms and a stronger ESMA, the European market supervisor.

It is also advisable to reflect on how we can facilitate the incorporation of more companies into the market, mainly SMEs, as well as greater participation and prominence of retail investors. This reflection, in the interest of providing tools and alternatives to both companies and retail investors, should in no way prevent their combination from being carried out with care. Especially if at the same time a reduction of disclosure requirements by issuers is promoted.

The combination of more listed SMEs, more retail investors and relaxed market access requirements may be ingredients in a dangerous recipe for several reasons. Firstly, in the case of retail investors, because in some cases they lack the appropriate training and experience to evaluate new entrants. Secondly, the need for greater coverage of the analysis of these types of smaller companies. And thirdly, the fact that SMEs are more often subject to higher volatility, to a higher risk-return ratio and therefore to higher default rates, which makes them investments with an additional risk component.

The only smart way to promote the new flow of SMEs and more retail investors at the same time is probably to encourage retail investors to access this new market through collective investment. Collective investment schemes managed by professional managers provide both diversification, which is key when it comes to SMEs, and analytical capacity, which reduces risks and increases returns. In fact, this type of vehicle could even be encouraged by regulation as opposed to direct investment in the shares of individual SMEs. Collective investment vehicles could also contribute to professionalising SMEs through activism and shareholder involvement. It is clear that we need to attract more companies to the listed world, from all sides of the spectrum: large and small, traditional and innovative. To this end, it is appropriate to reduce the costs and time needed to access the market, but in doing so we must be careful not to diminish investor protection. The key to strong and stable capital markets is long-term investor confidence and the development, improvement and enhancement of appropriate financial education to enable all investors to better understand risk in their investment decisions.

What the health crisis we have been experiencing for the last year and its effects on the economy have shown is that listed companies and, in general, issuers in the stock markets have found a wider range of resources to save the situation by being part of the market. Some Spanish companies, for example, led the largest secondary share offerings in 2020 and being already listed has made a real difference to them compared to what would have been the case as an unlisted company. The depth shown by EU capital markets has been truly remarkable in this regard.

But beyond a greater number of companies in the markets and, above all, a greater role for the retail investor, how can the two interact in a context dominated by growing sources of information accessible to all? And equally, recalling the Gamestop case from a couple of months ago, can external factors, such as social media, for example, shape a different landscape in terms of market structure and the rules that govern it?

Social media is an everyday element through which investors connect and supervisors cannot and should not ignore this fact. They contribute to a better-informed community, as long as the information shared through them is not false or inside information. Social networks are also increasingly used by issuers and even regulators, so they should not be blamed for possible abusive practices that may be agreed through them. Moreover, without actual orders and executions, no conduct (unless it involves false or misleading information) amounts to market manipulation. It is only with the actual trading that possible manipulative behaviour arises. In other words: the Market Abuse Regulation (MAR) does not cover "thought infringement".

The role of influencers and opinion leaders through these media is already subject to the rules of market abuse. The investment recommendations regime, for example, applies to anyone who "holds themselves out to be an expert", although many of them may not know it. Supervisors may need to make a special effort to increase retail investors' awareness of the regulations, through financial education initiatives, so that retail investors become familiar with which types of transactions are permitted and which are prohibited. And we will probably have to do so using methods other than the traditional ones, as it is not through official communications and speeches that we can reach the new community of connected investors that is already emerging.

I shall conclude by expressing the hope that this conference will be interesting and profitable and that the evolution and trends in the world of investment and in the stock markets will allow us, with the efforts of all, to facilitate a solid and rapid recovery of our economy in the near future.

Thank you very much for your attention.