OPINIONS

COMMITTEE OF THE REGIONS

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Opinion of the European Committee of the Regions — Green Paper — Building a Capital Markets Union

(2015/C 313/05)

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References: Green Paper — Building a Capital Markets Union

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I. **GENERAL REMARKS**

THE EUROPEAN COMMITTEE OF THE REGIONS,

1. welcomes the initiative set out by the European Commission in the Green Paper — Building a Capital Markets Union, the key element of which is creating a single capital market;

2. points out that the private initiative and entrepreneurship play an important role in the process of creating a competitive European Union economy;

3. stresses the importance of creating a common, single capital market;

4. calls on the Commission to speed up its work on the action plan and put forward legislative proposals as soon as possible to achieve the objective of a fully integrated single EU capital market by the end of 2018;

5. welcomes the Commission's efforts to bring down barriers to investment in business, which will particularly benefit small and medium-sized enterprises (SMEs); underlines that unlocking the potential of the capital market is an important dimension of obtaining sustainable local and regional growth and jobs;

6. underlines the need to take further structural and anti-cyclical initiatives in the field of financial markets so as to impact all EU Member States and also benefit regions with less developed financial markets;

7. recognises the need to diversify sources of financing the EU economy and for mechanisms which bring in new investments as factors which bring stability and promote development;

8. is specifically interested in those elements within a capital markets union which could boost regional and local development;

9. expresses particular interest in and strongly supports all actions aimed at:

(a) strengthening the potential of SMEs, recognising their local role in promoting entrepreneurship, creating innovation and shaping society based on the value of work;

(b) financial feasibility support for important and long-term investment projects with key regional significance which create conditions for effective local and regional development;

10. points out that a capital markets union must enable more diverse sources of financing for investment projects which require many financial entities to be involved due to their specific characteristics and scope;

11. agrees that the creation of a capital markets union will require particularly extensive analyses and consultations to identify barriers and possibilities and then to undertake various regulatory, institutional and educational measures;

II. **PRINCIPLES AND GOALS OF THE CAPITAL MARKETS UNION**

12. welcomes the beginning of work on the process of creating a capital markets union;

13. believes that a single, regulated capital market within the European Union will be another tool to improve resilience against asymmetric shocks resulting from varying speeds of development of the European Union's individual regions. The Committee observes that deeply rooted factors of the lack of aggregate demand such as unevenness of regional development are also a source of weakness of capital markets;

14. welcomes the preparation of a set of priorities for further work covering such things as: lowering barriers to accessing the capital market, making it easier for capital holders and SME-type entities to enter into relationships, security on the capital market, support and financing for long-term investments, development of non-public issuance and other forms of financing throughout the EU and decreasing administrative burdens;

15. states that the capital markets union has the potential to integrate fragmented capital markets in Europe by supporting cross-border flows of capital which would consequently increase the scale of investment in European businesses and infrastructure projects;

16. calls upon the Commission to consider also the supply side, in particular to analyse and address the root causes of why retail and institutional investors are not able to mobilise and transform sufficient capital to strengthen individual financial services and long-term investment in the real economy;

17. fears that the current objectives are too general, which could lead to failure to achieve a satisfactory level of diversification of sources of financing for SMEs;

18. considers that the emerging capital markets union should above all contribute to the development of SMEs but questions whether securitisation offers a long-term solution to SMEs' financing problems, particularly in view of its proportionally higher cost for SMEs;

19. welcomes the change of course towards increasing the involvement of individual investors in the capital market but points out that the Green Paper does not pay enough attention to private investors;

20. considers that the adoption of broad capital market reform needs to be accompanied by strong EU-wide and national supervision, including by strengthening ESMA's role in improving supervisory convergence, in order to avoid excessive risk taking and instability in financial markets;

21. encourages carrying out more extensive consultations concerning securitisation processes, taking into account conclusions taken from the financial crisis. Securitisation must not give rise to systemic risk and should therefore avoid high-leverage instruments and dependence on short-term financing;

22. points out the significant cultural, historical and legal variation of individual markets of Member States. The complexity of the task requires more extensive ex ante analysis of the establishment and impact of a capital markets union in each Member State;

23. is convinced that many of the initiatives concerning the capital markets union will have to be implemented concurrently and then supported by multilevel education programmes due to social barriers resulting from factors such as traditions and customs;

24. points out the low level of financial knowledge and investment culture among retail investors and owners of micro-enterprises and small businesses. These are structural factors which hinder development of a Europe-wide capital market;

25. considers that local and regional authorities have a key role to play in developing the general public's financial education. The Committee also highlights the role played by associations and educational establishments in disseminating knowledge of economics and finance among young Europeans;

26. believes it is appropriate to consider financial and institutional participation of the public sector in areas that directly contribute to the development of the capital market where private sector initiatives will be insufficient. Before involving the public sector, it ought to be ascertained that public funding does actually generate private initiatives. In such cases, public sector involvement should be based on concomitant economic analysis and have a clear plan for divestment after the desired effect has been achieved, but also should things go awry;

27. believes that in areas covered by the capital markets union plan, many countries have good practices that are worth promoting;

28. emphasises that local and regional entities can play a significant and varied role in capital markets as investors offering long-term start-up capital and their liabilities could be traded on markets;

III. **HARMONISATION OF LAW**

29. agrees on the need to create a consistent set of rules on capital markets. These provisions should be respected in all Member States;

30. considers it appropriate to assume that creating transparent frameworks for the functioning of a single capital market and unifying the collateral system should increase credibility among investors, leading to more effective allocation of capital;

31. stresses that a consistent set of rules would be a major step towards eliminating barriers and creating the environment necessary for the establishment and operation of a single capital market throughout the European Union, which is more integrated with international markets;

32. points out that regulatory proposals connected to the capital markets union should not lead to excessive regulatory burdens on SMEs or limiting the benefits this sector could reap as a result of creating a single capital market;

33. considers it important to create new legal categories enabling investment and raising of capital within the European Union;

34. is convinced that new market initiatives can be introduced by further increasing public transparency of available financial information and eliminating reasons why financial information might not be comparable between Member States;

35. reiterates its call to increase comparability and availability of data on the risk of financing businesses from the SME sector throughout the EU, as expressed in previous Committee of the Regions opinions;

36. considers it appropriate to establish simplified International Financial Reporting Standards (IFRS), which could ensure comparability of businesses and increase their ratings. Using these kinds of standards could also encourage investors to invest funds in businesses that apply transparent and generally acknowledged principles;

37. sees a need for systematic work on harmonising insolvency law and to reconcile financial restructuring process frameworks, and acknowledges how complicated this matter is, particularly the various ways in which social groups and certain groups of creditors are privileged;

38. supports the review of legislative frameworks including prudential rules with the aim of investigating barriers to securitisation of assets invested in the SME sector and which hinder the functioning of non-bank entities offering financing and less restrictive treatment of long-term involvement in infrastructure projects;

39. points out the potential problem of lack of harmonisation of financial markets because certain Member States are not part of the banking union;

40. emphasises that the capital markets union must be open and competitive internationally and attract international investment by maintaining high standards in the EU through such things as ensuring the integrity of the market and financial stability of investors;

IV. **DIVERSIFICATION OF SOURCES OF FINANCING FOR SMES**

41. would like to highlight the significance of the SME sector for the European economy and regional development. There were over 20 million SMEs in the EU-27, making up approximately 67 % of jobs and 58 % of gross value added. Furthermore, there were almost 19 million SMEs employing up to 10 people, which provided 1/5 of the jobs in the EU. During the crisis in 2008-2011, SMEs were better able to stabilise employment than large companies, but at the same time their share in GDP creation underwent a relative decrease ([1]);

42. points out that it is more difficult for SMEs to access diversified sources to finance their activities. Over 80 % of external financing sources for SMEs in the EU are bank loans and 40 % of companies make use of leasing, usually offered by entities associated with banks;

43. notes that SMEs have more problems accessing bank loans in periods of economic downturn, so intrabank processes are more pro-cyclical than anti-cyclical;

44. notes that increased competition for the banking sector is a necessary step towards decreasing its domination in providing sources of financing in the EU, particularly for the SME sector. There should be strong support for eliminating the barriers that limit this competition on the part of non-banking entities and financial instruments, new players and innovation from outside the financial sector, as well as for legislative initiatives in this area;

45. believes that the objective of the capital markets union is not to reduce the importance of banks in the European economy. The Committee considers it essential to maintain an appropriate balance between actions promoting investment banking and non-bank financing, on the one hand, and financing in the form of traditional bank loans, on the other;

46. welcomes the actions Member States have taken so far, such as financial support programmes for SMEs (guarantees, grants, accelerating commercial payments, seed capital);

47. points out key factors enabling SMEs to develop, such as a business-friendly environment, modern infrastructure, the existence of technologically advanced sectors of the economy and a highly qualified workforce. In light of the above, capital markets union initiatives should be prepared in such a way as to lower the transaction costs of raising capital and to reach the micro-enterprises group, which is both the largest and the one with the weakest links to capital markets; points out the need to minimise the administrative burden involved in the regulation;

([1]) *Annual report on European SMEs 2012/2013*, European Commission, October 2013.

48. is concerned that new EU banking sector regulations (CRD IV/CRR) could also limit SMEs' access to bank financing and therefore recommends cyclical studies of the impact of the abovementioned regulations on changes to SMEs' access to bank financing in individual countries;

49. stresses that regional and local banks have an important role to play in financing SMEs because they have better knowledge of the local and regional economies and unique methods of assessing credit risk of local businesses;

V. **STIMULATING COMPETITION ON THE CAPITAL MARKET**

50. hopes that the single capital market can contribute to the development and spread of alternatives to traditional forms of credit and investment intermediation. These forms have important potential to provide investment capital to local economic operators;

51. encourages the European Commission to promote good practices in alternative forms of financing which are well developed in some EU Member States;

52. considers it desirable, within discussions and work on the capital markets union, to ensure an environment, in particular a level of regulation and oversight, that is conducive to the development of the parallel banking system and crowdfunding. They are still relatively small in scale but have a significant growth rate [2];

53. acknowledges that alternative offers of financing directed at SMEs, particularly high investment risk instruments, work out better in the case of innovative ventures;

54. takes the view that the regulatory environment should be stimulating and not limit the accessibility of new instruments and forms of capital distribution;

VI. **FINAL REMARKS**

55. welcomes the EC's increased interest in the problem of access to non-bank financing;

56. acknowledges that the Green Paper — Building a Capital Markets Union is only the first step to creating a single capital market;

57. is willing to take part in further work, acknowledging that a diverse regional and local perspective makes it possible to create provisions which take the needs of all parties into account;

58. encourages discussion on a detailed work programme which should ensure the appropriate momentum needed to keep to the planned deadline for creating a single capital market;

59. stresses the need to integrate different environments with the aim of drafting an entirely satisfactory document which takes into account needs which vary by area and sector;

60. points out the need to step up programmes to improve knowledge of financial issues and educate the public on investment possibilities and needs. National initiatives and Europe-wide projects such as Consumer Classroom need to be amended and supported;

61. encourages further public debate on the Green Paper — Building a Capital Markets Union and the accompanying review of the directive on the prospectus and securitisation.

Brussels, 8 July 2015.

The President
of the European Committee of the Regions

Markku MARKKULA

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[2] *The European Alternative Finance Benchmarking Report*, Cambridge University, February 2015.