

Febelfin position on the Capital Markets Union

Febelfin, the Belgian Financial Sector Federation, represents the majority of the Belgian financial sector, including banks, credit providers, asset and fund managers, market infrastructures, stockbroking firms and stockbrokers, leasing companies, etc. Our broad representation basis delivers a comprehensive and balanced position that considers the unique characteristics of various branches within the financial industry.

Introduction

The Capital Markets Union (CMU) is an economic policy initiative launched by the former president of the European Commission, Jean-Claude Juncker to create a single market for capital. The aim is to get money – investments and savings – flowing across the EU so that it can benefit consumers, investors and companies, regardless of where they are located. While progress has been made since the CMU initiative was launched in 2015, and updated in September 2020, EU capital markets to this date remain fragmented.

Febelfin welcomes the renewed ambition to achieving the CMU as an essential instrument to help financing the multiple transitions the EU is going through. In this paper, the Belgian Financial industry shares its vision on how to achieve stronger European capital markets for the benefit of citizens, companies and Member States alike. The political momentum that we see today – reflected in recent reports and statements - should be leveraged to the greatest possible extent. The main target for Febelfin and its members is clear; to increase the size and depth of EU capital markets to effectively achieve a Savings and Investment Union. The end goals of the CMU should be to effectively provide economic growth, to provide for stable pensions for European citizens, to ensure competitiveness throughout Europe and to invest more funds in the green transition.

To achieve this, **Febelfin supports the idea of expanding the European investor base**. To effectively strengthen the participation of EU investors, we must work on quick and easy pathways to capital markets, ensure a stable regulatory framework, establish clear and effective information sources and improve the common perception of investing.

Next to that, Febelfin advocates– without pushing for blind deregulation – for a **profound reform of national frameworks across Member States to overcome fragmentation**. Febelfin outlines several objectives that policymakers can work towards. Additionally, **reviving the European securitisation market** is essential to breathe new life into our capital markets.

Current dynamics of EU capital markets

The common challenges we face require plenty of capital. To give an impression of the predicted demand; just to meet sustainability goals, finance the digital transition and effectively implement defense strategies in the EU, it is estimated that Europe will need approximately €1 trillion additional investments yearly¹. Those resources should be provided by the banking sector as well as by investors through capital markets.

The CMU project promises great benefits for the EU: providing more diversified sources of financing for companies (in particular for SME's, start-ups and scale-ups), new investment opportunities for citizens, strengthening the EU's global financial position, creating a more homogeneous environment enhancing competition and even a new barrier to systemic shocks. There's a win in it for every EU Member State as countries with small markets and large growth potential would more easily gain access to capital. More established markets would profit from additional investment opportunities and stronger economies in the Union.

But if the benefits are so clear, one could ask the question which factors may have hampered the effective integration of EU capital markets? The answer, we believe, lies in the complex nature of the CMU and the fact that there are no "silver bullets". Achieving a true CMU is not solely about regulating the financial industry, it requires deep reform in the Member States' national frameworks and, not to be forgotten, a competitive environment in the EU. If the EU lacks competitiveness, and therefore return, investors will continue channelling their available funds to better performing economies. In our view, we furthermore lack a common cause that pools the efforts to be made and that Member States can rally behind. We believe a shared sense of ownership is required to expand the European investor base and to overcome fragmentation. Also, the European securitisation market is to be revived to offer more oxygen to our capital markets.

The call for a CMU can certainly not be confused with a call for blind deregulation. Financial markets can expand naturally and safely if the right circumstances are created. Especially because today's framework for risk management has progressed since the 2008 Global Financial Crisis. Financial institutions have successfully internalised risks, created the required capital buffers and, to address future challenges, there are now more powerful supervisory mechanisms.

Febelfin acknowledges that the effects of several recent EU legislative initiatives² have not yet crystallized. We should derive the benefits of these initiatives in the next couple of years, and if necessary, make targeted adjustments. At the same time, EU institutions should focus on the due implementation of existing rules and regulation, instead of developing new legislative initiatives, and furthering supervisory convergence.

¹ As mentioned in the "Noyer Report" <https://www.tresor.economie.gouv.fr/Articles/e3283a8f-69de-46c2-9b8a-4b8836394798/files/6b8593b5-ca31-45a3-b61c-11c95cf0fc4b>

² Amongst others: ESAP, ELTIF, Listing Act, MiFIR II.

Expanding the European investor base

To increase the size and liquidity of EU capital markets, high-performing market infrastructures are necessary, but so is a pool of investors. Today, we lack - directly and indirectly - retail investor participation. In this context, Febelfin emphasizes that the ultimate beneficiaries of most, if not all, investments are households. Often, institutional investors (e.g., pension funds) pool resources from various households, ultimately serving their interests. The benefits of investing for households are plentiful, especially when started at an early age, with a long-term investment horizon. European issuers will equally benefit if their customers become investors, creating additional liquidity and generating brand awareness. Having more people engage in capital markets is also important because of the positive network externalities that exist on capital markets and specifically stock exchanges. When more people use it, its benefit increases³.

For Febelfin, more retail investor participation can be achieved through four key changes. The first focus should be to improve access to capital markets for investors. Easy and quick pathways towards investments, based on a seamless customer experience and correct advice, can be a way to give people a first experience in investing and get them familiar with capital markets. To achieve this goal, several ideas around an EU long-term investment product circulate. We recommend building a “savings product category” or “EU-label” to which existing products can comply. This would allow market participants to leverage the value of the diverse offer that exists today. The focus should be on diverting capital to long-term saving plans through tax-efficient saving schemes – including capital gains, income, and inheritance tax exemptions – to promote investment in European companies and a diversification of assets to balance risk with their time horizon.

A second element to enable more long-term investment is to ensure a stable regulatory framework that gives investors long-term certainty. The best way to stimulate EU citizens to invest with a long-term horizon, is to not change the rules of the game every couple of years.

Our third recommendation is to establish clear and effective information sources for all investors, including retail investors. For an investor looking to invest in assets that are issued in a different country, one of the major challenges is collecting adequate and reliable information about the investment itself, and about the legal, regulatory, operational and fiscal frameworks for the investment. In the EU this challenge is multiplied by the reality of 27 member states, each having its own frameworks. The European Single Access Point (ESAP) and the Consolidated Tape will be significant steps in dealing with the challenge of data, but they will not be sufficient. ESAP is limited in scope, and does not provide the full range of core capital market data that is necessary for making an investment. The provision of data by ESAP should be expanded, so that ESAP acts as the golden

³ Di Noia, C. (2001). Competition and Integration among Stock Exchanges in Europe: Network Effects, Implicit Mergers and Remote Access.

source of public information for, for example, corporate action events on a security. The EDGAR system⁴ in the US should serve as an example.

Our last recommendation is to ameliorate the common perception of investing. We lack a genuine investor culture. While investing comes with inherent risks and responsibilities, this is generally very positive as the potential benefits are often commensurate and outweigh the opportunity risk of not investing. We thus strive for a considered approach to risk-taking, both in the rhetoric of policymakers and in regulation. EU legislation on retail investors often aims to guide investors toward less-complex and/or less-risky products. Our goal is to achieve a balanced alignment between consumers' risk tolerance and their investment objectives. A second element to boost our investor culture should be to promote more strongly the notion of ownership in investing. By becoming an investor in a company/ fund, people have the power to effectively guide their money towards purposes that align with their personal values. We fully support efforts to raise awareness that investors hold the possibility to influence the economy toward achieving ESG goals. This is especially crucial as more individuals begin investing, recognizing their collective ability to drive meaningful change.

Overcoming fragmentation

EU capital markets should become more attractive to issuers and investors. They are difficult and complex to access, and too small. A major challenge for European capital market policy is to overcome fragmentation, and to create a true European single market for capital. In our view, this fragmentation largely stems from the frictions caused by the different national legal, regulatory, supervisory and fiscal frameworks. These should be overcome through a single rulebook to establish a fully harmonised framework of rules and regulations, and through supervisory convergence, to ensure effective enforcement.

Febelfin acknowledges that not all aspects of fragmentation can be resolved easily but we urge policymakers to (i) work towards intermediary objectives and (ii) strive for harmonisation in every legislative step.

The intermediary objectives should include, amongst others, an overhaul of the Shareholders Rights Directives to ensure that shareholder rights can be executed in a simple and straightforward manner, both domestically and cross border; streamlining tax processes and reporting requirements; harmonising the tax treatment of IPO fees⁵; and further harmonise and simplify listing rules.

⁴ In the US, the SEC launched the Electronic Data Gathering, Analysis, and Retrieval (EDGAR) system. EDGAR automates the collection, validation, indexing, acceptance, and forwarding of submissions of data from regulated entities who are legally required to disclose this information. It provides a federal-level access point to users, offering information that is often machine-readable and freely available online on an itemized basis.

⁵ For example, a tax incentive similar to Italy's "Bonus IPO" tax credit, which helps SMEs cover IPO-related costs.

To achieve further harmonisation through the legislative process, we propose strengthening the Better Regulation Guidelines by doing the following: The Commission should propose regulations rather than directives. Henceforth Member States would thus no longer be able to introduce all types of gold-plating when transposing directives. We also recommend that EU legislators refrain from allowing national discrepancies in Regulations, for example through opt-in or opt-out regimes. Lastly, Febelfin recommends strengthening the role of competitiveness assessments and extending it to every part of the legislative process instead of limiting it to the initial phase of the process. This can be achieved by developing a robust methodology and identifying dedicated responsible parties in each institution to monitor competitiveness assessments.

Another critical requirement is the need for further convergence with respect to post trade solutions. The EU needs to prioritize cross-border investments as a key objective and facilitate financial market infrastructures in their (voluntary) consolidation efforts. Challenging areas that require regulatory harmonization should finally be addressed, notably insolvency laws and remaining required adjustments to the post-trading regime.

In this context, the topic of single supervision has been prevalent in the ongoing discussions surrounding the CMU. In our opinion, while fragmented supervision may prove sub-optimal, it is not a core driver for fragmentation in the CMU. Supervisory convergence is important as fragmentation stemming from diversity of local interpretations of regulations and market practices is detrimental to primary market development. Let us start by developing a common framework that facilitates a single interpretation and application for supervisors (e.g., definitions, procedures, documentation). Febelfin recommends mandating supervisors to consider the overall “competitiveness” of the market on the same level as protecting investors’ interest, market transparency and financial stability (similar to what has been done in the UK).

Reviving the EU securitisation market

The potential for securitisation in the EU is materially underutilized. Between 2007 and 2022, total annual issuance volumes of securitised assets in Europe fell 61% to €157 billion from €407 billion (even when we exclude the share of the US market covered by public guarantee schemes, this is only 12% of US issuance); And, in 2023, European Issuance amounted to 0.3% of European GDP, compared with 2.6% in Australia, 1.4% in Japan and 0.7% in the UK⁶. Securitisation became a controversial concept following the global financial crisis, but we need to emphasize that securitisation is a very useful and, if set up properly, responsible source of financing of the real economy, not only used by banks, but also by large companies directly.

Contrary to claims that securitisation may lead to higher risk-taking or lower lending standards by banks, research shows otherwise. Studies published by the ECB and the BIS found that banks using

⁶ Noyer (2024), Développer les Marchés de Capitaux européens pour Financer l’Avenir.
<https://www.tresor.economie.gouv.fr/Articles/e3283a8f-69de-46c2-9b8a-4b8836394798/files/6b8593b5-ca31-45a3-b61c-11c95cf0fc4b>

securitisation did not lower their lending standards more than other institutions during the pre-crisis period⁷, and that securitised loans to Italian SMEs had better quality compared to non-securitised loans, indicating a positive selection effect⁸.

The market is now highly regulated; this results on the one hand in a high degree of transparency, but on the other hand also in securitisation becoming unviable for many market actors. Securitisation is often looked at from the perspective of banks, but in reality, European companies and households could also reap the benefits from securitisation. It provides more possibilities for those searching for finance, whether it is a company wanting to grow its business or a family renovating its' home.

To underpin the importance of securitisation for SME's and the green transition we refer to the European Investment Fund's working paper on SME finance (2022)⁹ which mentions the following; *“Given that SMEs have only limited direct access to capital markets, a well-functioning securitisation market can provide an indirect access by transforming illiquid loans to SMEs into an asset class with adequate market liquidity.”* The EIF also highlights the importance of securitisation for the green transition explaining that it has significant potential to support the green transition but concludes that to be able to do this “the overall development of the EU securitisation market is crucial for the growth of the sustainable segment”.

In the EU, corporates today rely heavily on bank financing to invest and grow. Even with strong capital markets, this will likely remain. Banks stand close to their clients and go over each loan application with diligence, experience, and ample information. Given this context, Febelfin too is convinced that securitisation can play a decisive role in enhancing the overall financing capacity of the system towards the ability of the EU to sustain the course of economic transformation and growth.

To activate securitisation in the EU, Febelfin recommends first to recalibrate the prudential treatment of securitised assets. Specifically, the capital charges and risk weight floors on senior tranches should be reviewed in line with their low risk profile. Next to that, we propose to upgrade eligibility of senior STS tranches as HQLA in the LCR ratio of banks, and to improve Solvency II capital treatment to re-incentivize EU insurers to invest in securitisations. Finally, to reduce barriers to entry on the market, it is necessary to streamline ESMA disclosure templates and adapt due diligence requirements.

Political stakeholders need to reconsider their perception on securitisation in a pragmatic and unbiased way. An evidence-based discussion is needed to overcome the difficulties securitisation faces. The renewed focus on the CMU offers an ideal opportunity to leverage securitisation as a

⁷ Kara, et al. (2015). Securitization lending standards: evidence from the European wholesale loan market. <https://www.ecb.europa.eu/pub/pdf/scpwps/ecbwp1362.pdf>

⁸ Albertazzi et al. (2017). Asymmetric information and the securitization of SME loans. <https://www.bis.org/publ/work601.pdf>

⁹ H. Kraemer-Eis et al. The European Small Business Finance Outlook 2022. https://www.eif.org/news_centre/publications/eif_working_paper_2022_84.pdf



crucial financial tool. By enhancing capital allocation efficiency and boosting financing capabilities, securitisation can play a pivotal role in strengthening the EU economy.

Conclusion

Febelfin urges Belgian and EU policymakers and national competent authorities to be ambitious and realistic in the coming years by taking decisive actions to expand the investor base, reduce market fragmentation, and revive the securitisation market.

Febelfin is committed to continuing the dialogue on these crucial topics and is prepared to offer targeted feedback to support these efforts.