Christian Staub

Europe Managing Director,
Fidelity International

Resilience, purpose and the Capital Markets Union

Financial crises often bring with them a reassessment of social purpose. Following the 2008 crisis, Adair Turner, chairman of the UK Financial Services Authority at the time, described some aspects of the credit derivative market as "socially useless." In the 11 years since those comments were made, concerns over the social utility of finance have moved from fringe products to the mainstream core of equity itself.

Greater attention is being paid to the role of equity in our system of financial capitalism, to how it can be more effectively harnessed to support the real economy and to how to address the balance between shareholder and stakeholder value.

The goal of policy will be to address these issues in a practical way. And, at Fidelity International, we firmly believe the European Union's Capital Markets Union (CMU), and the recommendations from the High-Level Forum (HLF), present a real opportunity to bring together the common interests of finance and society for the purpose of reinvigorating Europe's economy. Here's how.

Finding purpose in the CMU

Household financial resilience plays a central role in the framework. The job of a socially embedded capital market is to disperse household savings to the real economy for its use and profitable return, and the CMU reminds us of this in the very structure of its design – with households in need of investment opportunity at one end of a chain and industry in need of funding at the other.

From this flows an ambition to stimulate retail participation in the EU's economic growth, seeking to transform salary-earners into asset-owners. There is an implicit need for greater financial education for this to happen successfully, so that citizens understand how to map their own particular set of liabilities on to the assets available to them.

An increased investor base needs a broader and deeper pool of corporate issuances to pick from, and so the CMU and the HLF's support for greater SME participation in capital markets, either via the channels of Solvency II, Basel III or ELTIF, is a necessary central pillar.

SMEs are one of the main engines of economic growth at a national level and improving their access to funding will fuel job creation and greater investment. To encourage these companies to issue equity for the first time, they should have some relief from market abuse regulations aimed at larger institutions.

And so, a solid plan to encourage greater participation in equity markets would not only boost the financial resilience of households, but of companies too. In rebalancing the funding mix away from debt and towards equity, SMEs will become less vulnerable to sudden credit and liquidity crunches.

The need for resilience

If the interests of society and firms are to be more closely bound by equity, then corporate resilience becomes an end in itself. Non-resilient companies bring fragility both to their employees and investors, as well as to the economic system as a whole. -

There are elements of the CMU that will enable asset managers to guide corporates towards more resilient business models through capital allocation or stewardship. And the HLF's proposals around shareholding are a step in the right direction, as well as proposals to re-invigorate SME research and the EFAP.

However, there is room to widen the scope. In creating a new system of capital, as much as possible must be done to mitigate the systemic risks capable of puncturing it. We return once again to 2008, the response to which provided a policy blueprint for models of financial resilience.

Here, policymakers could make good use of bank and insurer recovery and resolution planning legislation, leaving capital adequacy rules aside but seeking to embed the same culture of resilience into non-financial firms. Here, policies from stress-testing to annual reporting may be applicable.

The CMU initiative clarifies the social purpose of equity, supported by the two pillars of increased retail participation in equity markets, and more dispersed corporate issuance. However, fragile companies risk breaking the virtuous circle of value creation and increased economic activity, as well as the trust of wary retail investors, requiring policymakers to consider a third pillar: that of corporate resilience. ●