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A way forward for EU capital markets – the auditors' view

As the Union's independent external auditor, the European Court of Auditors (ECA), not only assesses implementation of the EU budget, but also the performance of EU institutions and bodies in reaching their objectives. Among others, we evaluate actions of the European Commission, the European Supervisory Authorities, the European Central Bank as a banking supervisor and the Single Resolution Board. The ECA has been publishing reports on the EU's financial and economic governance since 2014. One of our recent reports deals with the Commission's work on the development of EU capital markets and building the Capital Markets Union (CMU).

In this report, titled "CMU – Slow start towards an ambitious goal", we concluded that the Commission has indeed pursued a number of legislative initiatives and other measures to implement its 2015 CMU action plan, yet no catalytic effect was observed. Many of the measures that the Commission was able to take within its remit only addressed narrow areas in the pursuit of the CMU objectives. So far, they did not lead to the highly anticipated structural shift from bank to more market funding for businesses in general, and SMEs in particular.

We observed that large discrepancies between Member States persist in the size of the SMEs' financing gap and the availability of funding sources. Access to capital markets remains expensive and burdensome, especially for SMEs. The so-called 'debt-equity bias' is a disincentive for the development and integration of capital markets. Other issues, such as a lack of harmonized insolvency proceedings and the general diversity of company law across the EU, are well known. The Commission's new 2020 action plan strives to address many of the issues identified. Certain actions, such as simplification of listing rules for public markets, can contribute to more market funding and private risk sharing, if implemented well. A simplified system of providing relief from withholding tax, as recommended by the ECA, could also bring significant improvements. However, without political dedication in building a truly European capital market and further measures to tackle key cross-border barriers, it will be difficult to deliver added value for EU businesses and investors. Hence, support and joint decisions by Member States is required, which so far have proved to be problematic.

Fostering efficient local capital markets will be key for building a

genuine CMU. Indeed, capital markets in Europe remain highly concentrated and strikingly heterogeneous among Member States. Thus, the first step would be to render local capital markets deeper, more liquid and better aligned with regional counterparts. This will require willingness, comprehension, substantive efforts and delivering real structural reforms.

To tackle the needs of Member States, in particular with less developed capital markets, action at both, national and EU-level, is required. We recommend to establish a comprehensive EU-wide strategy bringing together all relevant public sector actors, such as EU and Member State authorities as well as promotional banks, in order to identify and address the needs of local and regional capital markets and businesses seeking market financing. We recommend that the Commission use more actively all available tools, such as technical support and country-specific recommendations, to incentivise and help build financial ecosystems across Europe, not relying solely on national initiatives or demand. The coordinated creation recently of the legal framework for covered bonds simultaneously in three Baltic States is one example.

Another necessary action to address key cross-border barriers to investment is the reinforcement of financial literacy specifically among SMEs, primarily start-ups that are looking for ways to fund their not always "bankable" ideas. Although this mainly falls under the remit of Member States, the Commission can still play a critical supporting role via existing European programmes and by promoting best practices.

The ECA will continue to report on the EU's progress towards a single market for capital. We have recently started an audit to assess whether EU actions helped to develop an effective single market for investment funds to benefit consumers and businesses, while ensuring financial stability.