EU capital markets fragmentation

1. Current level of fragmentation

An industry speaker stated that fragmentation in EU capital markets should be assessed through both an institutional and retail perspective and also at the trading and post-trading levels. For institutional equity trading, the European landscape is relatively efficient when compared with the US: fewer lit and dark order books, fewer internalising brokers. Trading securities across the whole EU requires using additional lit books of domestic exchanges but that does not increase complexity significantly due to the fact that many of them operate on common technology. In terms of institutional post-trade, the direction of progress is positive also. There is a solid level of interoperability at the clearing level for equities with 75% of the equities market benefiting from full CCP interoperability, and a further 20% has partial interoperability, with only 5% lacking such functionality. The objective should be to achieve full interoperability. The CSD space is also improving with the investor CSD model[1] within T2S and CSDR. Much work remains to be done, but significant investments are being made by the larger CSD groups.

Retail markets are more problematic in terms of fragmentation, the industry speaker stressed. National markets are not connected to the same extent, and they vary significantly in terms of trading model, with different levels of on-exchange trading and internalisation and internalisation taking different forms across jurisdictions. This patchwork limits market efficiency and retail investor access.

A second industry speaker considered that EU capital markets are disproportionately fragmented. At the post-trading level, outstanding issues from the Giovannini barriers, including diverging national securities laws, insolvency regimes and withholding tax processes need addressing. Although three CSDs handle 95% of volume, the existence of 28 CSDs in Europe maintains inefficiencies.

On trading, the industry speaker challenged the previous speaker's optimistic view by highlighting that there are over 500 trading and execution venues across asset classes in Europe. This level of fragmentation has remained largely unchanged over the last two decades, despite efforts to unify the capital markets framework, and it is further exacerbated by an uneven regulatory landscape between lit and dark trading segments. The main issue is not the level playing field between entities, since exchanges now operate MTFs and offer a variety of trading mechanisms beyond their central limit order books, including RFQs, auctions and iceberg orders. Rather, the issue lies in the disparities between the rules governing the different market segments. For example, the rules applicable to cash equity exchanges, such as volume caps and reference price waivers, are not directly comparable to the rules governing systematic internalisers. This undermines the capacity of exchanges to drive greater market efficiency through the consolidation of trading activity across venues.

The industry speaker also suggested that the original objectives that underpinned the first iterations of MiFID and other capital market regulations need to be revisited with a stronger focus on strengthening the overall competitiveness of the EU capital market and increasing its capacity to attract innovative companies to list in the EU.

A third industry speaker noted that although three CSDs handle the bulk of settlement operations in the EU, the persistence of a large number of national CSDs imposes unnecessary costs on investors. The speaker also highlighted key differences between the EU and US capital market landscapes. While both jurisdictions host a large number of trading venues, the US benefits from a single consolidated tape per asset class, as well as a single infrastructure provider for clearing and settlement services. Moreover, in the US, securities are traded across all venues, whereas in the EU there is limited competition between domestic venues, both for listings and for secondary trading. Some pan-European MTFs compete in the secondary market, but national exchanges generally do not. Although there has been some consolidation and technical integration at the exchange level in the EU, order books, pools of liquidity, and market data pricing remain fragmented. As a result, market participants are yet to fully benefit from this integration.

A fourth industry speaker further illustrated the fragmentation of retail markets. The retail capital market environment is focused more at present on protecting investors than on fostering investment, leading to a fragmented market, as customer protection measures tend to be implemented differently at national level. Moreover, when tax incentives exist e.g. for investment accounts, there are often constraints to invest all or part of the portfolio in the home country and these products are not portable, creating home bias.

An official highlighted the persistent fragmentation of EU capital market supervision. While the single rulebook has been strengthened, national differences in interpretation and supervision undermine uniformity. Supervisory convergence efforts coordinated by ESMA, through colleges, peer reviews and common guidelines, have helped to make progress, but there is still a need to interact with multiple national authorities.

1. The investor CSD model allows a central securities depository (CSD) in one EU country to offer settlement services for securities issued in another country, facilitating cross-border settlement within the T2S platform and supporting CSDR objectives for market integration.

2. Impact of fragmentation

The chair noted that the fragmentation of EU capital markets is a persistent issue that limits the benefits from the single market. The latest SIU Strategy communication quotes IMF figures evaluating internal market barriers as imposing a de facto tariff exceeding 100%, which represents a huge cost to the European economy. One of the main objectives of the Savings and Investments Union (SIU) initiative is to reduce fragmentation in the EU capital markets.

An industry speaker emphasised that market fragmentation issues are also highly relevant to consider in light of evolving geopolitical dynamics. Recent volatility and the US threats to significantly increase tariffs underscore the urgency of deeper integration within the EU and completing the SIU to ensure the funding of the EU economy.

An official stated that although progress has been made under previous Capital Markets Union (CMU) action plans, fragmentation continues to impose high costs and inefficiencies. Investing in the EU is more expensive and complex than in other regions due to the requirement for investors to use multiple intermediaries to access the market and navigate various tax, legal, and reporting systems. The need to interact with multiple supervisory authorities also increases the compliance burden and administrative costs for financial institutions, reducing opportunities to build scale, for example in the asset management sector. This raises costs and reduces returns for retail investors. Fragmentation also increases financial stability risks due to the absence of consolidated supervisory views on cross-border institutions.

An industry speaker noted that the fragmentation of the retail market reduces returns for retail investors. This, combined with a lack of financial education and excessive risk aversion, means that the majority of savings are channelled into low-yielding vehicles, such as bank deposits and savings accounts. This creates an equity financing gap for corporates — especially young, innovative firms — that cannot be financed by bank loans.

The industry speaker also highlighted the impact of fragmentation on corporates. The net cost of IPOs in Europe is nearly double that in the US, and the complex, fragmented regulatory landscape makes delisting and the execution of squeeze-outs of minority shareholders more difficult. The lack of harmonisation in takeover regimes also contributes to legal arbitrage, which undermines investor protection and transparency. A more consistent framework would facilitate cross-border transactions and reduce uncertainty for international investors.

An official agreed that fragmentation is a fact in Europe and has significant impact, notably in terms of fees. However, this impact varies by country. In many CEE region countries, for example, local SMEs, the backbone of the economy and drivers of innovation, rely primarily on domestic or regional financing. While the broader benefits of capital market integration at the EU level are acknowledged, it is unclear whether a more unified trading or post-trading system would be relevant for the region's SMEs. National markets continue to play a critical role, especially in catering to the needs of smaller enterprises, and there is still room for them to grow.

3. Measures to further integrate EU capital markets

3.1 Trading integration

An industry speaker stated that there are opportunities for further integration in the trading space, as part of a comprehensive response to fragmentation that must address transparency, post-trading infrastructure, and trading venues. Deeper integration across these different areas would foster more attractive, resilient and liquid markets creating greater opportunities to optimize capital formation and allocation. The ongoing implementation of consolidated tapes for equities and bonds in the EU is a critical step forward in particular to enhance transparency and deliver better quality information to investors, though the latter tape still requires improved data timeliness.

Another industry speaker suggested that a greater harmonization of trading rules for given market segments is needed, notably regarding the transparency and waiver regimes, to level the playing field and reduce the current complexity. Only by aligning rules across all execution venues can a complete liquidity picture be achieved, supporting investor trust and market depth.

3.2 Post-trading integration

An industry speaker stated that further rationalising and consolidating post-trade remains essential, as redundant infrastructure creates inefficiencies and higher costs for investors and issuers. This requires greater interoperability of infrastructures with open access rules. To capture scale efficiencies what is needed is an optimisation of the post-trade infrastructure for each asset class, rather than a full consolidation, as the optimal model may be different for each asset class. This consolidation should be market-driven. What needs to be done from a policy perspective is to remove the explicit and implicit barriers that prevent further market integration and consolidation.

An official noted that consolidation must be distinguished from defragmentation. Consolidation is a market-driven process when it makes economic sense, whereas defragmentation is a policy objective focusing on eliminating obstacles that hinder integration and creating the conditions for further consolidation to be possible.

An industry speaker was in favour of maintaining healthy competition in the European CCP and CSD spaces, rather than aiming for a high degree of consolidation, as competition fosters innovation. Integration can be enhanced through interoperability, lifting post-trading legal barriers and developing participation in T2S. Member states have an important role to play in this regard. All of them should participate in T2S, which is not the case at present, and T2S usage should also be incentivised with fee rebates.

The 28th regime could also potentially be used on a voluntary basis to overcome legal fragmentation, the industry speaker suggested, bypassing entrenched national obstacles in tax, insolvency and securities law. Starting at the issuer level, such a regime could gradually gain traction, but it should remain optional.

An official observed that despite being fragmented, the EU's post-trade system performed in a reliable way, even during stress periods. Further integration is however necessary. Harmonising security, tax and insolvency laws remains key, though this is a long-term endeavour. In the interim, market-driven integration should be pursued, building on the T2S platform and increasing the number of participants on the platform.

Another official suggested that the transition to T+1 settlement could potentially lead to greater efficiency and innovation in the post-trading market and to the development of competitive post-trading services in a more effective way in the short term than a further centralisation of the market infrastructure.

An industry speaker agreed that T+1 settlement can be an important driver of efficiency in the post-trade area. The decision to transition to T+1 settlement by 2027, aligning EU and UK timelines, is a positive step.

3.3 Role of technology

An official stated that technology can also play a key role in fostering integration in the post-trading market, particularly in the context of the implementation of a wholesale central bank digital currency (CBDC) at the Eurosystem level. A trial phase involving 60 participants was completed at the end of 2024 to test solutions for settling tokenised asset transactions. Three bridging solutions between tokenised assets and TARGET Services were tested, along with a tokenised central bank money solution.

The next step is to develop a viable solution for settling DLT-based transactions. The Eurosystem will follow a two-step roadmap, with further details expected by June. The goal is to unlock the potential of tokenised asset markets in Europe and enhance post-trade competitiveness. The first step aims to consolidate the best features of the three bridge solutions into a single interoperability layer linking DLT platforms with existing TARGET Services, enabling safe and efficient settlement in central bank money. The longer-term objective is to implement direct central bank money settlement on DLT platforms.

3.4 Further unification of supervision

An official emphasised that cross-border supervision is an area where targeted reform could be beneficial and that deserves further assessment. The benefits of supervisory convergence are already widely acknowledged, and many stakeholders, including the European Council, the ECB, ESMA, and the European Commission, have recognised the need for more unified supervision of certain capital market activities, although this is not viewed as a silver bullet. The objective is not to introduce radical changes, but to consider further centralising supervision where it is justified, particularly for large cross-border or systemic entities, such as major market infrastructures, pan-European asset managers, or large cryptoasset service providers.

Moving towards more centralised supervision would not imply transferring all supervisory authority to the current ESMA structure overnight. New mandates, additional resources, and probably also a revised governance model would be required. While supervisory standards and common doctrines should be defined at the EU level, ESMA's governance must be adapted to enable decision-making on systemic institutions on a case-by-case basis. An AMLA-style executive board could potentially be introduced to handle such cases. In parallel, interactions between the EU and national supervisory authorities must be appropriately structured. Establishing joint supervisory teams combining ESMA and national authorities, similar to the approach taken in the SSM and AMLA, appears to be the most effective way to foster cooperation.

4. Measures to increase retail investment

4.1 Enhancing financial literacy and long-term investment product offering

An industry speaker stressed the importance of directing Europe's vast pool of retail savings, currently held mainly in bank and savings accounts, towards more productive investments. A longer-term investment horizon is also needed. One proposed solution is to enhance the interoperability of existing private pension products, allowing them to be more easily transferred across borders within the EU and thereby improving portability. This approach appears more pragmatic than attempting to impose a single European pension product, such as the PEPP, on all Member States. More broadly, reforms are needed to expand funded pensions in Europe. Currently, 62% of the continent's funded pension assets are concentrated in just three countries, while demographic trends are deteriorating. With the dependency ratio worsening, fewer working-age citizens are supporting a growing number of retirees. Creating sustainable, funded pension schemes is becoming increasingly urgent to ensure adequate retirement savings. Financial education is another structural challenge to address. A recent OECD study found that just over half of respondents could correctly answer basic financial literacy questions. This knowledge gap hampers the development of a long-term investment culture.

An official noted that developing retail participation is a long-term effort that may span several generations, given the widespread risk aversion and limited financial literacy among many European investors. The Czech

Republic has implemented a national financial education strategy. While the effects have been positive, challenges remain. Younger investors often show a preference for crypto assets over traditional securities, reflecting evolving attitudes toward investment. A flexible long-term investment product label, covering a range of instruments such as shares, bonds, and investment funds, and supported by tax incentives, has also been introduced, with encouraging uptake so far.

Another official observed that certain Eurosystem central banks, such as the Bundesbank, have long engaged in financial education initiatives, including with programmes to integrate the subject into school curricula. However, progress has been slow due to competing educational priorities. For financial education to advance meaningfully, it must become a political priority.

An industry speaker agreed that increasing financial literacy to mobilise retail savings into more productive investments is necessary, but it is a long-term endeavour, as it depends on broader cultural and educational shifts. Ease of access to adequate financial products is also an important factor. Tax-incentivised accounts for long-term retirement savings can play a critical role in encouraging retail participation.

4.2 Adapting trading models to retail specificities

An industry speaker stressed that, in addition to financial literacy and access to suitable products, retail investors must have confidence that they are treated fairly when participating in securities markets. Achieving this requires the development of trading systems—both on and off exchange—that are designed to serve the needs of retail investors in an effective way. Given that retail orders are typically smaller and not strategically timed, retail investors are less likely to possess insider information or move market prices. This makes their trades less risky for liquidity providers, allowing for more competitive pricing. Trading models should recognise these characteristics and ensure that retail investors benefit from fair, transparent and efficient market outcomes.

A second industry speaker suggested that the EU should eventually build a harmonised model for retail trading execution centred around public markets. The EU should not replicate the US market with OTC and public markets running in parallel, where OTC trading surpassed on-exchange volumes for the first time in 2024, with 52% of volumes. Although pricing may be fair at present, excessive reliance on OTC trading risks weakening price discovery. Obligations should also be introduced for intermediaries to interact with public prices for retail flows, while maintaining a level regulatory playing field between exchanges and alternative venues. Such a model would enhance transparency and liquidity, making the market more diverse, competitive and attractive and would benefit retail investors as well all market stakeholders – market infrastructures, liquidity providers and banks - allowing them to focus on their core activities.

The first speaker cautioned against misinterpreting US data on off-exchange trading. While it is often cited that over 50% of trades happen off-exchange, that figure refers to trading volumes. When measured by the value of trades, the proportion is closer to 40%, and much of it is in fact driven by institutional, not retail, activity.

5. Wrap up

The chair summarised that there was a broad consensus within the panel that EU capital markets remain insufficiently integrated. Long-standing issues, such as legal and fiscal barriers, as well as the need to strengthen pensions and improve tax process harmonisation, must be addressed. Addressing these challenges requires decisive action from all stakeholders: EU authorities must provide a consistent regulatory framework and market standards, Member States must complete necessary reforms at the domestic level to eliminate legal barriers, and industry must support innovation and engage in closer cooperation. The objective in terms of policy is not to force consolidation, but to remove the obstacles to further market consolidation and integration and foster interoperability across market infrastructures. With the current momentum surrounding the SIU initiative, the EU must also look ahead, embracing technological change and anticipating geopolitical shifts in order to build capital markets fit for the future and able to support the European economy.