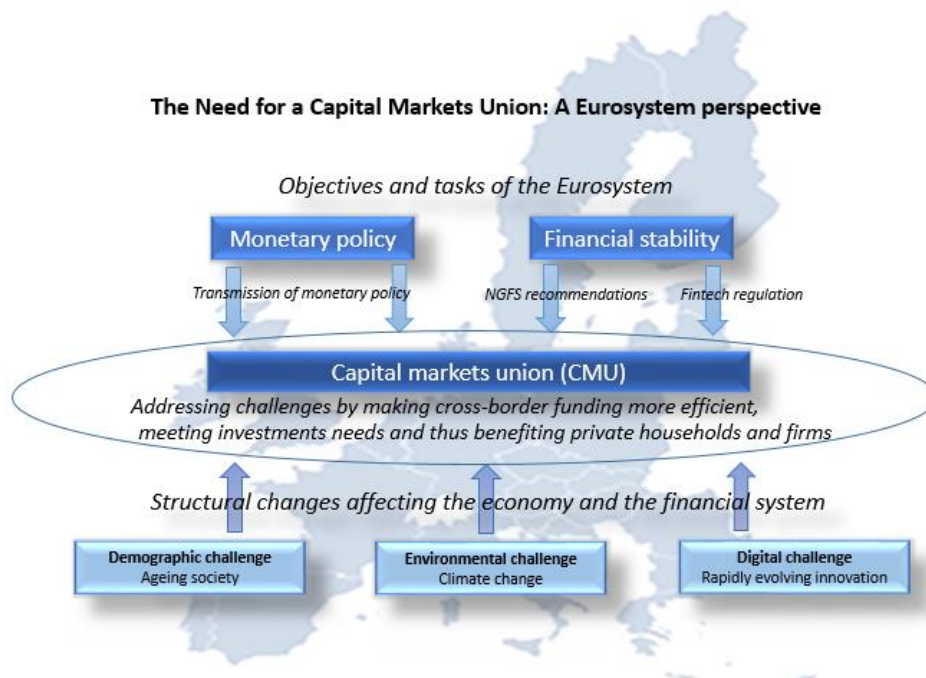


**STIMULATING GROWTH AND INNOVATION THROUGH INCREASED FINANCING OPPORTUNITIES
FOR BUSINESS AND INVESTORS
A CONTRIBUTION TO THE CAPITAL MARKETS UNION**

There is an urgency to stimulate growth and innovation through improved European financing opportunities, bringing benefits to households and firms. The CMU action plan of September 2015 and its June 2017 mid-term review set out a comprehensive agenda. In October 2019, the report of the Next CMU High-level Group, provided input on how to proceed with the CMU project¹. On 10 October 2019 the European Commission launched a call for expressions of interest for a High-Level Forum on CMU that is supposed to propose targeted policy recommendations for future CMU actions to ensure that citizens and businesses can access capital markets across the EU on equal terms, irrespective of their geographical locations.

Central banks have long been supporters of such initiatives on capital markets, which closely relate to their objectives and tasks along several dimensions (see diagram below):

- First, the smooth **transmission of monetary policy** is promoted by well-functioning and deeply integrated financial markets. In that respect, the CMU complements the banking union by broadening the sources of funding for European corporates;
- Second, deeper capital markets integration may contribute to the **preservation of financial stability** by strengthening private-sector risk-sharing, in particular through well diversified sources of financing, allowing for better resilience to shocks;
- Third, a CMU that significantly reduces frictions within and across territories may help European countries to master the massive structural changes affecting the functioning of the European economy, such as **climate change², population ageing and technological change**.



¹ To signal the new orientation of the project, we support the Next CMU High-level group proposal to rename it the “Savings and Sustainable Investment Union”.

² Central banks are involved in the climate change agenda via the Network for Greening the Financial System (NGFS).

While many of the outgoing Commission's proposals have been adopted, much remains to be done to reach truly integrated markets for the purpose of investment and innovation.

Against the backdrop of the Aachen Treaty of 22 January 2019 - which promotes Franco-German harmonisation of business law -, the release of the proposals of the Next CMU report and the appointment of a new European Commission, this paper compiles a set of complementary options to address priorities with respect to CMU from a central banking perspective.

Keeping in mind that a successful CMU should operate for the benefit of all participants, households, firms and in particular SMEs, while ensuring stability, the options are presented as follows:

I. Benefits to households

Households have a major interest in borrowing or investing their financial resources soundly and efficiently within Europe. This requires ensuring that frictions and costs within Europe are minimised. They are also beneficiaries of investments (e.g. in infrastructures) conducted in Europe to support the ongoing structural transformations, such as energy transition, digital transformation, and demographic change.

Of direct interest to EU citizens is the availability of adequate savings instruments and vehicles. This is particularly important in the area of pension savings. While the proposal by the Commission requires concrete implementing measures, the adoption of pan-European pension products is a first step to generate more long-term savings.

Other pan-European savings and investment products could be developed, such as green finance instruments, including via digital distribution channels. Additionally, in terms of wholesale financial instruments, we took note of the Energy Efficient Mortgage Initiative (EEMI), an attempt by the industry to design a standard for green pan-European mortgages taking into account energy efficiency building (see annex 1).

To ensure that a large number of citizens seize the opportunity to diversify their savings they need to understand the risks and trust the effectiveness of market supervision. Generating more long-term savings requires increased financial literacy of the public, and adequate consumer protection.

II. Benefits to firms

The euro area crisis highlighted the dependence of European firms on bank lending and the relative scarcity of alternative financing channels. When the banking system ran into trouble, credit became scarce in many countries, impairing investment activity and thus growth. In addition to making the banking system safer with the Banking union, complementary sources of financing for non-financial corporates could be further developed, including market instruments and venture capital. Equity financing should in particular enable innovative SMEs to grow.

More can be done in terms of data transparency to improve potential investors' access to information about SMEs, especially if these are located in another European country. Eventually, such efforts could also attract investors from outside of the EU to European SMEs. To this aim, the Bundesbank and Banque de France are working on data management and support mainstreaming the use of the Legal entity identifier (LEI) (see annexes 2 and 3). A European approach to data transparency should avoid the multiplication of regulation layers and guarantee the quality and the accessibility of harmonised data. In order to further develop equity markets, data transparency on SMEs' data should be increased, to accelerate and set a calendar for the implementation of a European Electronic Access Point and extend it to companies listed on SMEs Growth Markets. As a result, information on companies would be improved, reporting integrated, and the costs to access information reduced, for the benefit of SMEs seeking financing.

European banks could benefit from the development of a consistent and integrated system for collecting statistical, resolution and prudential data. This is currently assessed by the EBA Feasibility study on integrated reporting which will take into account the work that the ESCB has already carried out regarding the integration of data collections (Integrated Reporting Framework (IReF), Banks' Integrated Reporting Dictionary (BIRD)).

III. Financial stability and environmental challenges

An efficient and effective supervision is a necessary condition for the soundness of capital markets in the EU. Strengthening the European supervision of financial markets can help: (i) to mitigate systemic risks; (ii) to safely accommodate financial innovation; and (iii) to attract cross-border investments in Europe, with a single regulatory point of entry³. Strengthening European supervision can take place in several ways:

- convergence of supervisory practices is already part of the mandate of ESMA; coordination between supervisors can be improved in some areas and it could be explored whether there is a need to strengthen ESMA's supervisory role for specific products or entities;
- development of a consistent and integrated system for collecting statistical, resolution and prudential data. EBA and ESCB should align their initiatives in order to develop a common European reporting framework.

Progress is also needed to promote pan-European banking to increase financial flow fluidity between EU financial market places. This requires striking a delicate balance between national responsibilities for financial stability and the objective to further integrating European financial markets. To this end, we need to explore avenues to (i) reduce to the extent possible regulatory obstacles to cross-border activities; (ii) balance financial stability concerns and frictionless activities of pan-European financial firms. In addition to home/host issues, pan-European retail banking is also hampered by fragmented Anti-Money-Laundering (AML) regulation and supervision.

Furthermore, insolvency and taxation regimes have financial stability implications and are important for investment and funding decisions. The scope for improving efficiency, effectiveness and transparency of insolvency regimes should be explored as well.

The newly created High-Level Forum on capital markets union, the report of the Next CMU High-level Group, central banks and Supervisors involved in the Network for Greening the Financial System (NGFS) and in the Task Force for Climate-related Financial Disclosures (TCFD) of the Financial Stability Board (FSB) point to initiatives to enhance sustainable long-term projects (see annex 1).

³ See annex 4 for rules at the EU level for Fintech.

EUROPEAN INITIATIVES FOR IMPROVING ACCESS TO CAPITAL MARKETS ACROSS THE EU

- a. Next CMU High-level Group:
<https://www.nextcmu.eu/publications/>
 - b. High-level Forum on capital markets union:
https://ec.europa.eu/info/publications/cmu-high-level-forum_en
 - c. Capital Requirements Regulation (CRR II) Integrated Reporting Framework
Feasibility report on the integrated reporting system (Article 430c)
<https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32019R0876&from=BG>
 - d. The ESCB's long-term approach to banks' data reporting (IReF, BIRD)
https://www.ecb.europa.eu/stats/ecb_statistics/cooperation_and_standards/reporting/html/index.en.html
 - e. European Banking Federation
<https://www.ebf.eu/ebf-media-centre/data-reporting-european-banks-underline-need-for-an-integrated-and-standardized-eu-framework/>
 - f. LEI:
CMFB opinion on business identifiers and business registers:
Recommendations for statistical production, 2 December 2016
<https://circabc.europa.eu/sd/a/98871143-34f9-46a4-a642-a68e3461aeb8/2016-12-02%20-%20CMFB%20opinion%20on%20business%20identifiers%20and%20business%20registers%20-%20recommendations%20for%20statistical%20production.pdf>
- Globally:
FSB Peer review examines implementation of the LEI to support authorities and market participants in identifying and managing financial risks, 28 May 2019 <https://www.fsb.org/wp-content/uploads/P280519-2.pdf>

Annex 1:

Supporting sustainable finance

Financing needs for a transition to a low-carbon economy are massive. As an example, it is estimated that an additional EUR 177 billion per year will be necessary over the period 2021-2030 to reach the EU's energy and climate objectives for 2030. This amount is a challenge, but it also creates opportunities for companies and investors. In that context, the Capital Markets Union can play a pivotal role in allocating investments and savings where they are needed to achieve the energy transition and the EU's climate objectives.

Equity financing is an efficient way of funding businesses in the early stage of the innovation cycle. It is therefore a powerful means to foster technological breakthroughs to encourage the transition.

To make a significant contribution to the transition, the Capital Markets Union needs a robust framework for environmental- and climate-related disclosures. At this stage, the work done by the Task Force on Climate-related Financial Disclosures (TCFD) presents a widely recognized framework for climate-related disclosures. In its first comprehensive report, published in April 2019, the members of the **central banks and Supervisors Network for Greening the Financial System (NGFS)** pledge their collective support to the TCFD recommendations. However, there is a need to transform this framework into standards and to enlarge its scope (from climate to environmental disclosure in a broader sense). Such a framework needs to be robust and internationally consistent, aligning expectations regarding the type of information to be disclosed and allowing for the sharing of good practices. Once sufficiently harmonized and stabilized, due consideration should be given to make those requirements mandatory.

Furthermore, these disclosures need to be built on sound taxonomies. The NGFS therefore recommends that policy-makers support the development of taxonomies of economic activities. The taxonomy published on 18 June by the Technical Expert Group (TEG) on Sustainable Finance of the European Commission and the agreement reached by the Council end of September regarding the proposal for a *taxonomy* are decisive steps. The TEG's taxonomy presents a list of 67 economic activities contributing substantially to climate mitigation objectives without doing significant harm to one of the five other environmental objectives. The trilogue negotiations between the European co-legislators started end of October. The progress made on the European level towards a green taxonomy is certainly an important step forward, but there is also a need to develop a brown taxonomy in order to better measure the exposure to climate-related risks.

More generally, the deliverables of the TEG on (i) taxonomy, (ii) a European Green Bond Standard (EU GBS), (iii) benchmarks, and (iv) disclosure are part of the European Commission's action plan on sustainable finance. The TEG's proposals could help to enhance green finance on the European level by creating a standardized approach. For instance, the EU GBS proposed by the TEG should ultimately help to further develop the green bond market and facilitate more investments in green projects. Such initiative would help green finance to mature and upgrade its standards and should aim to ensure an efficient allocation of financial flows towards green projects in the context of the CMU.

Putting into action the two recommendations made by the NGFS on disclosure and taxonomy, could also contribute to making progress on another recommendation made by the NGFS: bridging the data gaps. In order to do so, there is a need to adapt the national accounting standards. Indeed, as of today the national accounting standards are not sectorial and do not allow to efficiently reflect exposure to climate-related risks. However, the TCFD recommendations might build a common understanding on which national accounting standards can be adapted.

The new European commission led by Ms von der Leyen has also pledged for an ambitious “European Green Deal” that will hopefully help Europe to become a low-carbon economy. It will be important to enhance the development of projects contributing to the energy transition and to encourage private investments by helping to turn financing needs into bankable and marketable projects.

Furthermore, the official sector impetus for enhanced transparency might act as a catalyst for more initiatives from the private sector. As an example, we took note of the **Energy Efficient Mortgage Initiative (EEMI)**, launched in September 2016 by the European Covered Bond Council (ECBC).

Annex 2:

Supporting the implementation of the Anacredit feedback loop

A feedback loop enables reporting credit institutions to get feedback on the global loans exposures of non-financial companies, among which SMEs, from the ANACREDIT loan-by-loan, entity-by-entity Eurosystem database. For example, when a bank enters into a discussion with an SME to grant a loan, the access to selected information of ANACREDIT via the “feedback loop” would enable the bank to know the overall amount of loans already granted by the other banks reporting to ANACREDIT, as well as some key characteristics of these loans.

The implementation of a feedback loop is foreseen by the ANACREDIT Regulation (*Regulation EU of the European Central Bank of 18th May 2016 on the collection of granular credit and credit risk data – recital 18 and art. 11*). However, this regulation opens the way to NCBs to set up this feedback, but is not sufficient to enable them to do so: legal national frameworks have to allow for it, which is not the case in many EU countries. The ECB is not entitled to establish a European legal basis, which would be the best solution.

1. Key factors of success for the implementation of feedback loops

- Progress in the quality of data at individual borrower level (which ultimately is in the hands of the reporting entities and partially of NCBs where restrictions apply in the use of official registers, such as DE);
- On-time implementation and regular enlargement of IT infrastructure, at ECB level and National level;
- The establishment of an EU legal framework or second best national legal frameworks allowing the exchange of “third-party-data” to banks, where not yet available;
- A large number – if not all – NCBs should commit to the feedback loop framework;
- As many NCBs as possible should strive to exchange in the feedback loop on the basis of the “maximum list”, i.e. all data considered fit for purpose.

2. How to commit to a fruitful feedback loop

These factors are to a large extent out of direct control of Banque de France and Deutsche Bundesbank. However, we can commit to a fruitful feedback loop by:

- An efficient cooperation with the reporting entities and own IT development to achieve rapid progress in quality;

- A bilateral exchange of experience in the setting up of DQM-related work and underlying IT algorithms with a view to jointly fostering data quality
- Joint work to conceptually prepare a feedback loop framework and reflect on the best way forward.

Annex 3:

Reducing the costs and improving the safety of raising capital by broadening the coverage of the Legal Entity Identifier

A. Setting a good example at the national level

A.1. Using the LEI as the national identifier

Within the framework for the reduction of statistical obligation, the German authorities are currently examining the implementation of a basis register of German enterprises for administrative purposes. In this regard, it will be investigated to use the LEI as identifier. Promoting the LEI would allow benefiting from a unique identifier not only nationally but also worldwide.

France, which already has a unique national identifier, could foster the reduction of GLEIF fees to a not noticeable level and then to investigate ways for the registration authority to also issue the LEI, for better connecting French entities in banking and international processes, such as payments and anti-money laundering.

A.2. Promoting nationally good practice using LEI in the context of supervision and data transparency

For instance, it could be required from GSIBs and main financial groups the registration and yearly renewal of all their subsidiaries and foreign branches with a full reporting of their relationships (parents, head office). The LEI could also be required for main counterparts. Finally, the LEI could support tools to cryptographically sign regulatory reporting.

Registration authority, statistical authorities, prudential authority could also be convinced to provide the LEI along with the national code when they publish the lists and databases under their responsibility.

B. Promoting the LEI in European regulation

Regarding prudential regulation, the LEI could be promoted to identify banks' counterparts in regulation discussed under the aegis of EBA and thus addressed to the European legislator.

Regarding the regulation on company law (digital tools and processes, business statistics), it could be ensured that the LEI is mentioned as a desirable alternative optional ID, side by side with the EUID and VAT number, in the implementing acts.

Regarding regulation on information accompanying transfers of funds for the purpose of fighting money laundering and terrorist financing, the LEI could be included in future versions of the European regulation, especially for international wire transfer messages.

C. Supporting the extension of LEI use through FSB standards

Based on the proposals of the FSB peer review on LEI, which have been published on 28 May 2019, this would help increasing the use of the LEI in the financial domain. FSB initiatives that could be supported are:

- The use of the LEI for the resolution of financial institutions and in financial innovation issues.
- The use of LEI for all group entities and major counterparties of global systemically important financial institutions, as well as clearing members of central counterparties (CCPs) and their ultimate parents.
- The effective implementation of the LEI option in payment messages.

Annex 4:

Developing rules at the EU level for Fintech

1. Crypto tokens

A uniform European regime for crypto tokens regulation⁴ would be best for achieving the objectives of the capital markets union (ESMA has spoken out against national regimes, inter alia) or a bridging solution should be implemented via transitional national regulation.

European rules would give ICO issuers the opportunity to raise funds across the EU, thereby promoting cross-border financing and enabling enterprises and innovative projects to tap into a further alternative source of funds.

2. Electronic securities

European rules for debt securities and equities would be conducive to achieving the aims of the capital markets union. From a financial stability perspective, there is also potential to harness the following advantages:

- At present, securities are held in what are sometimes very long and opaque custody chains, with up to five sub-custodians. This can theoretically increase the risk that financial distress at a major sub-custodian can give rise to liquidity problems (of systemic proportions) for market participants.
- Generally speaking, the introduction of electronic securities, possibly in conjunction with the issuance of the security on a blockchain, has the potential to shorten these custody chains and thereby mitigate the aforementioned risks. However, it will be necessary to weigh the capabilities of a new technology against the risks associated with using it.

⁴ The German Federal Ministry of Finance and the German Federal Ministry of Justice and Consumer Protection recently published a “key issues paper”, proposing that Germany plays an active role in the European legislative process in order to achieve a European regime for crypto tokens regulation.