Towards a genuine capital markets union

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Virtually everything about Brexit is surrounded by uncertainty, but one thing has become clear – how costly it is going to be to leave the single market. Our common market is an out-and-out success. It has raised economic output, increased the choice of goods and services, and at the same time lowered prices for consumers. But we can make it work better. With respect to capital markets, we still forego the benefits of further integration. While geographical diversification is already quite high in some market segments, cross-border activities in other areas remain weak and have been stagnant in recent years.

By tearing down the remaining barriers to free capital flows and investment we can strengthen financial integration, leverage our common market and reap a double dividend of higher growth and stronger resilience. This will ultimately benefit EU citizens. In order to strengthen our Economic and Monetary Union and avoid overburdening monetary policy, there are many reform proposals like the extension of the banking union or fiscal mechanisms being discussed at governmental level. But there is no reform so broadly agreed on as the capital markets union. Yet despite some recent achievements, progress on the agenda is proving difficult and slow. It is now high time to move forward and complete the capital markets union.

A genuine capital markets union would not only help to better channel the abundant savings – which exceeded investment in the euro area by €340 billion in 2018 – towards concrete investment needs such as energy transition, digital innovation or SME growth: it would also facilitate macroeconomic adjustment within our Economic and Monetary Union. Integrated capital markets can cushion shocks that hit parts of a currency area. When company ownership is highly diversified geographically, business profits and losses are widely distributed as well. In the United States, for example, capital markets allow almost half of the burden of an economic shock to be spread across the states – more than by fiscal transfers. In the euro area, only one-tenth of an economic shock is cushioned by private risk sharing.

Equity financing is particularly conducive to risk sharing, as profits and losses are shared in like manner. Furthermore, equity financing is better suited to the high level of uncertainty and the delayed profitability that innovative projects are often associated with. Ample supply of external equity was one of the drivers of the increase in research and development in the United States during the 1990s. Venture capital, in particular, seems to facilitate innovation. This market remains underdeveloped in the EU. In relation to the size of the economy, the US venture capital market is more than five times as large as the European one. Remaining obstacles to the development of the venture capital market should thus be removed. The adoption of the European Venture Capital Fund Regulation (EuVECA) has been a useful step forward. Harmonisation of rules may help to increase cross-border investment. The Aachen Treaty of January 2019 envisages the establishment of a Franco-German economic zone with common rules, notably in business law. This could serve as a laboratory for European efforts, also regarding more cooperation and further convergence in insolvency matters.

A good example of how a capital markets union would complement the single market is pensions. Labour mobility is hindered as long as employees cannot take their pension product with them when they want to work in another member state. The new pan-European pension product is portable across member states and offers consumers a wider range of investment opportunities.

Integrated capital markets require effective supervision. As a starting point, the European Securities and Markets Authority (ESMA) should contribute to further convergence of supervisory practices, in accordance with its mandate, notwithstanding the open debate on future integration steps. The recent agreement on the framework for the European System of Financial Supervision will also contribute to more harmonisation.

The capital markets union can promote growth and stability for the EU as a whole. Together with the banking union, the capital markets union would establish a genuine "Financing Union for investment and innovation". Such a Financing Union would be a decisive and feasible step to complete our Economic and Monetary Union.