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Audit preview

Information on an upcoming audit

Building an effective Capital Markets Union

October 2019

In 2015, as part of the Investment Plan for Europe, the Commission started work on the Capital Markets Union (CMU), a major EU initiative to lay the building blocks of an integrated capital market in the EU by 2019.

The CMU is expected to give individual and corporate investors access to a wider variety of investment opportunities. It should also benefit businesses in search of funding, expanding the options available to them and reducing their exposure to the vulnerabilities of the banking system. By complementing banks and spreading financial risks across the EU as a whole, the establishment of the CMU should result in a more stable financial system that is better equipped to boost growth and create employment.

The European Court of Auditors has recently launched an audit of the effectiveness of the Commission’s action so far to build the CMU.

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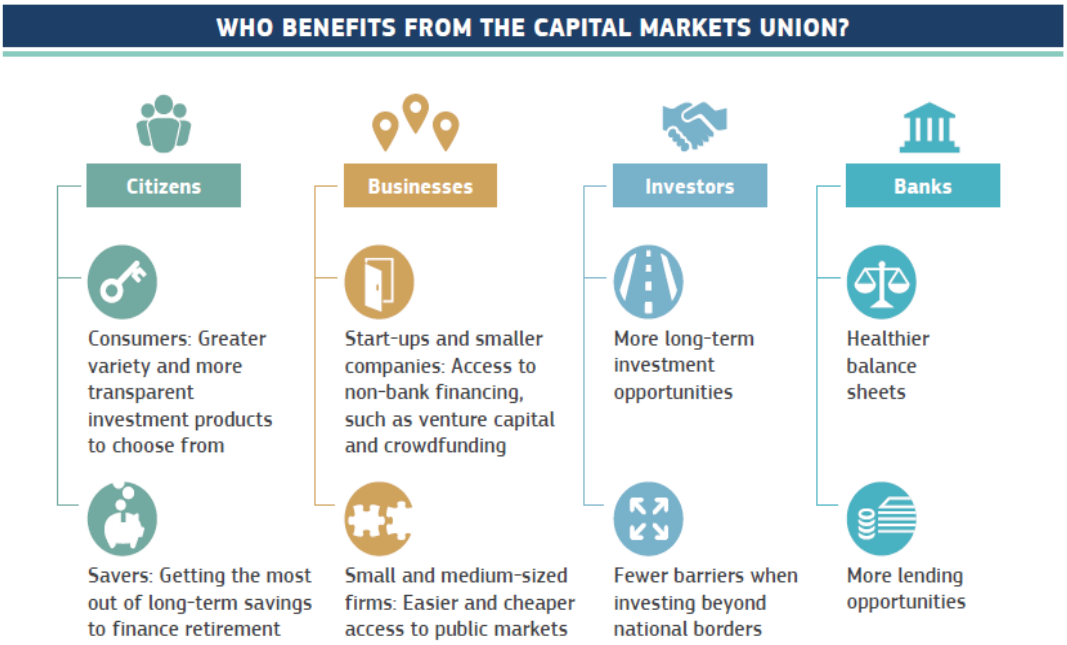
Background

What is the CMU?

The "four freedoms" – the free movement across borders of people, goods, services and capital – are at the heart of the European single market. The free movement of capital is therefore a key long-standing objective of the European Union. Despite some progress over the years, Europe's capital markets are still heavily fragmented along national lines, with the result that they are not readily accessible to all would-be investors. Since the banking system continues to provide the bulk of funding to the EU's economies[1], these are highly vulnerable when difficult times – such as the 2008 financial crisis – compel banks to tighten their lending conditions.

The Capital Markets Union (CMU) was launched in June 2015 as a major EU initiative (part of the "Juncker Plan"[2]) to lay the building blocks of an integrated capital market in the EU by 2019. The CMU action plan included more than 30 legislative and non-legislative measures. By complementing banks as a more diversified source of financing, deeper and more integrated capital markets in Europe should offer investors and savers additional opportunities to put their money to work and open up new sources of funding for all EU businesses, in particular start-ups and smaller companies (see ***Figure 1***). The result should be a more stable financial system that is better equipped to boost growth and create employment.

Figure 1 – Who benefits from the CMU?



Source: European Commission.

The CMU is part of the broader long-term single market policy across the EU as a whole; while financial stability is a precondition for its success, it does not address the specific rules and arrangements for stability but relies on leveraging and reforming the current regulatory and institutional architecture.

State of play

Progress made so far on the CMU

At a time when banks have been struggling to provide funding to businesses and overall levels of bank lending have fallen sharply, Europe's capital markets have grown steadily since the CMU was first announced in November 2014. At the same time, the total market capitalisation of EU-listed companies now exceeds pre-crisis levels, which signals the increased potential of the sector to take on much of the burden of financing the EU's economies. However, the EU in general, and more particularly the euro area, is still lagging behind internationally in terms of capital markets as a share of GDP.

In the EU, the central and eastern European countries have the greatest potential for capital market growth[3] – but there is also substantial room for development in larger economies such as Germany, Italy and Spain (see ***Figure 2***).

Figure 2 – Depth of capital markets across EU countries

The ranking of the overall depth of capital markets by country and by sector, divided into four groups: from the most-developed (top quartile) to the least-developed countries (bottom quartile).

	Rank	Country	Overall depth	Pools of capital	Equity markets	Bond markets	Asset management	Private equity & VC
Top quartile	1	Luxembourg	Top	Top	Second	Top	Top	Top
	2	UK	Top	Top	Top	Top	Top	Top
	3	Netherlands	Top	Top	Top	Top	Top	Top
	4	Sweden	Top	Top	Top	Top	Top	Top
	5	Denmark	Top	Top	Top	Second	Top	Top
	6	Ireland	Top	Second	Second	Top	Top	Second
	7	France	Top	Second	Top	Top	Top	Top
Second quartile	8	Belgium	Second	Top	Second	Top	Second	Second
	9	Finland	Second	Top	Top	Second	Second	Top
	10	Spain	Second	Second	Top	Second	Third	Second
	11	Malta	Second	Second	Second	Third	Second	Second
	12	Italy	Second	Second	Second	Second	Second	Third
	13	Germany	Second	Second	Second	Second	Second	Second
	14	Portugal	Second	Third	Third	Second	Third	Third
Third quartile	15	Austria	Third	Second	Second	Second	Second	Third
	16	Cyprus	Third	Third	Bottom	Bottom	Third	Second
	17	Czech Republic	Third	Third	Third	Third	Bottom	Bottom
	18	Poland	Third	Bottom	Third	Third	Third	Third
	19	Greece	Third	Bottom	Third	Third	Bottom	Bottom
	20	Croatia	Third	Third	Third	Third	Third	Bottom
	21	Hungary	Third	Third	Third	Bottom	Bottom	Third
Bottom quartile	22	Estonia	Bottom	Bottom	Bottom	Third	Second	Third
	23	Latvia	Bottom	Bottom	Third	Bottom	Bottom	Second
	24	Bulgaria	Bottom	Bottom	Bottom	Third	Bottom	Bottom
	25	Slovakia	Bottom	Third	Bottom	Bottom	Third	Bottom
	26	Slovenia	Bottom	Third	Bottom	Bottom	Bottom	Bottom
	27	Romania	Bottom	Bottom	Bottom	Bottom	Bottom	Bottom
	28	Lithuania	Bottom	Bottom	Bottom	Bottom	Third	Third

Top quartile · Second quartile · Third quartile · Bottom quartile   11

Source: P. Asimakopoulos and W. Wright, *Unlocking the growth potential in European capital markets: Analysis of the size, depth and growth potential of capital markets in the EU,* New Financial, June 2019.

Reviewing and refining the CMU

In June 2017, the Commission published a mid-term review of the CMU process in which it re-emphasised the considerable potential of a Union of capital markets to spread investment risks and reduce the impact of any asymmetric shocks. At the same time, it raised a number of new questions about financial integration. The Commission followed up the mid-term review by updating and adding to the CMU action plan to take account of the possible UK withdrawal and further challenges like sustainable finance and Fintech. It also introduced the concept of sustainable/green finance as an integral part of the CMU, and aligned the CMU more closely with the need for action to remove the remaining barriers to the Banking Union.

During 2018 and the first half of 2019, the Commission made progress towards new legislation in the area of the CMU (see ***Figure 3***). A new strategy for the CMU is among the top priorities listed for the Commissioner responsible for financial services[4].

Figure 3 – Overview of CMU legislative measures

	Measure	Deadline	COM	EP	Council	Adoption
1	**EuVECA/EuSEF review**	Q3 2016	July 2016			Oct. 2017 (OJ publication)
2	**Prospectus Regulation (review)**	Q4 2015	Nov. 2015			June 2017 (OJ publication)
3	**STS securitisation Regulation**	Q3 2015	Sep. 2015			Dec. 2017 (OJ publication)
4	**Pan-European Personal Pension Product (PEPP)**	Q2 2017	Adopted on 29. 6.2017	Negotiating mandate obtained in September 2018	Negotiating mandate obtained in June 2018	Political agreement reached in Dec. 2018
5	**European Supervisory Authorities review, including AML rules**	Q3 2017	Adopted on 20.9.2017	Negotiating mandate obtained in December 2018	Negotiating mandate obtained in Feb. 2019	Political agreement reached in March 2019
6	**Investment firms review**	Q2 2018	Adopted on 20.12.2017	Negotiating mandate obtained in September 2018	Negotiating mandate obtained in Jan. 2019	Political agreement reached in February 2019
7	**Crowdfunding**	Q4 2017 (IA) Q1 2018	Adopted on 8.3.2018	Negotiating mandate obtained in November 2018	Negotiating mandate obtained in June 2019	Trilogues expected to start end October 2019
8	**Covered bonds**	Q1 2018	Adopted on 12.3.2018	Negotiating mandate obtained in November 2018	Negotiating mandate obtained in Nov. 2018	Political agreement reached in February 2019

	Measure	Deadline	COM	EP	Council	Adoption
9	**Cross-border distribution of investment funds**	Q1 2018 (IA) Q2 2018	Adopted on 12. 3.2018	Negotiating mandate obtained in December 2018	Negotiating mandate obtained in June 2018	Political agreement reached in February 2019
10	**Rules to give SMEs easier access to growth markets**	Q2 2018 (IA) Q3 2018	Adopted on 24.5.2018	Negotiation mandate obtained in December 2018	General Approach agreed end Feb. 2019	Political agreement reached in March 2019
11	**European market infrastructure regulation (Supervision)**	Q2 2017 (COM(2017) 225 final)	Adopted on 13.6.2017	Negotiating mandate obtained in May 2018	Negotiating mandate obtained in Dec. 2018	Political agreement reached in March 2019
12	**Preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures (DG JUST)**	Q4 2016	Adopted on 22.11.2016	Negotiating mandate obtained in September 2018	Negotiating mandate obtained in Oct. 2018	Political agreement reached in February 2019
13	**Law applicable to third party effects of transactions in claims (DG JUST)**	Q4 2017	Adopted on 12.3.2018	Negotiating mandate obtained in February 2019	Not agreed yet	Not started

Source: European Commission.

Roles and responsibilities

European Commission

A Commission department, the Directorate-General for Financial Stability, Financial Services and CMU (DG FISMA), was set up in 2014 to, among other things, develop and promote the CMU action plan. It has overall responsibility for the plan's implementation.

Other Commission DGs collaborating on the project are the Directorate-General for Economic and Financial Affairs (DG ECFIN), the Directorate-General for Internal Market, Industry, Entrepreneurship and SMEs (DG GROW), the Directorate-General for Justice and Consumers (DG JUST), the Directorate-General for Taxation and Customs Union (DG TAXUD), and the Directorate-General for Research and Innovation (DG RTD).

The Structural Reform Support Service (SRSS) is a Commission service department whose main responsibility in respect of the CMU is to provide technical assistance to reinforce the capacity of Member States' domestic capital markets.

The European Securities and Markets Authority (ESMA), an independent EU body fully accountable to the Parliament, the Council and the Commission, also collaborates on the CMU.

Member States and the European Parliament

Under the subsidiarity principle, certain key policy areas for the CMU (e.g. taxation and judicial systems) are the responsibility of individual Member States. Moreover, all 13 legislative measures, proposed by the Commission, are adopted by the European Parliament and the Council via the co-decision procedure. The success of the CMU initiative depends, therefore, on not only the Commission but also the political will and ambition of the European Parliament and the Member States.

Financing

There is no specific spending programme for the CMU, and DG FISMA's outgoings are limited to staff and other administrative costs, including those incurred for expert and advisory bodies, meetings and studies. The Commission's technical assistance, which includes projects relating to the development of local capital markets, has an overall budget for 2017-2020 of €222.8 million. Other EU mechanisms and programmes share the business support objectives of the CMU action plan. These include the European Semester[5], the Programme for the Competitiveness of Enterprises and SMEs (COSME), the Horizon 2020 research and innovation programme, the European Structural and Investment Funds (ESIF) and the European Fund for Strategic Investments (EFSI).

Focus of the audit

Although the direct impact of the CMU project remains to be seen, as the adopted legislation is still being phased in, it is time to assess how effectively it was designed and is being implemented by the Commission, and how much progress has been made so far, while taking into account the institutional framework, the role of the Member States, other stakeholders and any relevant external factors. In this connection, we will examine whether the Commission:

- has achieved its objective of diversifying funding sources for EU companies, in particular small and medium-sized enterprises;
- has proposed measures for fostering more integrated and deeper capital markets;
- is implementing the CMU in such a way that the measures of the action plan benefit businesses and domestic capital markets, in particular by making use of technical assistance and aligning the CMU action, as appropriate, with that of other EU programmes.

Since we identified the issues underlying these areas of enquiry before the audit work got underway, they should not be regarded as audit observations, conclusions or recommendations.

ABOUT ECA SPECIAL REPORTS AND AUDIT PREVIEWS

The ECA's special reports set out the results of its audits of EU policies and programmes or management topics related to specific budgetary areas.

Audit previews provide information in relation to an ongoing audit task. They are based on preparatory work undertaken before the start of the audit and are intended as a source of information for those interested in the policy and/or programme being audited.

If you wish to contact the team in charge of this audit, please do so at the following e-mail address: **ECA-CMU-audit@eca.europa.eu**.

[1] New Financial, Report: A decade of change in European Capital Markets, February 2018.

[2] The Investment Plan for Europe, which has three "pillars": to mobilise private investment, to promote the visibility of investment opportunities, and to improve the business environment by removing regulatory barriers. The CMU essentially relates to the third pillar.

[3] Vienna Initiative, Report by the Working Group on CMU, 12 March 2018.

[4] Mission letter from Ursula von der Leyen President-elect of the European Commission to Valdis Dombrovskis, Executive Vice-President-designate for An Economy that Works for People, 10 September 2019.

[5] An annual mechanism, overseen by the Commission and endorsed by the Council, for coordinating economic policy in all the EU Member States.