



Capital Markets Union, relevance for Central and Eastern Europe and securitisation in practice

Filip Keereman and Corina Weidinger*

**Head of Unit and economist
National Financial Systems (FISMA.E.2)**

Round table: CMU
Central Bank of Austria

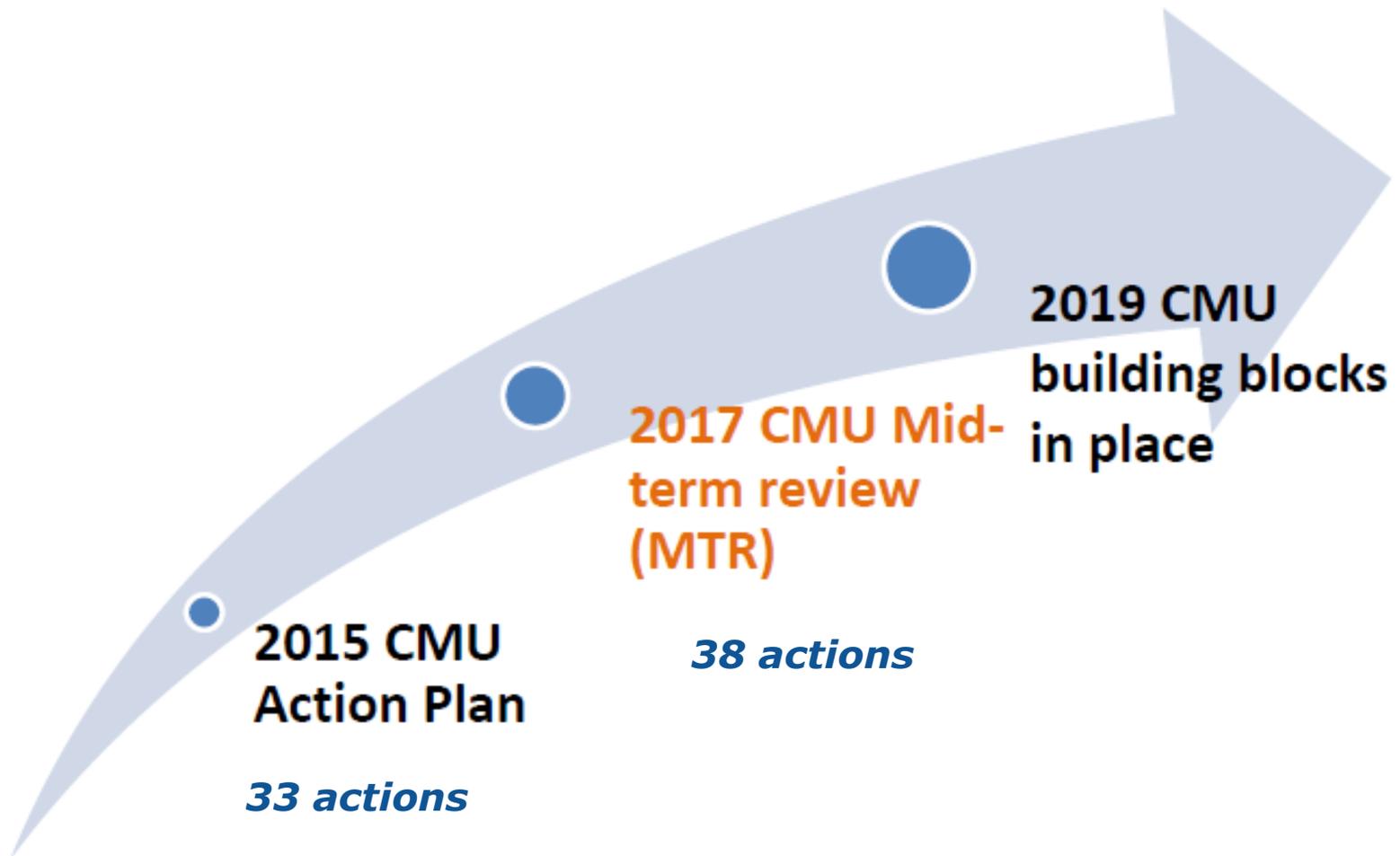
20 June 2018
Vienna

Outline

- I. Background and context**
- II. Relevance of CMU for Central and Eastern Europe**
- III. Securitisation**
- IV. Concluding remarks**

Background and context

- The CMU Action Plan, adopted by the European Commission in September 2015 and a key priority of President Juncker to boost investment, jobs and growth, (http://ec.europa.eu/finance/capital-markets-union/docs/building-cmu-action-plan_en.pdf) aimed at promoting alternative sources of finance, complementary to bank-financing, including capital markets, venture capital, crowdfunding and the asset management industry with special attention for SMEs and start-ups
- Mid-Term Review of the CMU Action Plan, adopted by the Commission in June 2017 (https://ec.europa.eu/info/publications/mid-term-review-capital-markets-union-action-plan_en) with stronger focus on sustainable and green financing, fintech and local and regional capital market development (in particular in countries with high catch-up potential, such the CESEE region)



Why do we need the CMU

Bank lending to EU companies has contracted since the crisis and there is a lack of alternative funding

European start-ups and SMEs need more funding to invest in innovation and growth

Access to stock markets is costly and complex for European businesses

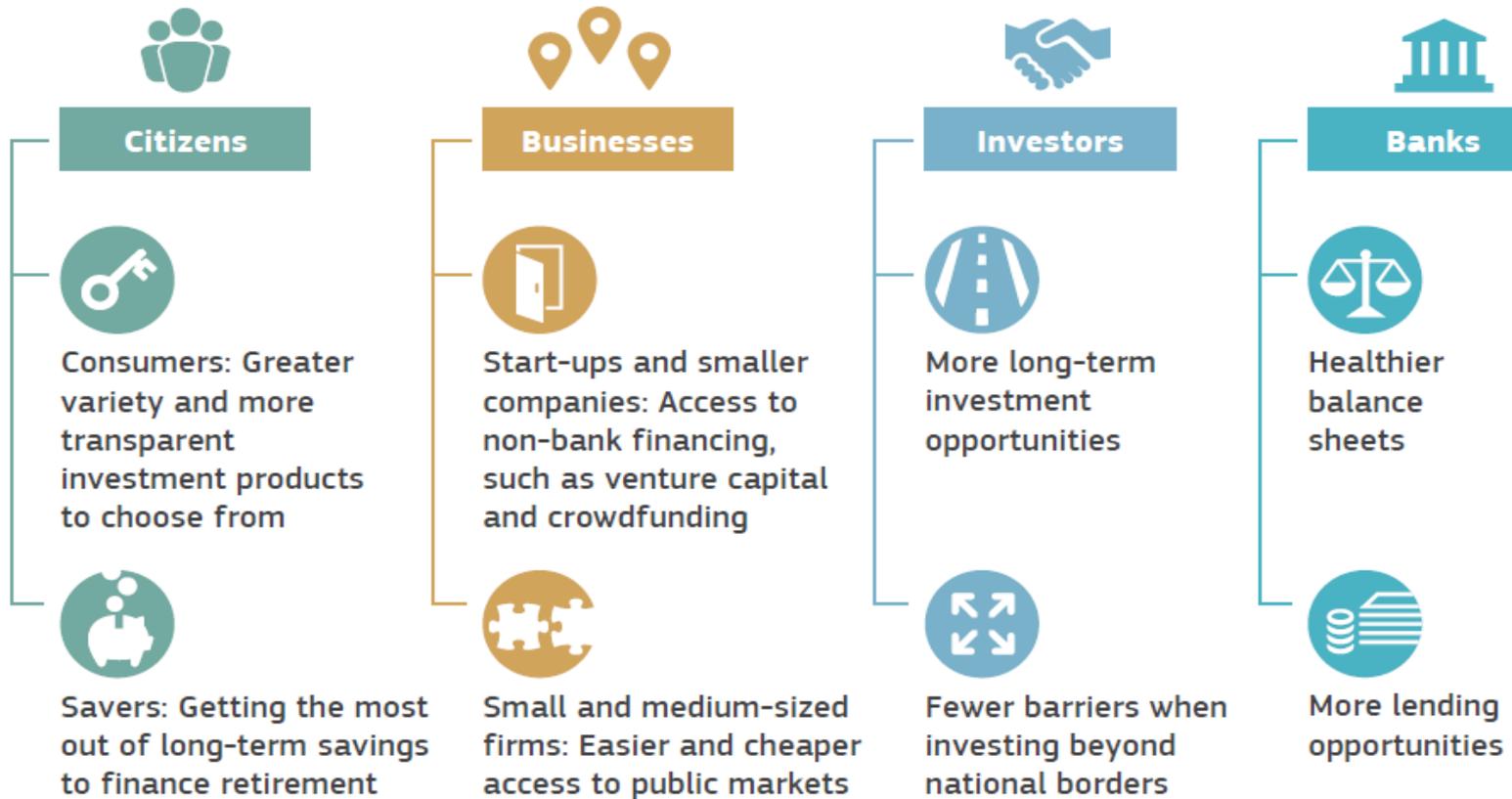
Investors face many barriers when investing in other EU countries

EU households have one of the highest savings rate worldwide, but most of it is not put to good use



European
Commission

WHO BENEFITS FROM THE CAPITAL MARKETS UNION?



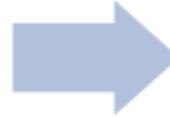
What challenges is the MTR addressing?

Future departure of the UK from the Single Market



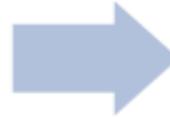
Strengthening EU-27 capital markets

Uneven standards of supervision and enforcement



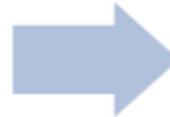
Make the supervisory framework more effective and consistent

FinTech is transforming capital markets



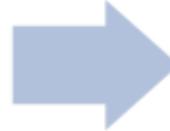
Increase competition and lower costs for businesses and investors

Europe must face environmental and social challenges



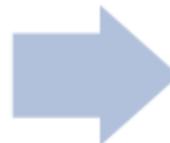
Re-engineer the financial system to make investments more sustainable

Challenges set out in CMU Action Plan remain as relevant as ever



Need for ambitious implementation of outstanding CMU actions

Capital markets are still very diverse across Europe



Savers and businesses in all Member States should benefit from capital markets

Supervision (I)

- The supervisory framework is a key component for well-functioning and integrated capital markets
- Strong and effective supervision performed to the same standard across all markets ensures a level playing field for market participants and eliminates regulatory arbitrage
- **Propose amendments to the functioning of the European Supervisory Authorities (ESAs) and ESRB to promote more effective supervision;** in targeted areas, strengthen the powers of ESMA to support a well-functioning CMU
- **Commission proposal - September 2017**

Supervision (II)

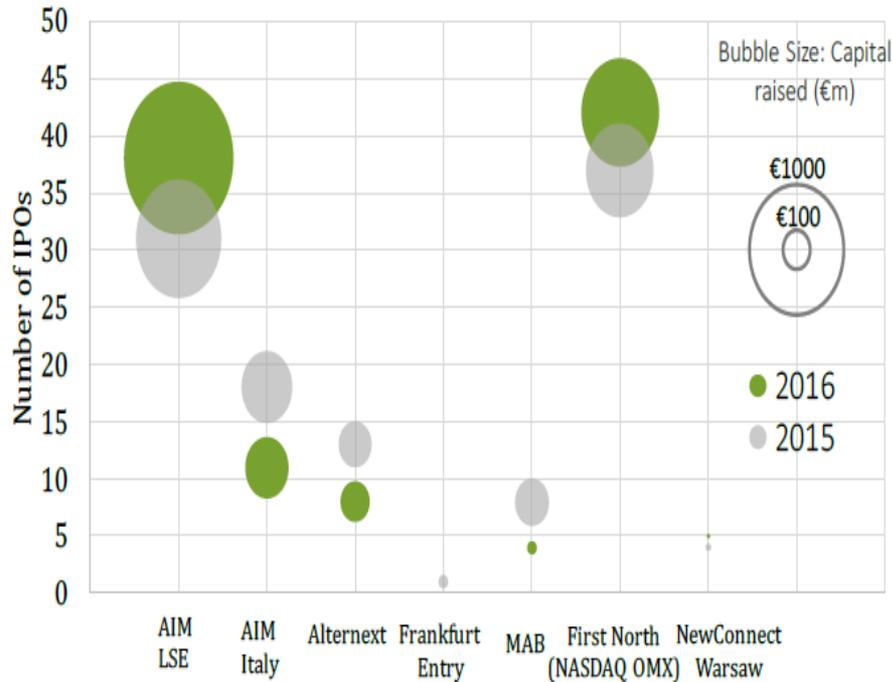
- Main features of the Commission proposal:
 - (i) Stronger **coordination of financial supervision** across the EU
 - (ii) Extended **direct capital markets supervision** by European Securities Market Authority (ESMA); areas of direct supervision: capital market data, capital market entry, capital market actors (certain investment funds), market abuse cases
 - (iii) **Improved governance and funding** of the ESAs
 - (iv) Promoting **sustainable finance** and **FinTech**

Enhance the proportionality of rules to support IPOs

- Public listings of SMEs remain low in the EU, as equity raised on SME-dedicated markets decreased substantially compared to pre-crisis levels
- The current regulatory environment may discourage these firms from raising capital on public markets
- Review how **targeted amendments to EU legislation** can deliver **a more proportionate regulatory environment to support SME listing on public markets**
- **Commission proposal - May 2018**

SME Markets in 2016 - less IPOs, but more proceeds

IPOs on Jr markets (number of deals and capital raised, €m)



- **151 IPOs (2016) vs. 172 (2015)**
- **2,360 EUR Mio. raised in 2016 vs. 2,045 EUR Mio. in 2015**
- **Strong IPO originations on AIM London and First North**

Source: Dealogic

SME listing package (I)

- Commission proposal includes:
 - (i) a regulation which amends certain **technical rules in the Market Abuse Regulation (MAR)** and the **Prospectus Regulation**
 - (ii) technical amendments to **delegated acts** (i.e. to Level 2 measures) **under the MIFID II**
- **Main proposed changes to the SMEs listing rules:**
- Adapt current obligations to keep registers of persons having access to price-sensitive information, to avoid excessive administrative burden for SMEs

SMEs listing package (II)

- Allow issuers with at least 3 years of listing on SMEs Growth Markets to issue a **lighter prospectus when transferring to a regulated market**
- Make it easier for **trading venues specialised in bond issuance to register as SME Growth Markets**
- Create a **common set of rules on liquidity contracts for SME Growth Markets in all Member States**, in parallel to national rules
- Facilitate the **registration of Multilateral Trading Facilities (MTFs) as SME Growth Markets**

Investment firms

- Investment firms provide services which give investors access to securities and derivatives markets
- Authorisation and conduct of investment firms are governed by MiFID, but investment firms are also subject to CRR/CRD
- Need for a more effective prudential and supervisory framework calibrated to the size and nature of these firms
- **Present a legislative proposal to review the prudential treatment of investment firms** (i.e. more proportionate and effective rules for investment firms)
- **Commission proposal - December-2017**

Prudential framework for investment firms

NEW CLASSIFICATION AND PRUDENTIAL REGIME FOR INVESTMENT FIRMS

SYSTEMIC	NON-SYSTEMIC	
CLASS 1	CLASS 2	CLASS 3
<ul style="list-style-type: none"> ▪ Largest firms (with assets over EUR 30 billion) ▪ Carry out risky, bank-like activities ▪ Will remain under CRR/CRD and subject to banking supervision 	<ul style="list-style-type: none"> ▪ Large firms, above specific thresholds (e.g. assets under management, balance sheet, revenues, etc) ▪ New risk assessment tailored to their business ▪ Simplified version of existing rules (if they trade financial instruments) 	<ul style="list-style-type: none"> ▪ Smaller, non-interconnected firms ▪ Simpler capital requirements (higher of initial capital or fixed costs in previous year)

WHAT WILL CHANGE IN THE FUTURE?

		REGULATION	SUPERVISION
Class 1	TODAY	CRR/CRD	National arrangements
	NEW REGIME	CRR/CRD	Banking supervisor (SSM for Banking Union)
Class 2&3	TODAY	CRR/CRD	National arrangements
	NEW REGIME	New prudential regime for investment firms	National arrangements

FinTech

- FinTech can contribute to deepening and broadening EU capital markets by integrating the potential to change business models through data-driven solutions in asset management, intermediation and product distribution
- **Commission will assess the case for an EU licensing and pass-porting framework for FinTech activities;** this will draw on the results of an public consultation with stakeholders
- **Commission proposal – March 2018: Action plan on FinTech and legislation on crowdfunding**

FinTech action plan

ENCOURAGE INNOVATIVE BUSINESS MODELS

- Easier and more uniform licensing rules for new FinTech activities

COMMISSION INITIATIVE TODAY

- New EU rules to enable crowdfunding
- Align standards
- Supervisors help FinTech firms apply rules and access market ('innovation facilitators')
- 'Regulatory sandboxes': Supervisors apply rules to FinTech firms in flexible and proportionate way

A MORE COMPETITIVE AND INNOVATIVE FINANCIAL MARKET

- Facilitate information sharing on cyber threats among market participants
- Higher supervisory convergence and enforcement of IT risk management
- Increased EU coordination in cyber threat testing

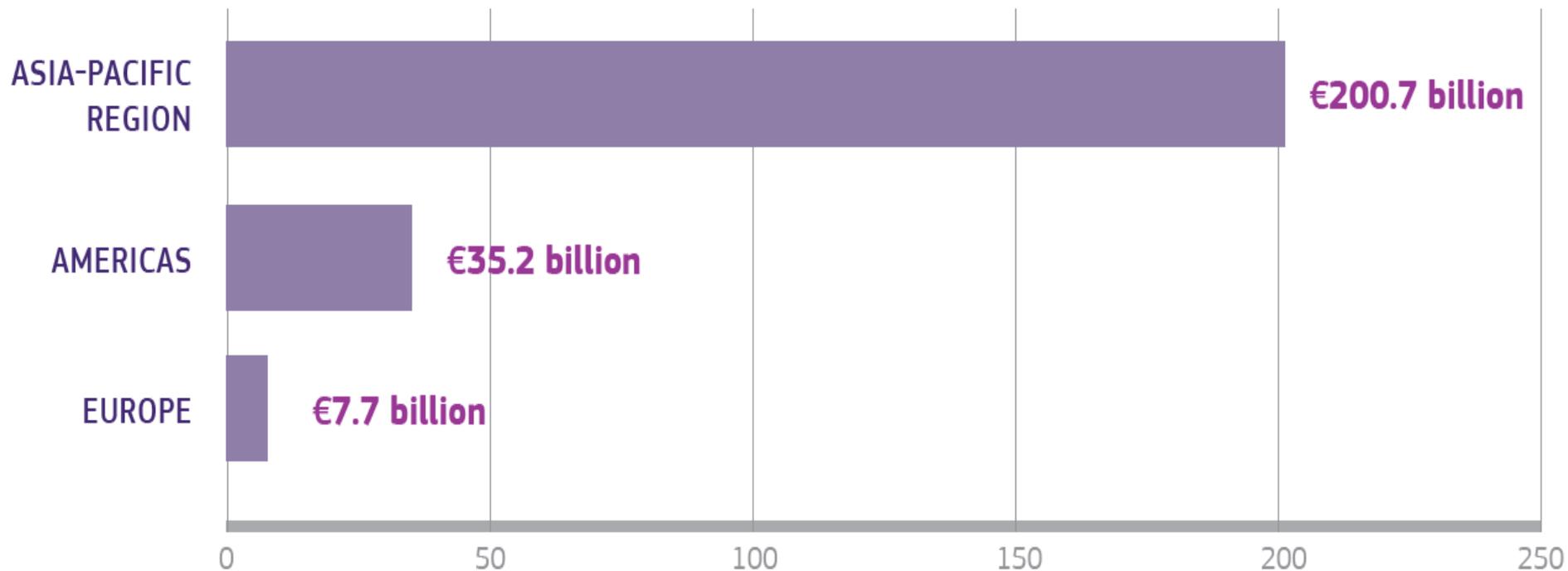
STRONGER CYBER RESILIENCE

- Assess whether current EU rules are adapted to new technologies (e.g. distributed ledger technology, artificial intelligence)
- Clarify rules to facilitate use of cloud services
- EU initiative to promote blockchain, including in financial services
- New 'EU FinTech Lab' to increase knowledge of technologies among EU and national authorities

SUPPORT UPTAKE OF NEW TECHNOLOGIES

Crowdfunding (I)

CROWDFUNDING IN EUROPE IS STILL UNDERDEVELOPED



Crowdfunding (II)

The Commission proposed **regulation on crowdfunding**:

- Establishes a **one-stop-shop access** to the EU market and therefore helps crowdfunding platforms in overcoming the barriers they face operating cross-border
- Provides **tailored rules for European crowdfunding services providers** covering investment-based and lending-based business models
- Gives **more opportunities to European investors** while safeguarding a high level of investor protection in relation to crowdfunding services
- Defines the **requirements** crowdfunding service providers have to fulfil in order **to get the authorisation and provides a single point of entry for authorisation and supervision** by ESMA

Support secondary markets for non-performing loans (NPLs)

- NPLs are weighing heavily on several banking sectors of Member States, impacting therefore the capacity of banks to lend
- Policies aimed at improving the functioning of NPL secondary markets– including capital market solutions- are a key part of durable solution for NPL resolution
- **Present measures to support secondary markets for NPLs**
- **Launch an impact assessment for a possible legislative proposal to strengthen the ability of secured creditors to recover value from secured loans to corporates**
- **Proposal for an accelerated enforcement of collateral by banks and measures to support the secondary markets for NPLs**
- **Commission proposal – March 2018**

Non-performing loans package (I)

The Commission proposal of measures to tackle NPLs includes the following initiatives:

(i) A **regulation** amending the capital requirements regulation (CRR) – introduces **common minimum coverage levels for newly originated loans that become NPLs (statutory prudential backstop)**

(ii) A **directive on credit servicers, credit purchasers and the recovery of collateral** – to support the development of markets for distressed assets

(iii) A **blueprint on the setting-up of national asset management companies (AMCs)**

Non-performing loans package (II)

The package sets out a comprehensive approach with a mix of complementary policy actions that target four key areas:

- Ensuring that **banks set aside funds** to cover the risks associated with loans issued in the future that may become NPLs
- Encouraging the **development of secondary markets** where banks can sell their NPLs to credit servicers and investors
- **Facilitating debt recovery**, as a complement to the insolvency and business restructuring proposal put forward in November 2016
- Assisting Member States that so wish in the restructuring of banks, by **providing non-binding guidance** for establishing AMCAs or other measures dealing with NPLs

Sustainable finance

- Reorienting private capital flows to more sustainable investment requires comprehensive and deep rethinking of financial framework
- **Decide concrete follow-up to recommendations of High Level Expert Group on Sustainable Finance (by Q1-2018)**
 - Launch work to prepare measures to improve disclosure and better integrate sustainability in rating methodologies and supervisory processes, as well as in the investment mandates of institutional investors and asset managers
 - Develop an approach for taking sustainability considerations into account in upcoming legislative reviews
- **Commission proposal - May 2018**

Sustainable finance package (I)

The Commission proposal includes 3 legislative initiatives:

(i) A regulation on the **establishment of a framework to facilitate sustainable investment**

(ii) A regulation on **disclosures relating to sustainable investments and sustainability risks** amending Directive (EU) 2016/2341 (IORPs)

(iii) A regulation amending Regulation (EU) 2016/1011 (BMR) on **low carbon benchmarks and positive carbon impact benchmarks**

The Commission also launched consultations on targeted amendments to MIFIDII and the Insurance Distribution Directive in respect of suitability test requirements

Sustainable finance package (II)

Main features of the package:

- Establishment of a **unified sustainable finance “taxonomy”**, to help businesses and investors to determine whether an economic activity is environmentally-sustainable by creating a common classification system
- Improvement of **consistency of how institutional investors should integrate (environmental, social and governance) ESG factors into their investment decision-making process**
- Creation of **low-carbon and positive-carbon impact benchmarks** – the new benchmarks should reflect companies’ carbon footprint and give investors greater information on an investment portfolio’s carbon footprint

Investment funds

- Investment funds in the EU are still small and less cost-efficient than in some other jurisdictions, with fund distribution remaining geographically limited; evidence from public consultation shows that the lack of regulatory and supervisory convergence contributes to this situation
- Greater cross-border distribution (in particular digital cross-border distribution) would allow funds to grow, allocate capital more efficiently across the EU and deliver better value
- **Launch an impact assessment for a possible legislative proposal to facilitate the cross-border distribution of UCITS and AIFs**
- **Legislation to facilitate cross-border distribution of investment funds**
- **Commission proposal – March 2018**

Breaking down barriers to cross-border investments

Commission proposal includes:

- (i) A Regulation, which **improves transparency** by aligning national marketing requirements and regulatory fees; it introduces **more consistency** in the way these regulatory fees are determined; it enables ESMA to better monitor investment funds
- (ii) A Directive, which **harmonizes the conditions under which investment funds may exit a national market**; it creates the possibility for asset managers to stop marketing an investment fund in defined cases in one or several host Member States; it also allows European asset managers **to test the appetite of potential professional investors for new investment strategies through pre-marketing activities**

Treatment of cross-border EU investments

- EU single market freedoms provide comprehensive rules for investment protection; national authorities might not always be fully aware of such rules/may find them difficult to apply
- Intra-EU investors may lack appropriate mechanisms to prevent disputes with Member States or solve them amicably
- **Launch an impact assessment with a view to setting out an adequate framework for amicable resolution of investment disputes; currently on-going**
- **Adopt interpretative Communication to provide guidance on existing EU rules for the treatment of cross-border EU investments**

Upcoming initiatives (I)

Comprehensive EU strategy on local and regional capital market developments across the EU (Communication)

Report on best practice in supply chain finance

Recommendations on private placements to promote best practices

Implementing measures on prospectuses for public offerings

Communication (roadmap) on corporate bond market liquidity

Assessment of the impact of MiFID II level 2 rules on listed SME equity research (non-legislative measure)

Monitor progress on IASB commitment to improve disclosure, usability and accessibility of IFRS (non-legislative measure)

Upcoming initiatives (II)

Develop best practices on the use by Member States of EU funds to partially finance costs borne by SMEs when seeking admission

Assessment of the drivers of equity investments by insurance companies and pension funds

Assessment and amendment of the prudential treatment of private equity and privately placed corporate debt in Solvency II

Report on whether the accounting treatment of equity instruments in IFRS 9 is sufficiently conducive to long-term financing

Assessment of distribution systems of retail investment products across the EU

Recurrent reporting by the ESAs of cost and performance of the principal categories of long-term retail investment and pension products

Feasibility study on the development of a centralised hub for mandatory disclosure requirements and related services

Based on MS experience with Investment Savings Account and an existing study on employee share ownership schemes, develop best practices

Upcoming initiatives (III)

Amendments to Commission Delegated Regulation to introduce a specific prudential treatment for STS securitisation in Solvency II

Assess the case for European Secured Notes for SME loans and infrastructure loans

Benchmarking study on outcomes that banks experience under national loan enforcement (including insolvency) systems when managing defaulting loans

Communication (roadmap) to address remaining Giovannini barriers and other barriers

Study on discriminatory tax obstacles to cross-border investment by pension funds and life insurers

Facilitate the cross-border exercise of shareholder rights, including voting in the implementation of the Shareholders Rights 2 Directive published on 20 May 2017 (DG JUST)

Interpretative Communication to provide guidance on the existing EU standards

Impact assessment on a possible framework for the amicable resolution of investment disputes

Development of capital markets

Priority action 9 under the MTR

By Q2 2018, the Commission will propose a comprehensive EU strategy on steps that can be taken at EU level to support local and regional capital market development across the EU. This will build on the report of the Vienna Initiative's CMU Working Group and will take account of experience through the growing delivery of on-demand technical support under the Commission's Structural Reform Support Programme.

Council Conclusions, 11 July 2017

[...]

LOOKS FORWARD to a comprehensive EU strategy to be prepared by the Commission on steps that can be taken at the EU level to support local and regional market development across the EU. [...]

UNDERLINES the importance of enhancing the efficiency of European financial markets as a whole, which implies striking the right balance between harmonised rules and the need to cater for local and regional market characteristics [...].

Outline

- I. Background and context
- II. Relevance of CMU for Central and Eastern Europe**
- III. Securitisation
- IV. Concluding remarks

Outline

II. Relevance of CMU for Central and Eastern Europe

1. The Vienna Initiative

2. Financial markets in CESEE: state of play

3. Policy suggestions

Vienna Initiative

	Vienna Initiative 1	Vienna Initiative 2
Launched	2009	2012
Organisation	Public-private sector coordination platform without formal organisation structure	More formal structure, with Steering Committee (Chair Boris Vujcic, CNB, succeeded to Marek Belka, NBP) and a Secretariat (EBRD)
Membership	EBRD, IMF, WB, EIB, EC Home countries: AT, IT, EL, BE, FR, DE, SE, FI Host countries with BOP programmes: HU, RO, RS, BiH, LV	Many host countries in the CESEE joined, including PL, CZ, SK, LT, EE as well as non EU: UA , AL and FYROM
Focus	Commitments of banks to maintain exposures to the BOP programme countries (to avoid run to the exit) and provide capital support their CESEE subsidiaries	Enhancing home-host supervisory coordination and monitoring credit and deleveraging in the CESEE

Vienna Initiative

The establishment of the Working Group on Capital Markets Union under the Vienna Initiative at the Full Forum in Luxembourg on 6 March 2017 is one of the actions to help in this process developing local capital markets.

EBCI | Vienna Initiative



(Parallel Working Group on making better use of the International Financial Instruments offered by the International Financial Institutions: first meeting on 29 June 2017 in Brussels, 27 November in Vienna, 15 June in Luxembourg)

Terms of reference

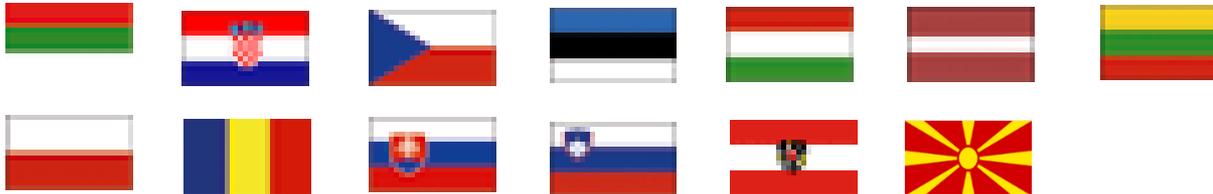
Objective

"The key objective of the Working Group will be to identify the most significant gaps in the capital market regulatory and institutional frameworks of the CESEE countries in terms of funding investment needs, and to identify the most promising channels for capital market development, taking account of the different business and economic structure of the countries concerned."

Vienna Initiative

Working Group

Countries: 12 Member States + Macedonia (Stock Exchange, Financial Services Supervisor, Central Bank, Ministry of Finance)



Interest groups: Association for Financial Markets in Europe (AFME), Eurochambers

Commercial banks: Erste Group Bank, KBC Group, Raiffeisen Bank International, Unicredit

Three meetings of the Working Group were held in Brussels during 2017: 4 April, 30 June and 3 October 2017

Output

A report by end 2017, adopted at the Full Forum in London (EBRD) on 12 March 2018 (<http://vienna-initiative.com/wp-content/uploads/2018/03/VI-CMU-Working-Group-Final-Report-March-2018.pdf>)

The Reports by the Vienna Initiative do not bind any of the participants.

Outline

II. Relevance of CMU for Central and Eastern Europe

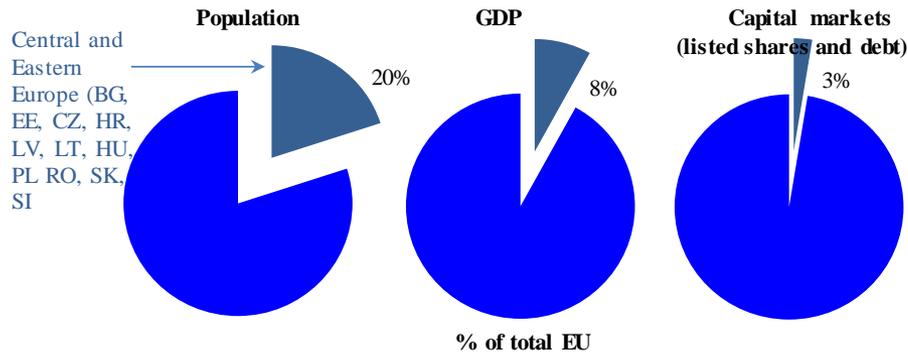
1. The Vienna Initiative
2. Financial markets in CESEE: state of play
3. Policy suggestions

2. Financial markets in CESEE: state of play

1. **The catch-up potential of financial markets in CESEE**
 - **Capital markets and bank intermediation**
 - **Capital markets and growth**
2. **Demand for funding**
 - **Corporates**
 - **SMEs**
 - **Financial education**
 - **Structure of the economy**
3. **Supply of funding**
 - **The importance of institutional investors**
 - **The role of private equity**
 - **Households saving preferences**
 - **The regulatory environment**
 - **Market infrastructure**

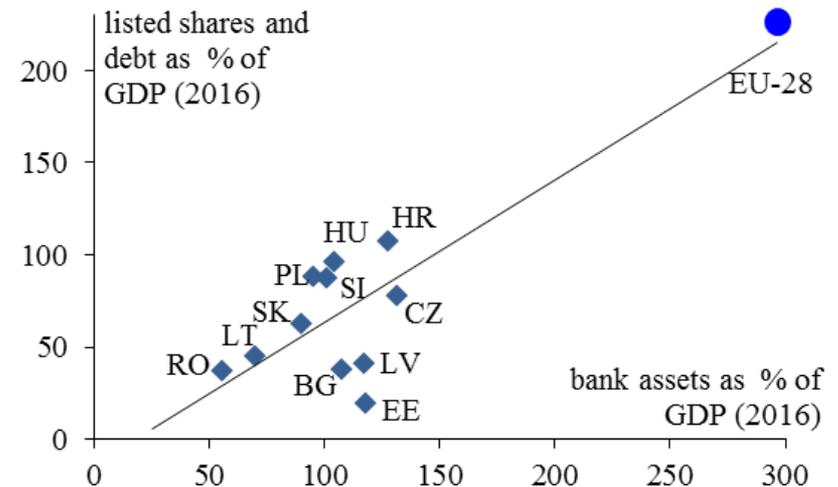
The catch-up potential of financial markets in CESEE

The underdevelopment of Capital markets in CESEE in perspective



Source: Eurostat, ECB

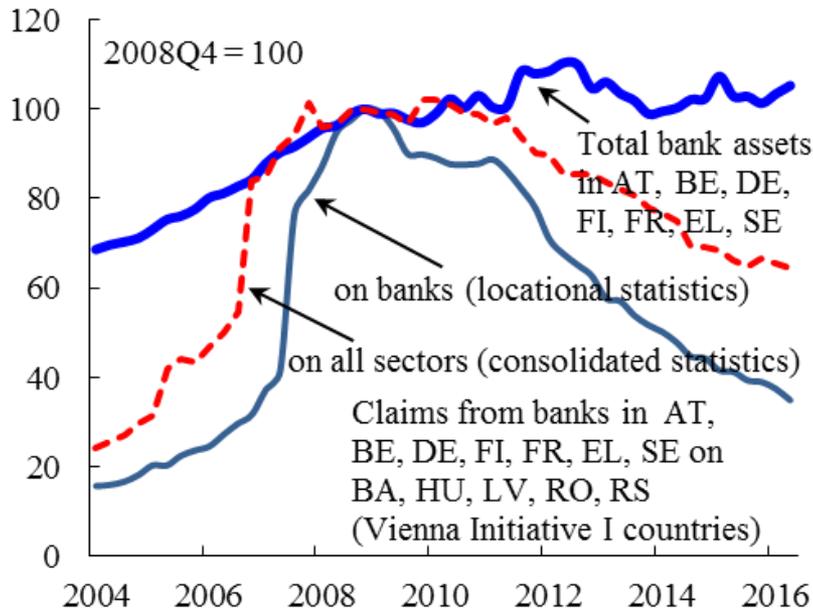
Capital markets vs bank intermediation



Source: ECB

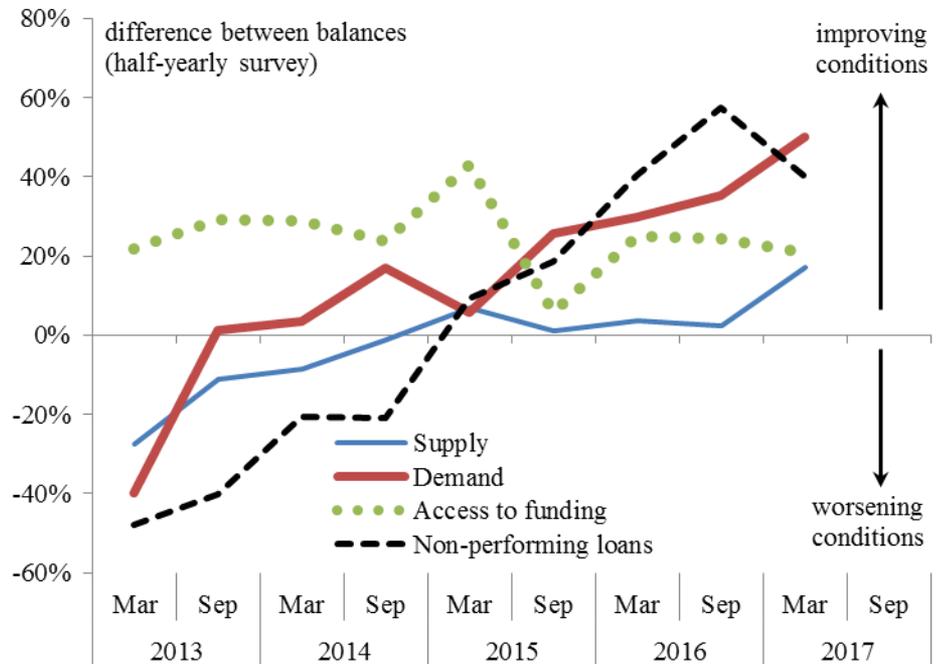
The catch-up potential of financial markets in CESEE

Bank deleveraging towards CESEE

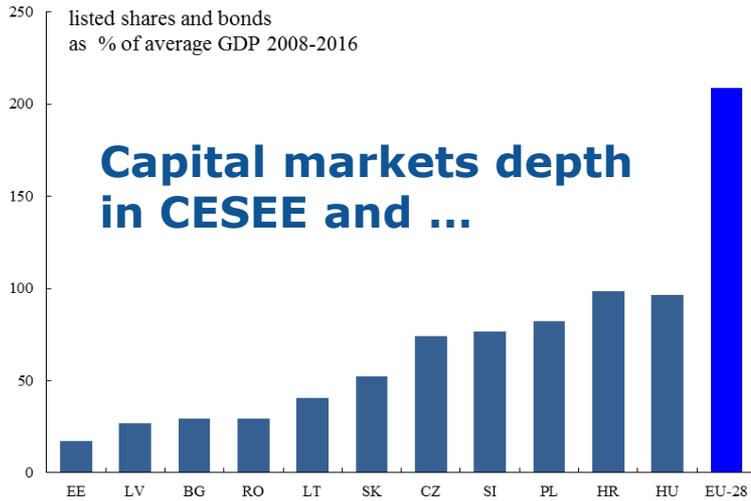


Source: ECB, BIS

Bank lending conditions in CESEE

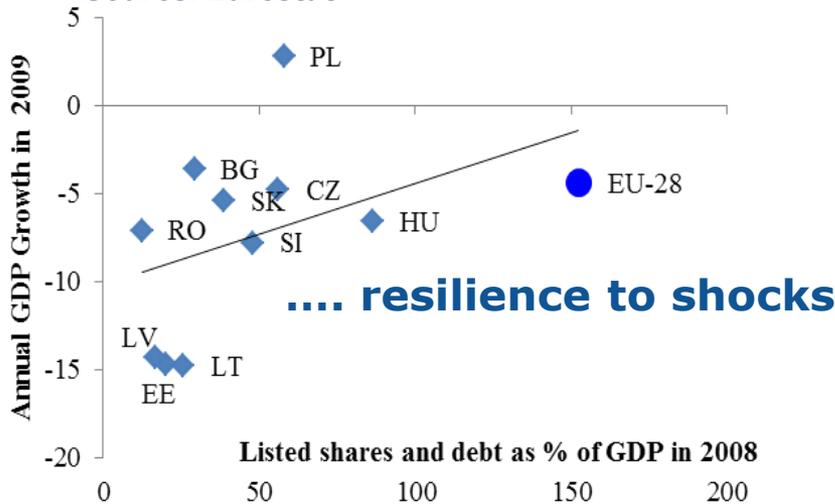


Source: EIB CESEE Bank Lending Survey 41

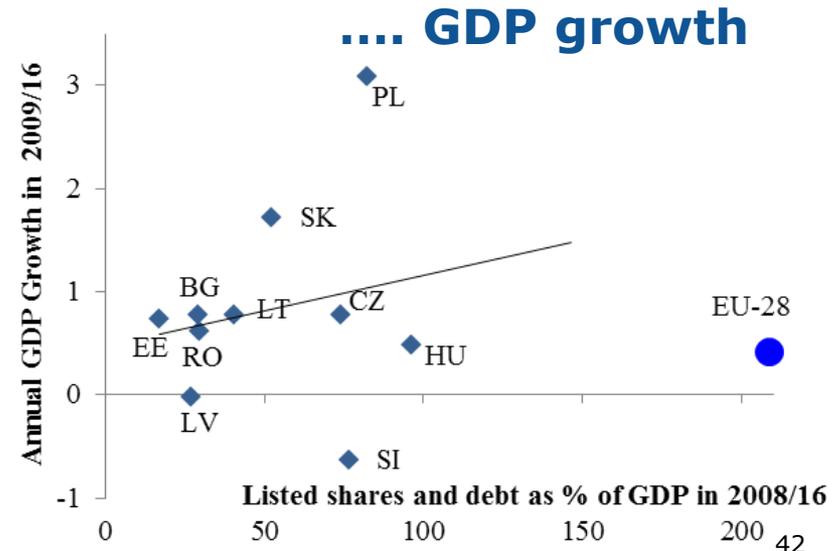


The catch-up potential of financial markets in CESEE

Source: Eurostat



Source: ECB



Source: ECB

2. Financial markets in CESEE: state of play

1. The catch-up potential of financial markets in CESEE
 - Capital markets and bank intermediation
 - Capital markets and growth
2. Demand for funding
 - Corporates
 - SMEs
 - Financial education
 - Structure of the economy
3. Supply of funding
 - The importance of institutional investors
 - The role of private equity
 - Households saving preferences
 - The regulatory environment
 - Market infrastructure

Demand for funding

The financing structure of corporates

2015 % total financial liabilities	Own resources	<i>of which</i>			Debt securities	Loans	Other accounts receivable / payable
		Listed shares	Unlisted shares	Other equity			
EU-28	54,0	20,9	-	-	5,7	28,6	6,4
Bulgaria	49,9	1,2	23,7	25,0	1,3	38,9	9,8
Czech Republic	52,3	7,7	27,2	17,4	5,4	24,9	16,5
Estonia	60,9	2,2	47,3	11,3	3,0	28,4	7,5
Croatia	45,6	13,8	10,0	21,9	2,9	43,4	8,0
Latvia	41,6	2,1	-	-	0,5	38,3	19,6
Lithuania	58,6	3,0	52,9	2,7	0,2	25,6	15,5
Hungary	59,5	4,8	17,9	36,8	0,7	31,7	7,5
Poland	50,5	12,4	12,1	26,1	3,9	30,4	14,8
Romania	38,9	6,2	19,5	13,2	0,1	36,0	25,0
Slovenia	46,0	7,8	11,8	26,5	1,9	38,3	13,6
Slovakia	47,2	2,2	42,9	2,2	3,0	27,7	22,1

Source: Eurostat

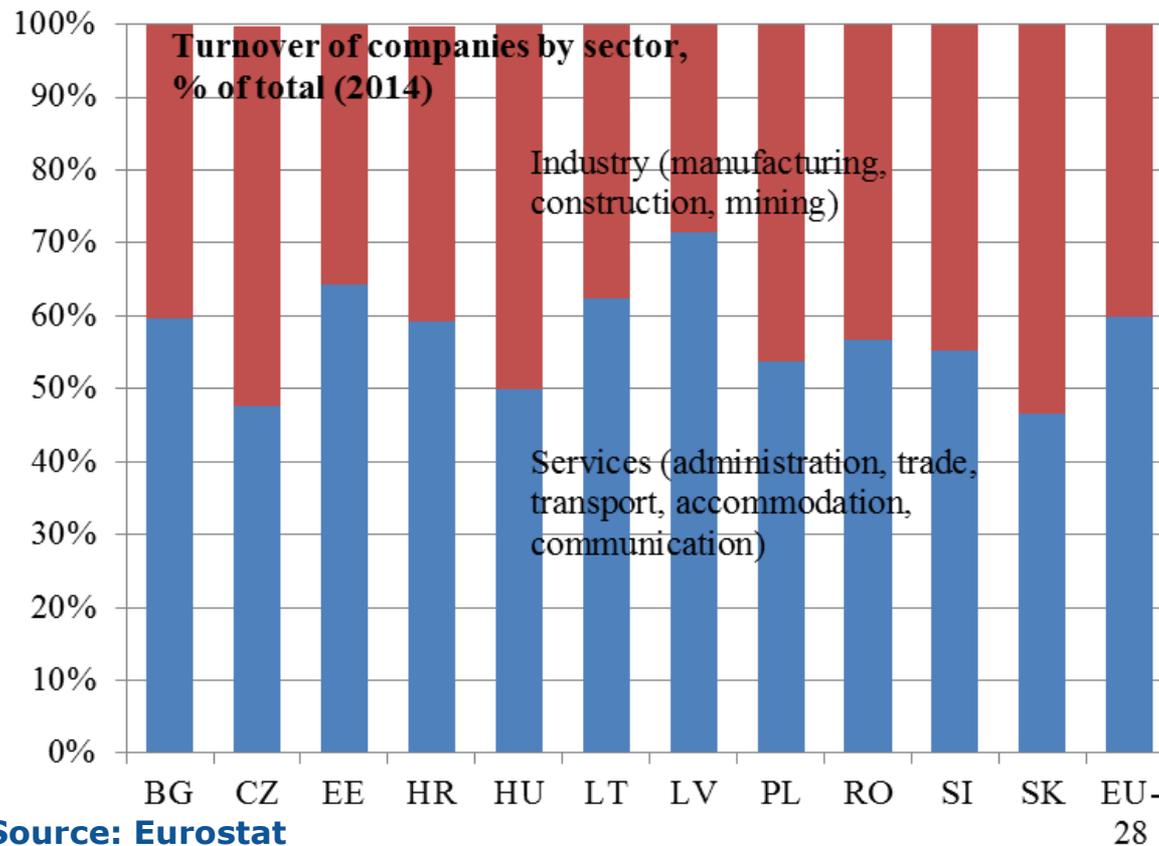
Regulatory change and the demand for funding by banks

MREL - Minimum Required Eligible Liabilities:

- **New regulation, e.g. on a minimum of 'bail-inable' liabilities for bank restructuring, may set new trends in capital market development and give a potential boost to bank bond markets**
- **Risk of crowding out corporate bond markets**
- **Given the small size of local capital markets, international investors need to play a role**

Demand for funding

The structure of the economy



Source: Eurostat

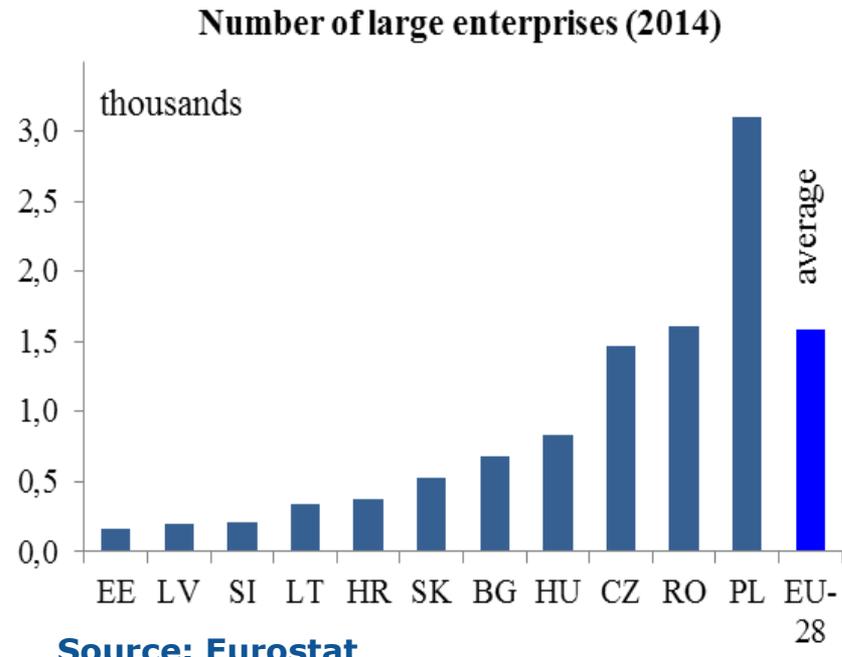
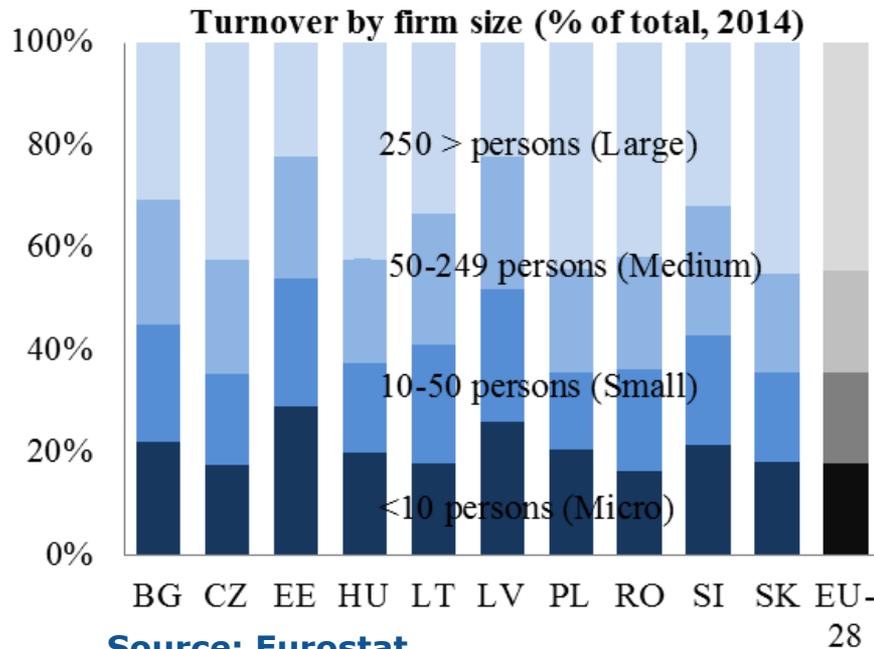


European Commission

Demand for funding

Firm size and turnover:
Importance of SMEs: 70%
of employment; 60% of
turnover (56% in EU-28)

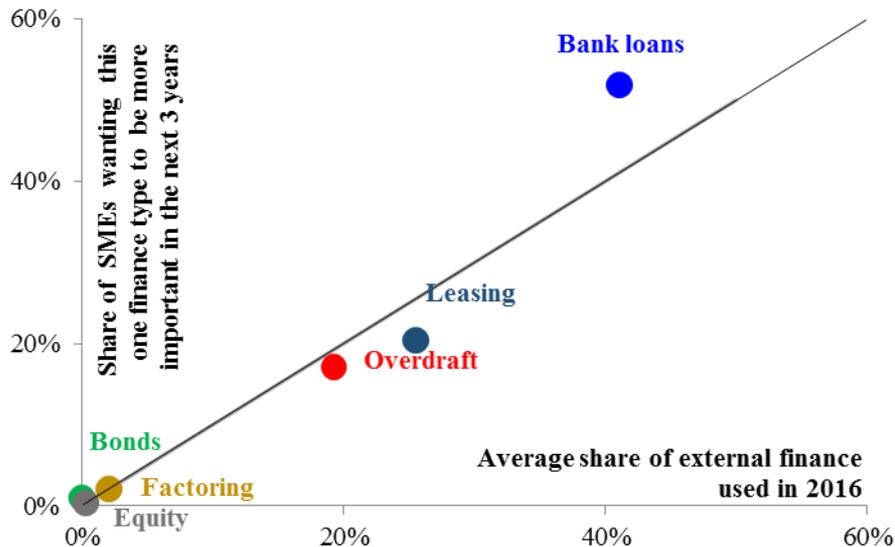
Only Poland with more
than 3000 large firms is
significantly above the EU
average



Demand for funding

Access to finance: problem for 6% to 15% of SMEs in CESEE (9% EU-28)

Financial education: confidence in talking about finance



Source: EIB, Investment Survey 2017

yes, %	With banker	With equity and venture capital investor
EU-28	67	22
Bulgaria	75	22
Czech Republic	69	9
Estonia	57	21
Croatia	62	16
Latvia	43	12
Lithuania	44	20
Hungary	59	18
Poland	67	25
Romania	51	14
Slovenia	62	12
Slovakia	69	23

Source: SAFE Survey 2016

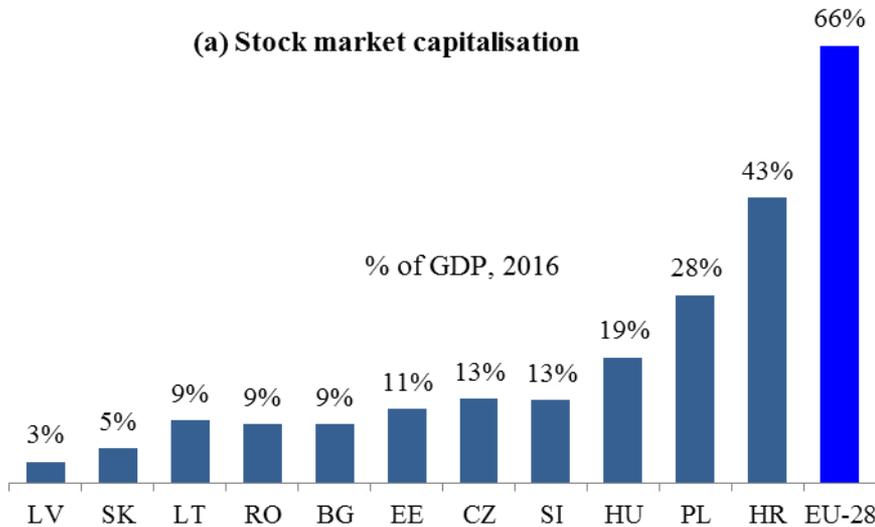
2. Financial markets in CESEE: state of play

1. The catch-up potential of financial markets in CESEE
 - Capital markets and bank intermediation
 - Capital markets and growth
2. Demand for funding
 - Corporates
 - SMEs
 - Financial education
 - Structure of the economy
3. Supply of funding
 - The importance of institutional investors
 - The role of private equity
 - Households saving preferences
 - The regulatory environment
 - Market infrastructure

Supply of funding

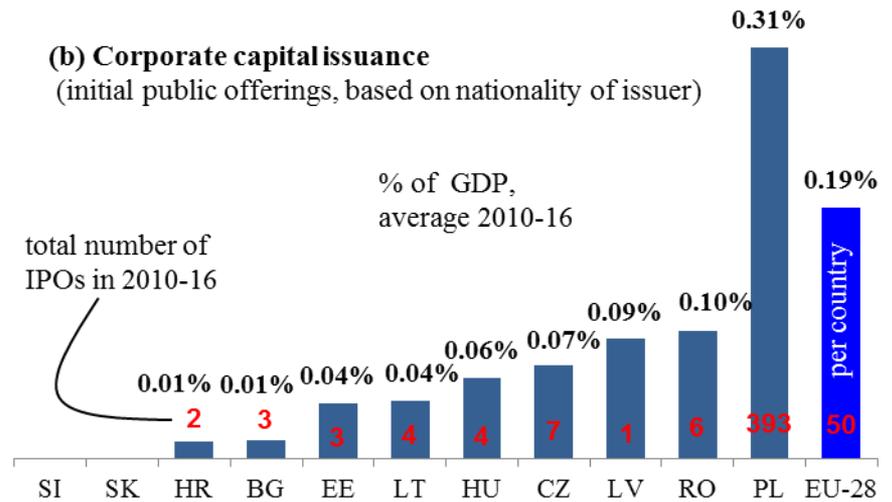
The importance of stock markets

(a) Stock market capitalisation



(b) Corporate capital issuance

(initial public offerings, based on nationality of issuer)

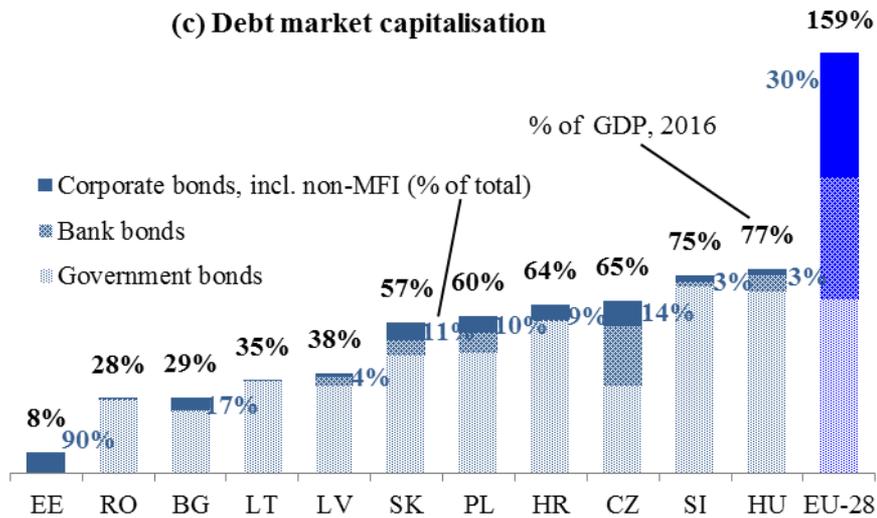


Source: ECB, Association for Financial Markets in Europe

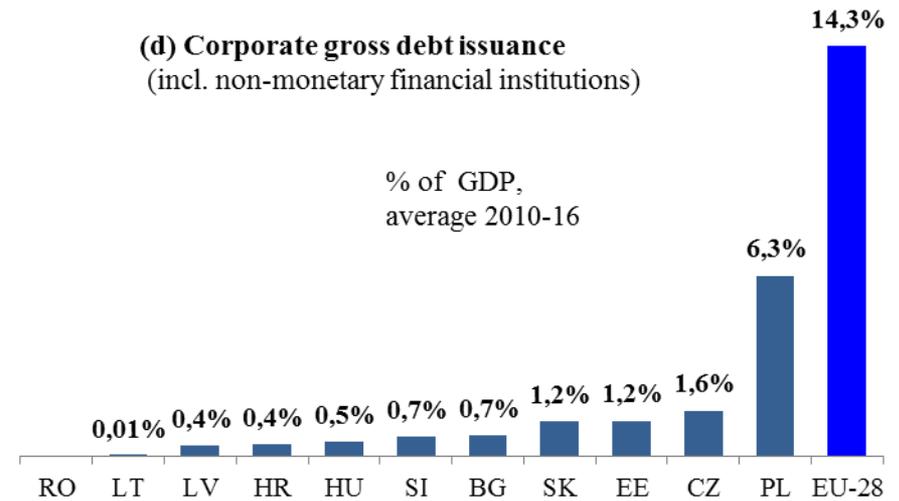
Supply of funding

The importance of debt markets

(c) Debt market capitalisation



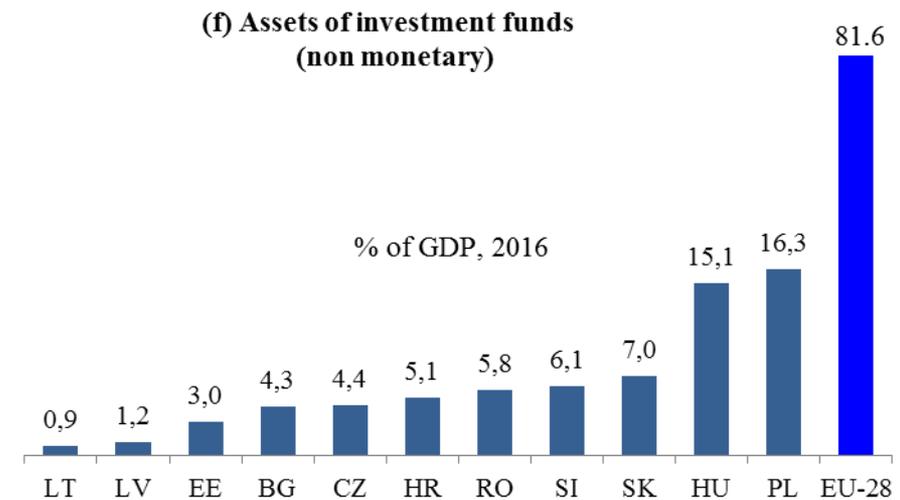
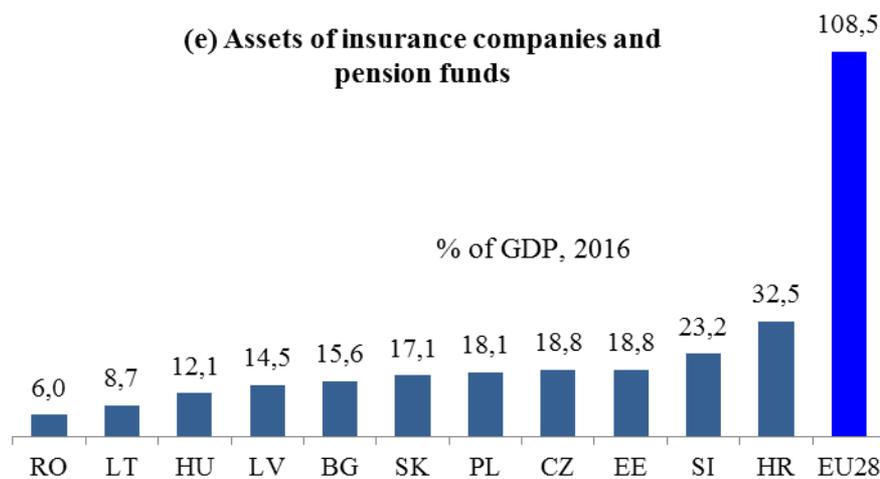
(d) Corporate gross debt issuance
(incl. non-monetary financial institutions)



Source: ECB, Association for Financial Markets in Europe

Supply of funding

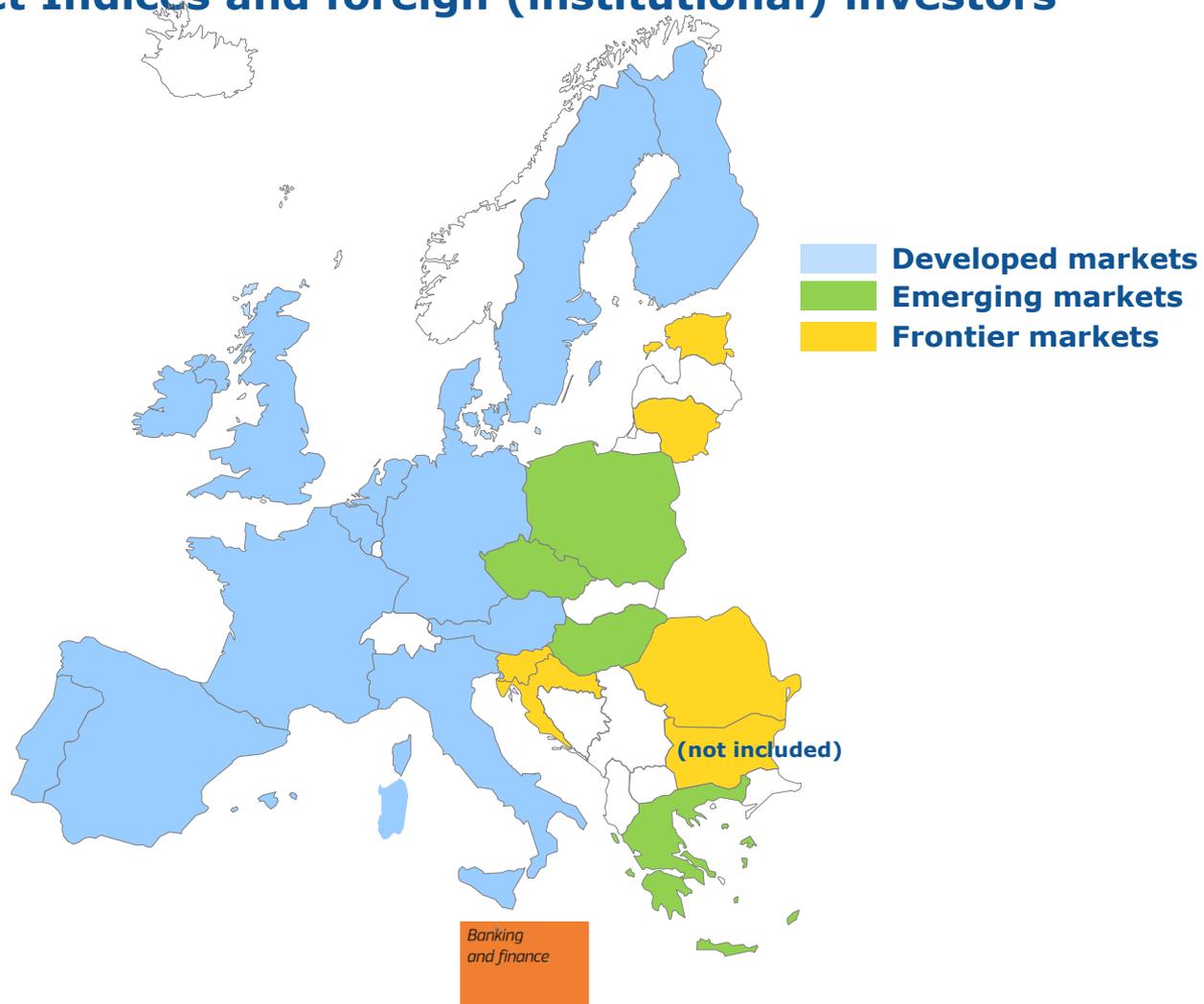
The importance of institutional investors



Source: ECB, Association for Financial Markets in Europe

Supply of funding

MSCI Market Indices and foreign (institutional) investors



Supply of funding

The role of private equity

(2015)	Private equity				Business	Crowd
	total		of which	venture capital	angels	funding
	EUR mio	% of GDP	EUR mio	% of total	EUR mio	EUR mio
EU-28	47464,1	0,32	4400,0	9,3	443,4	5430,0
BG	46,1	0,10	1,1	2,4	4,3	na
CZ	13,8	0,01	1,7	12,1	na	9,0
EE	17,8	0,09	3,7	20,8	6,7	32,0
HR	9,0	0,02	1,2	13,3	0,4	na
LV	35,6	0,15	6,6	18,6	0,8	15,0
LT	48,9	0,13	9,9	20,2	1,2	na
HU	158,3	0,14	25,0	15,8	na	na
PL	887,4	0,21	19,6	2,2	12,4	10,0
RO	144,3	0,09	1,8	1,3	na	na
SI	11,4	0,03	1,4	11,8	1,9	na
SK	11,9	0,02	8,9	74,9	1,8	na
RS	229,1	0,68	0,4	0,2	2,1	na

Note: crowd funding includes peer-to-peer consumer and business lending

Source: Invest Europe, Eban, Cambridge Centre for Alternative Finance

Supply of funding

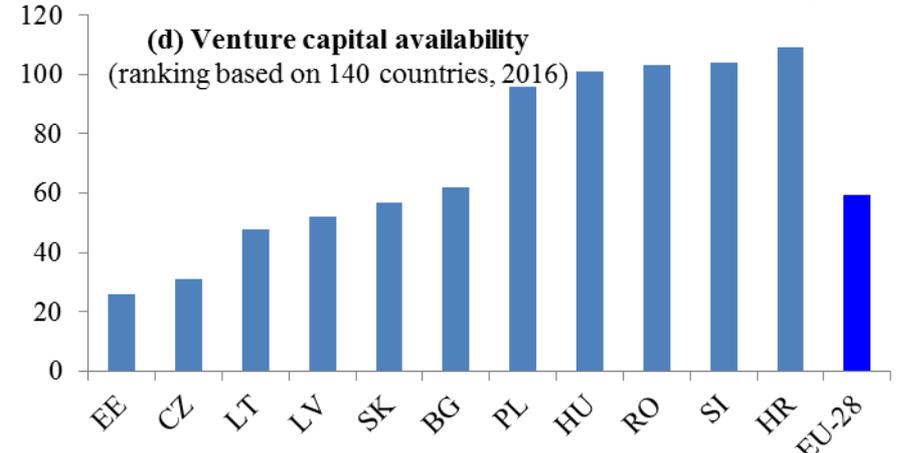
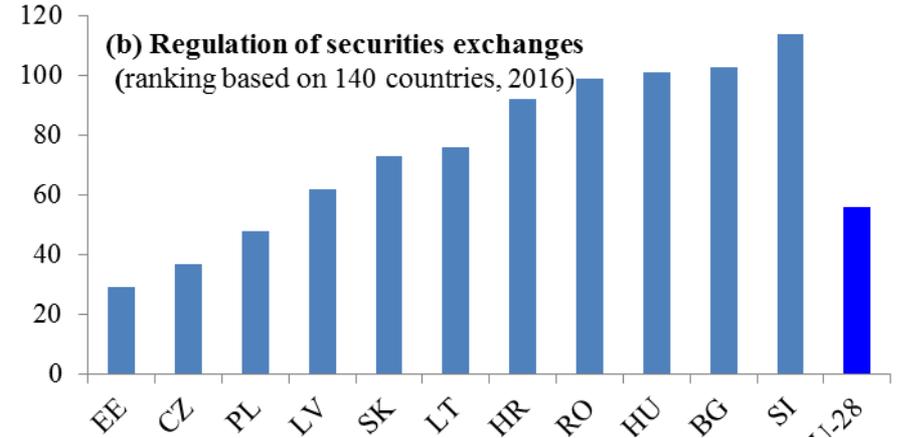
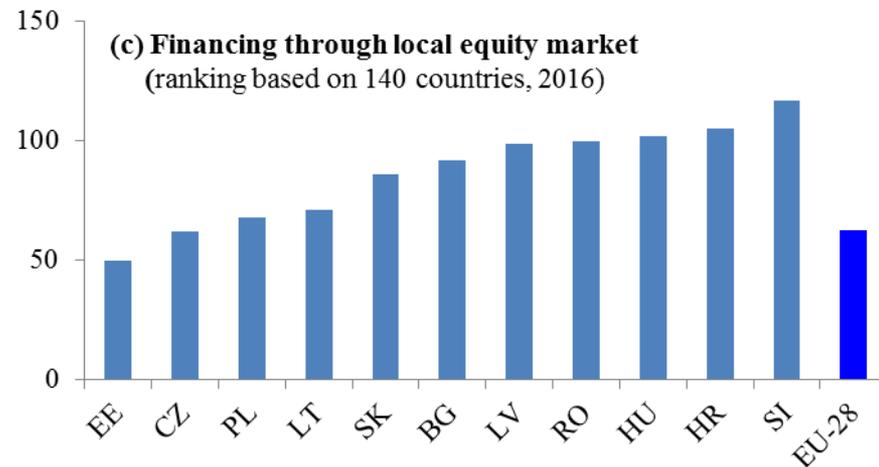
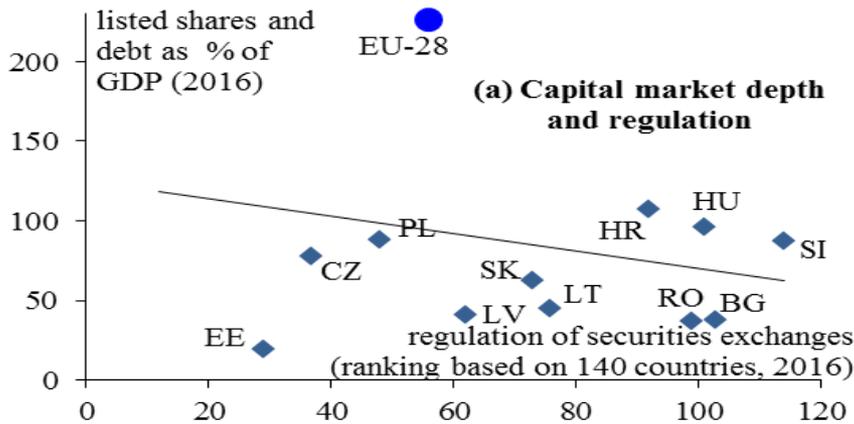
Household savings preferences

<i>% of total, 2015</i>	Currency and deposits	Debt securities	Equity and investment fund	Insurance and pensions	Other
EU-28	30,4	3,1	24,4	39,3	2,4
Bulgaria	38,3	0,1	41,9	9,6	8,8
Czech Republic	50,5	3,7	28,4	13,0	4,4
Estonia	30,1	0,3	51,9	14,9	2,6
Croatia	55,1	0,2	17,6	23,8	3,3
Latvia	37,7	0,9	22,7	12,0	16,8
Lithuania	36,0	1,6	40,2	9,3	12,2
Hungary	28,3	9,5	40,1	8,5	10,7
Poland	47,9	0,3	25,6	15,2	10,2
Romania	35,3	1,3	24,4	6,7	32,1
Slovenia	50,0	0,3	26,2	17,2	4,6
Slovakia	62,3	2,5	8,6	19,5	6,9

Source: Eurostat

Supply of funding

The regulatory environment and capital market development



Source: ECB, World Economic Forum

Supply of funding

Market infrastructure – stock exchange, capitalisation, turnover, listing, IPOs

Country	Stock Exchange				Equities					
	Name	Majority owner	Regional cooperation	Supplier of trading system	Capitalisation	Turnover		Listed companies		IPOs
					EUR million	Total EUR million	Share turnover ratio %	Domestic Number	Foreign Number	Number
Bulgaria*	Bulgarian Stock Exchange (BSE - Sofia)	State	SEE link	Deutsche Boerse (Xetra)	4.417	156	4%	365	0	1
Czech Republic	Prague Stock Exchange (PSE)		CESEEG		-	-				
Estonia	Nasdaq Tallinn	Nasdaq Nordic	Baltic Market	Nasdaq OMX (INET)	1.888	149	8%	15	0	0
Croatia	Zagreb Stock Exchange (ZSE)	Diversified	SEE Link	Nasdaq OMX (OMX X-Stream)	16.834	387	2%	186	0	2
Latvia	Nasdaq Riga	Nasdaq Nordic	Baltic Market	Nasdaq OMX (INET)	1.277	45	4%	26	0	0
Lithuania	Nasdaq Vilnius	Nasdaq Helsinki	Baltic Market	Nasdaq OMX (INET)	3.339	75	2%	29	1	0
Hungary	Budapest Stock Exchange (BSE)	Central bank	-	Deutsche Boerse (Xetra)	16.246	7.005	43%	45	0	0
Poland	Warsaw Stock Exchange (WSE)	State	-	NYSE Euronext	123.659	56.256	45%	838	64	49
Romania	Bucharest Stock Exchange (BVB)	Diversified	-	in-house designed	17.027	1.865	11%	82	2	0
Romania	SIBEX	Takeover by BVB underway	-	Athex Group	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Slovenia	Ljubljana Stock Exchange (LJSE)	Zagreb Stock Exchange	SEE Link	Deutsche Boerse (Xetra)	5.523	340	6%	46	0	0
Slovakia	Bratislava Stock Exchange (BSSE)	State	-	in-house designed	2.119	6	0%	14	0	0

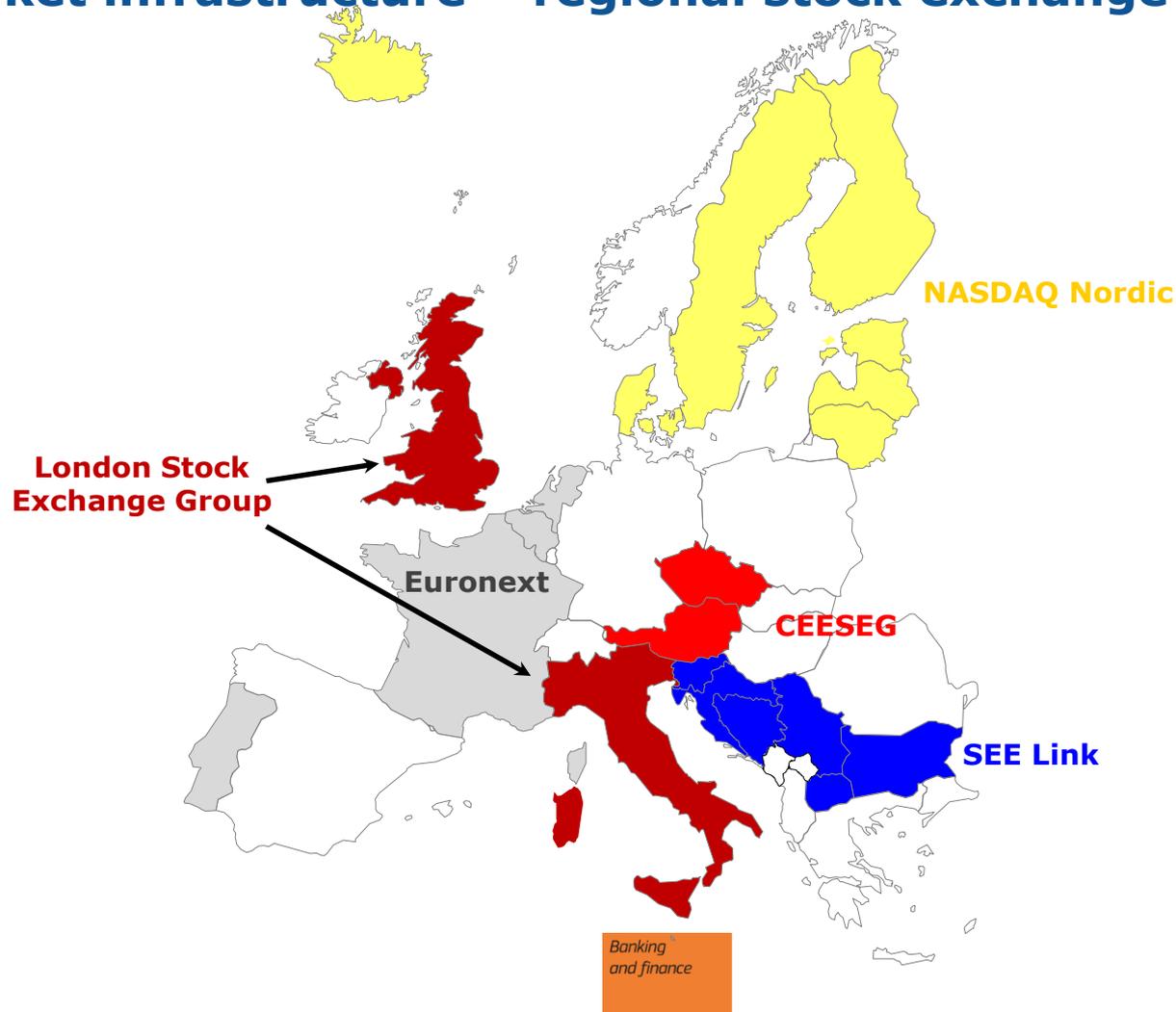
Source: : EBRD (2016) Capital Market Infrastructure. CMI Facts & Figures 2015



European
Commission

Supply of funding

Market infrastructure – regional stock exchange alliances





European
Commission

Supply of funding

Market infrastructure – MTF, CSD, CCP, crowdfunding, rating

Country	Multilateral Trading Facilities (MTF)	Central securities depository (CSD)				Central Clearing Counterparties (CCP) / Clearing Houses	Crowd-funding platforms	Rating agencies
		Owner	Bank licence	Participants Domestic Number	Foreign Number			
Bulgaria		Banks and brokers 49.7%	no	113	1	0	0	BCRA
Czech Republic								
Estonia	First North Estonia	Nasdaq Nordic	no	11	1	0	2	0
Croatia	Zagreb Stock Exchange's MTF	State + FINA	no	56	3	SKDD-CCP Smart Clear [pending regulatory approval]	3	0
Latvia	First North Latvia	Nasdaq Riga	no	17	4	0	0	0
Lithuania	First North Lithuania	Nasdaq Helsinki	no	41	16	0	1	0
Hungary	Beta Market	Central bank	yes	152	16	KELER - 90% owned by CSD; 111 members	3	0
Poland	Newconnect, Catalyst, Bondspot	WSE, NBP, MoF: 33.3% each	no	74	6	KDPW_CCP (owned by CSD). Clearing members: 36 on regulated market, 16 on OTC market.	8	Fitch Polska, EuroRating
Romania	BSE SA	BSE	no	43	8	Bucharest Clearing House - owned by BSE (non operational)	2	0
Romania	Monetary-Financial and Commodities Exchange - Sibiu SA	Sibex	no	8	0	Romanian Clearing House - owned by Sibex (licence withdrawn in 2015, derivatives cleared in Athens)	n.a.	0
Slovenia		Diversified	no	24	1	0	0	0
Slovakia	Bratislava Stock Exchange MTF	BSSE	no	16	4	0	0	European Rating Agency

Outline

II. Relevance of CMU for Central and Eastern Europe

1. The Vienna Initiative
2. Financial markets in CESEE: state of play
3. Policy suggestions

3. Policy suggestions

- ❑ **Priorities for policy action at national level**
- ❑ **Potential for cross-border projects and cooperation**
- ❑ **Policy issues at EU level**

➔ Technical assistance by the Structural Reform Support Service

Priorities for policy action at national level (I)

National strategy and promotion

- ✓ Development of capital markets strategies; country-specific initiatives:
 - ✓ Adopted capital market strategies – BG, HU, LV
 - ✓ Strategies in preparation – CZ, EE, PL (financed by SRSS); LT, MK

✓ **Business environment**

- ✓ Stable legal framework and judicial system
- ✓ Efficient administration
- ✓ Predictable taxation environment for capital markets; favourable tax treatment, less burdensome tax procedures
- ✓ Country-specific proposals for improving the taxation regime:
 - ✓ Possibility to introduce an Investment Savings Account - LV
 - ✓ Common standards for dividend/coupon payments, tax reclaims linked to such payments, rights issues and tender offers - CZ
 - ✓ Reducing taxes for listed SMEs - PL

Priorities for policy action at national level (II)

Public support to companies to access capital markets

- ✓ Use of public funds (i.e. EU funds/national state budget) to support the listing of SMEs and their access to finance; country-specific initiatives (already implemented and proposed):
 - ✓ 4 Stock: facilitating the access of SMEs to capital markets – PL (Warsaw Stock Exchange and Polish Agency for Enterprise Development)
 - ✓ ELITE programme: different forms of financing to companies, which prepare for IPOs – HU (Budapest Stock Exchange and London Stock Exchange)
 - ✓ Promotion and expansion of access to finance of SMEs through issuances of securities - LV
 - ✓ Public support for setting up private equity and venture capital funds - LV
 - ✓ Financing of analytical reports on SMEs in line with the needs of institutional investors - PL

Privatization

- ✓ Encourage privatization (even partial privatization of SOEs) through IPOs

Priorities for policy action at national level (III)

Institutional investors

- ✓ Expand the base of institutional investors on local capital markets
- ✓ Country specific initiatives regarding institutional investors:
 - ✓ Project (financed by SRSS) to create new financial instruments and a more favourable environment for institutional investors - LT

Financial education

- ✓ Strengthening of financial education, in particular the financial literacy of retail investors and SMEs
- ✓ Country specific initiatives (already adopted and proposed):
 - ✓ National strategies for financial education – HU, HR, LT, LV
 - ✓ Financial education of retail investors, potential issuers (in particular SMEs) and financial market analysts – CZ
 - ✓ Information campaigns (planned) targeting the holders of dormant accounts to re-activate their assets - SK

Priorities for policy action at national level (IV)

Supervisory framework

- ✓ Strengthening of risk-based supervision; country-specific initiatives on enhancing risk-based supervision:
 - ✓ ASF project on capital markets supervision (financed by SRSS) - RO
- ✓ Strengthening of supervisory capacity of regulators including through hiring of specialised/experienced staff
- ✓ Twinning projects among supervisors
- ✓ Secondment of supervisors to regulated institutions
- ✓ Training at EIOPA and ESMA

Potential for cross-border projects and cooperation (I)

Regional alliances of stock exchanges

- ✓ Strengthening of existing regional alliances (Nasdaq Baltic Market, CEESEG, SEE Link) through further geographical expansion and deeper integration; setting up other strategic alliances

Foreign listing and market access

- ✓ Create opportunities for domestic issuers and investors to access foreign markets through the local stock exchange: setting up by the national stock exchanges of new markets dedicated to foreign trading
- ✓ Country-specific initiatives:
 - ✓ BSE International: Project for the creation of a new regulated market segment for financial instruments with EU - compliant prospectuses and setting up of a Multilateral Trading Facility for all other instruments - BG (Bulgarian Stock Exchange)

Potential for cross-border projects and cooperation (II)

Central Securities Depositories (CSDs)

- ✓ Facilitate the settlement procedures within the regional alliances of stock exchanges; proposals for improvement:
 - ✓ SEE Link Project (supported by the EBRD) to facilitate the settlement procedures among the participating stock exchanges
- ✓ Setting up of CSD links with EU-based CSDs to facilitate cross-border trading, clearing and settlement

Central Clearing Counterparties (CCPs)

- ✓ Explore the possibilities for joining existing CCPs—due to the high cost and complexity of setting up national CCPs
- ✓ Existing EMIR compliant CCPs in the region, which could expand their services cross-border: KDPW_CCP (PL), Keler (HU); CCP pending recognition of compliance by ESMA: SKDD-CCP Smart Clear (HR)

Potential for cross-border projects and cooperation (III)

Creating regional markets through harmonization of legislation

- ✓ Need to harmonize legislation at regional level in several areas, for instance, covered bonds (similar to the coordination of rules for covered bonds in the Baltic countries), financial instruments

Policy issues at EU level (I)

Concerns related to the proportionality of EU law:

- ✓ Particular attention should be paid to "small jurisdictions" according to the state of development of capital markets; proposal for a definition based on technical criteria based on advice by ESMA and EBA - AT
- ✓ The specific case of MREL eligible liabilities allow parent banks to buy MREL bonds issued by subsidiaries under MPE resolution strategy - AT
- ✓ Current legislation should be reviewed and introduce different levels of sanctions and requirements according to the size of entities operating on capital markets - CZ

Policy issues at EU level (II)

Concerns related to the proportionality of EU law:

- ✓ Examples of requirements which are burdensome for smaller markets:
 - ✓ High remuneration requirements imposed by the UCITS5 Directive on small companies, which only offer non-complex products – HR
 - ✓ High level of sanctions for small issuers/players (Transparency Directive and MIFID 2) – HR and HU
 - ✓ High level of penalties (in particular, for small companies) for disclosing insider information - PL

Implementation of EU legislation

- ✓ TA for the implementation of EU legislation could be provided by the EU (SRSS); TA should have a practical dimension and should be tailored to the needs of recipient countries

Policy issues at EU level (III)

Harmonization of legislation at EU level

- ✓ Areas of further legislative harmonization at EU level suggested by participants:
 - ✓ Corporate, insolvency and securities law - CZ
 - ✓ Crowdfunding - LT
 - ✓ FinTech - CZ, LT
 - ✓ Taxation - SK

EU financial support instruments

- ✓ Use of EU/IFIs financial instruments to support the development of capital markets in the region
- ✓ Planned/proposed initiatives:
 - ✓ Setting up of a fund financed by European Structural and Investment Funds (ESIF), which will provide funding to SMEs – SK
 - ✓ Setting up of national/supra-national funds financed by ESIF, European Fund for Strategic Investment (EFSI) or EIB to mobilize additional capital in Europe – SK
 - ✓ IFIs support for capital market development through venture capital investment, securitization, project bonds - AT

Technical assistance by the Structural Reform Support Service (I)

- The Structural Reform Support Service (SRSS) of the European Commission provides technical support to Member States, including within the area of capital markets development under the Capital Markets Union initiative.
- The SRSS has closely followed the work of the Group and stands ready to assist Member States, upon their request, with country-specific technical support to address recommendations stemming from this report



SRSS projects (II)

Country	Title	start	Country	Title	start
BG	Development of a single entry point for disclosure and distribution of information by [capital] market participants ('single entry point')	4Q2017	IT	Italian Capital Markets and the Capital Markets Union – Access to Finance	3Q2017
CY	Supporting the New Framework for Insolvency Practitioners	3Q2017	LT	Improvement of investment environment for institutional investors	3Q2017
CZ	National Strategy on the Development of Czech Capital Market	3Q2017	LT	Addressing corporate insolvency reform in LT	3Q2017
CZ	Analysis and promotion of business angels in the Czech Republic	3Q2017	LV	Legal and Regulatory Framework for Creation of Structured Products	3Q2017
CZ	Developing a Communication Strategy on Financial Literacy (Previously: Educational video series on capital markets)	4Q2017	LV	Preparation of SME Equity Support Instrument	3Q2017
EE	Capital Market Diagnostic	3Q2017	LV	Achieving Emerging Market Status	3Q2017
EE	Legal and Regulatory Covered Bond and Securitisation framework reform to be provided by EBRD LC2 Team	3Q2017	MT	Export Credit Guarantees	3Q2017
EE	Opening Estonian Regulatory Framework for Innovative Technical Solutions	1Q2018	MT	National Strategy for Electronic Payments	4Q2017
EL	Decoding the European legislation on cooperation guidelines of the Member States on private debt issues	4Q2017	PL	Strategy for capital market development	3Q2017
EL	Study and preparation of Request for Proposal (tender documents) for the development of the information system of the Independent Credit Authority.	3Q2017	PL	Strengthening institutional and administrative capacities of the KNF to address the new supervisory tasks resulting from the implementation of the European Union law	4Q2017
EL	Electronic and online indebtedness management tools	3Q2017	RO	Setting up of National Promotional Bank of Romania	4Q2017
EL	Fund for Entrepreneurship and Development	3Q2017	RO	Consolidating risk based supervision across all sectors	3Q2017
EL	Supporting the New Framework for Insolvency Administrators	3Q2017	SI	Effective modelling of non-maturing deposits to manage liquidity and interest rate risk	1Q2018
HR	Integration and improvement of Risk Based Supervision in Croatian Financial Services Supervisory Agency (HANFA)	4Q2017	SI	Request for Technical Assistance with regards to preparation of case study for building a new cash centre in Slovenia	4Q2017
HR	Support for bankruptcy Law	3Q2017	SI	Organizational effectiveness of financial sector regulator – Value added benchmarking	4Q2017
HR	Operationalization of resolution tool- SPV asset management	3Q2017			
HR	Reclassification of DGS as financial auxiliaries	3Q2017			

Outline

- I. Background and context**
- II. Relevance of CMU for Central and Eastern Europe**
- III. Securitisation**
- IV. Concluding remarks**

Outline

III. Securitisation

1. In general

2. Sovereign Bond-Backed Securities

Securitisation framework

- The securitisation framework is one of the **main elements of the CMU to develop a fully functioning capital markets union by the end of 2019**
- Developing a securitisation market will help **create new investment possibilities and provide an additional source of finance**, particularly for SMEs and start-ups
- Commission proposal – September 2015; Council approval – November 2017
- Securitisation package includes:
 - (i) A regulation **setting rules on securitisation and establishing criteria to define STS securitisation**
 - (ii) A regulation **amending the Capital Requirements Regulation**

Securitisation package (I)

Common rules for all securitisations

- **Due diligence requirements for investors:** investors should verify origination practices; assess the risk characteristics and structural features of the transaction; establish written procedures to comply with due diligence requirements
- **Risk retention requirements:** skin in the game (5% net economic interest); safeguards included in the regulation so that requirements for risk retention cannot be circumvented
- **Transparency requirements:** Originators, sponsors, securitisation special purpose entities (SSPEs) must make available to holders of a securitisation position, competent

Securitisation package (II)

competent authorities and, upon request, to potential investors, certain information on the transaction and underlying exposures

- **Supervision:** provisions related to **powers of the competent authorities** when involved parties are regulated or not under the EU financial services legislation; **notification duties** and cooperation between competent authorities in the case of cross-border transactions
- **Sanctions:** Member States shall **impose administrative sanctions** for the breach of the regulation by the involved parties; penalties may reach EUR 5 million for natural persons and 10% of total annual turnover for legal entities



European
Commission



Source: AFME

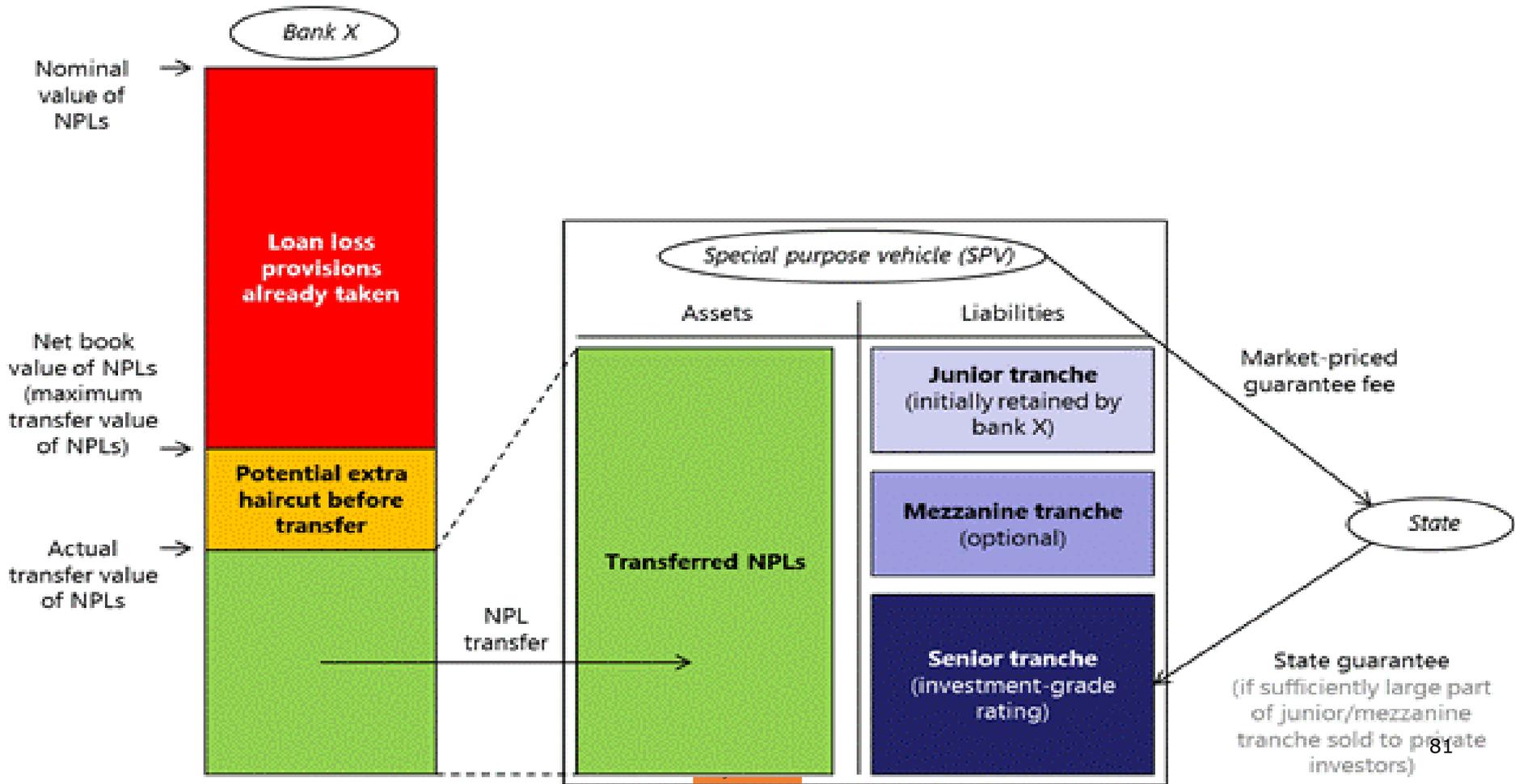
Framework for simple, transparent, standardised (STS) securitisation

Simplicity	Transparency	Standardisation
<ul style="list-style-type: none"> ✓ Homogenous asset type ✓ No defaulted exposures ✓ No re-securitisation ✓ Cash flow not substantially dependent on sale of asset ✓ At least one payment made 	<ul style="list-style-type: none"> ✓ Historical default and loss performance data ✓ Sample of exposure verified independently ✓ Liability cash flow model linked to exposure ✓ Originator and sponsor responsible for transparency 	<ul style="list-style-type: none"> ✓ Risk retention satisfied by originator, sponsor original lender ✓ Interest and currency risk mitigated ✓ Predefined remedies or actions in case of delinquency or default of debtors or conflicts of investors



European
Commission

Example of a NPL securitisation – Italian scheme



Outline

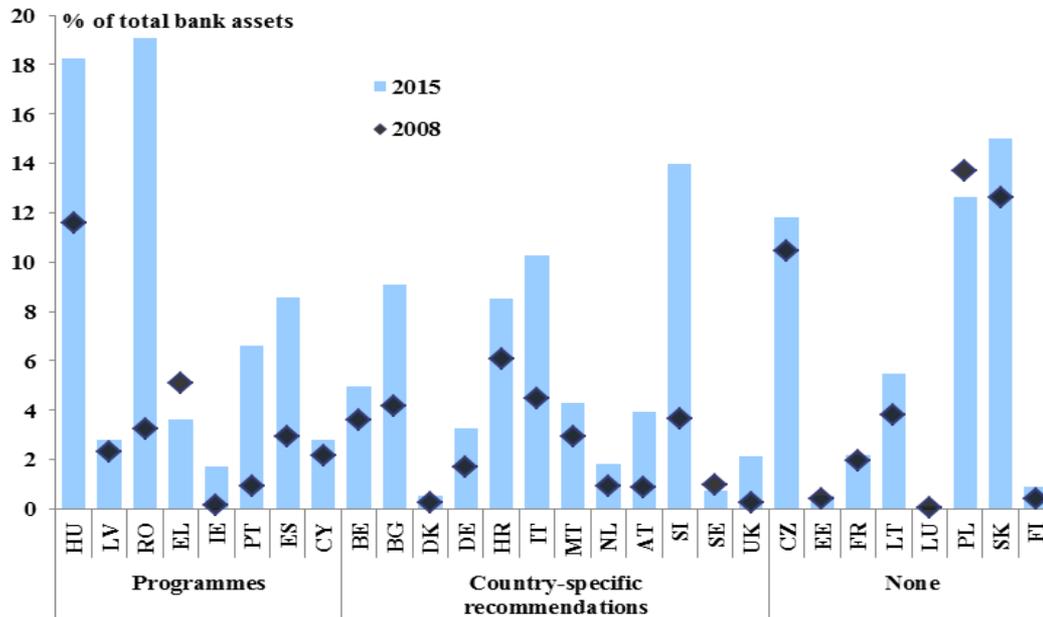
III. Securitisation

1. In general

2. Sovereign Bond-Backed Securities

SBBS - context

The sovereign/bank nexus



Source: [Report by the Commission \(Coping with the international financial crisis\)](#)

- Home bias, bank/sovereign loop
- This can hinder the good functioning of Banking Union. SBBS can help addressing this
- Original idea (ESBies) from academics (Brunnermeier et al., circa 2010-11)

- ESRB High-Level Task Force established in mid-2016, extensive Commission analysis, outreach to market participants

SBBS - basic concept

- Pooling (→ diversification)
 - Tranching (→ seniority)
 - No mutualisation
- } "Safe" asset

*Could be arranged
by any qualified
institution: private
or public!*

*Pooling ⇒
diversification*

Portfolio of (central euro area) government bonds (e.g. ECB capital key weights)	Senior (calibrated for low risk)
	(Mezzanine)
	Junior

*Tranching
⇒ seniority*

Key findings of ESRB Task Force: effect of current regulation

- **SBBS would be treated as securitisation and consequently, current regulation hinders emergence of SBBS.**
- **However, SBBS do not pose the securitisation-specific issues (no asymmetry of information, no transformation of illiquid assets, but attributing risks in non-linear manner)**

An enabling framework is needed: *Proposal of 24 May 2018 (COM(2018) 339 final) for a Regulation of the European Parliament and of the Council on sovereign bond-backed securities*

SBBS eligibility criteria

- **Fixed portfolio of euro area sovereign bonds (based on ECB capital key, with narrow margins)**
- **At least two tranches: senior (70%), sub-senior (30%)**
- **Procedures to modify, in specific exceptional circumstances, for future issuances**
 - **underlying portfolio, and**
 - **size of senior tranche**
- **SPE "bankruptcy remote"**

SBBS compliance framework

- **Modelled on setup for Simple, Transparent and Standardised (STS) securitisations (ex-ante self-certification, supervision by competent authorities, sanctions if infractions are detected)**

SBBS Regulatory treatment

- **Modifications to sectoral legislation to align treatment for SBBS to that of EU/euro area sovereign bonds (UCITS Directive, CRR, IORP II Directive, Solvency II Directive)**
- **Some adjustments to come via level-2 changes (e.g. LCR)**

Outline

- I. Background and context**
- II. Relevance of CMU for Central and Eastern Europe**
- III. Securitisation**
- IV. Concluding remarks**

Concluding remarks (I)

- **The CMU Action Plan has delivered already several concrete results and more initiatives are in the pipeline**
- **The Vienna Initiative provides an interesting public-private forum to exchange information and discuss policy challenges in the financial sector in Central East and South East Europe**
- **The Report of the Working Group shared best practices and suggested policy action to take at national, cross-border and EU level in order to develop local capital markets**
- **At EU level, on one hand, proportionality of regulation is a main concern for small capital market development. On the other hand, due attention has to be paid to macro-financial stability and consumer protection**

Concluding remarks (II)

- **The Commission is preparing a Communication based on the Vienna Initiative report**
- **With respect to securitisation, the new rules are expected to bring an increased degree of certainty and help further develop this market; a challenge going forward will be the development of implementing measures (technical standards and guidelines) required in order to implement this new regime**
- **On Sovereign Bond-Backed Securities (SBBS), the Commission has launched a Regulation for an enabling framework without any procedure for mutualisation by public authorities. The jury is out as it has to be picked up by the private sector**