FESE strategy paper on the Savings and Investments Union

Brussels, 27th February 2025

The EU must leverage its capital markets and promote a market-driven financing system to boost long-term competitiveness and growth. The European Savings and Investments Union (SIU) should serve as a catalyst, advancing a new vision for the Capital Markets Union (CMU) that empowers EU businesses and citizens.

The SIU's success will depend on progress in three interconnected pillars of EU capital markets: the supply side, the demand side, and market structure. Tackling challenges and seizing opportunities in these areas will require strong, coordinated action from policymakers at both the EU and Member State levels.

Following the release of FESE's manifesto, "C.H.E.C.K-list to Getting European Capital Markets in Motion" (available here), this paper aims to provide further market insights and recommendations for a future roadmap.

FESE policy recommendations

1. Boost an attractive listing ecosystem

- Enhance pre-IPO financing frameworks. For instance, the EIF could be provided with increased liquidity and an expanded mandate to facilitate public listings.
- Consider initiatives to foster regulatory alignment in areas such as dual listing, listing requirements, or a European prospectus.
- Simplify regulatory requirements. In particular, it is essential to enhance the attractiveness and accessibility of SME Growth Markets.

2. Stimulate investment and expand capital pools

- Reform national pension systems to adopt market-based pension funds as a standard practice.
- Offer straightforward cross-border investment and savings products for retail investors, such as an updated PEPP or a product similar to Sweden's Investment Savings Account.
- Increase efforts to enhance the financial literacy of EU citizens.
- Review prudential ratios under Solvency II and Basel II and adopt a more flexible approach to investments in UCITS and equity infrastructure.

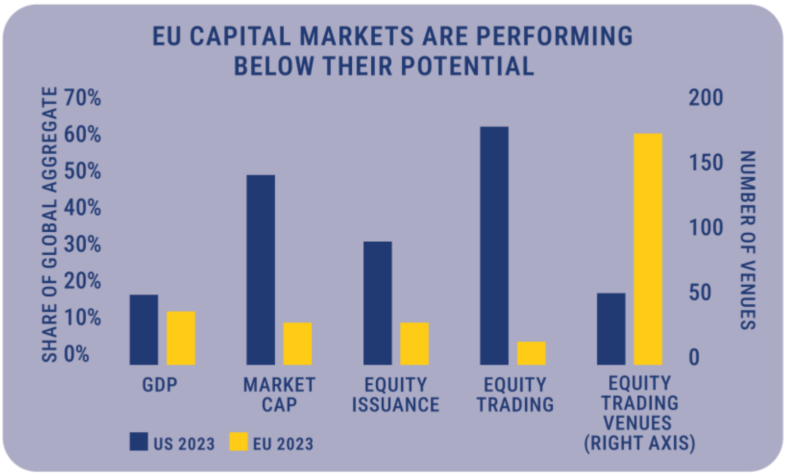
3. Tackle liquidity fragmentation and fostering transparency in EU markets

- Promptly reevaluate the current regulatory framework (e.g. MiFID II/R) to identify what needs to be improved for deepening and increasing liquidity.
- Strengthen and harmonise the authorisation, supervision and enforcement regime for SIs, and resolve data quality issues arising from OTC and SI trading.

1. Boost an attractive EU listing ecosystem

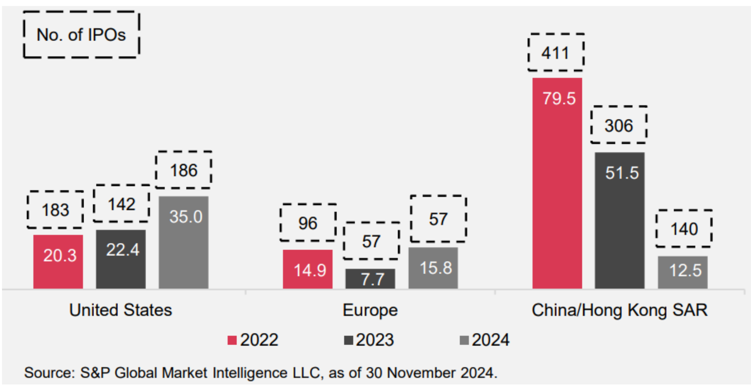
- To enhance its competitiveness in the global economy and sustain ongoing economic growth, the EU must unlock the full potential of its capital markets and cultivate a more market-driven financing system, along with deeper and more resilient European capital pools. Therefore, the EU and its Member States need to work together with a commitment to deliver concrete change and address the challenges hindering the success of EU capital markets.

Fig. 1 Comparison of capital market statistics in the EU and US[1]



- The international competitiveness of EU capital markets is intrinsically tied to the robustness and appeal of their primary markets, where new securities are issued for the first time. Primary markets are vital for enabling businesses to raise capital for expansion, innovation, and job creation. However, the weak Initial public offering (IPO) figures point to the declining perceived attractiveness of the EU's listing ecosystem. The observed structural trend of European companies listing abroad in more favourable jurisdictions, particularly the US, clearly illustrates the challenge. Its deeper and broader capital pools, higher potential valuations, and more integrated listing and trading ecosystem make it an attractive alternative, while the EU continues to lose its 'champions' and promising scale-ups.[2]

Fig. 2 IPO proceeds (USD bn) and volumes (2022 to 2024)[3]



[1] FESE, May 2024, Check list 2030 – Getting European Capital Markets in motion, available here. // Data obtained from IMF, 2024; World Bank, 2023; SIFMA, 2023; ESMA, 2023; WFE, 2023; and FESE, 2023.

[2] European Start-Ups associations and European exchanges, including FESE, published a letter in September 2024 titled "Europe needs to keep its best Tech IPOs at Home" (available here), where we also outline some key recommendations in this regard.

[3] S&P, December 2024, Global IPO Watch 2024, available here.

- To realise the aspiration of developing a vibrant capital market ecosystem that can rival their global counterparts, it is essential to strengthen the investment in the early stages of the EU stock market lifecycle. The European IPO market needs to get boosted with deeper pockets at the pre-IPO stage, especially in terms of European venture capital, to create a vibrant European tech and SME/startup ecosystem preparing for successful European IPOs.
- It is encouraging that the Eurogroup recognised the need to explore effective ways to catalyse and leverage private capital at both national and European levels, including through the involvement of the EIB.[4] FESE believes that the EIB can play a key role in supporting strategic sectors via private-public partnerships and an exit fund to facilitate public listings.
- Both the industry and policymakers should explore additional regulatory initiatives to support primary markets, especially from a cross-border perspective and in terms of regulatory alignment. Possible actions could include an analysis of the appropriateness of streamlining the process for dual listing, further harmonising listing requirements, and introducing one European prospectus to facilitate harmonised access without additional requirements in all EU countries.
- The definitions of SMEs are also restrictive and outdated. Amending these definitions would enable more companies to benefit from the advantages of SME reliefs and SME Growth Markets, reducing regulatory burdens and making public capital markets a more attractive growth option for them.
- For example, the US Securities Act offers newly listed growth companies reduced disclosure requirements and lower internal control obligations for the first five years after the IPO. The EU could consider these developments when formulating its strategy to support growth companies. Early-stage growth companies do not always have sufficient resources to meet all transparency and compliance regulations, and should instead be able to allocate their resources towards growth.
- SME Growth Markets serve as a key gateway for SMEs into the realm of capital markets, and these markets should be enhanced by streamlined requirements to make them more attractive and accessible. Local markets can offer more suitable opportunities for SMEs, as their proximity to local stakeholders often plays a crucial role. Besides, this connection can lead to better access to local retail investors and contribute positively to the local economy.
- Finally, the EU needs to boost its attractiveness for businesses by simplifying and streamlining regulatory requirements and make them consistent across Member States to create a more predictable business environment.

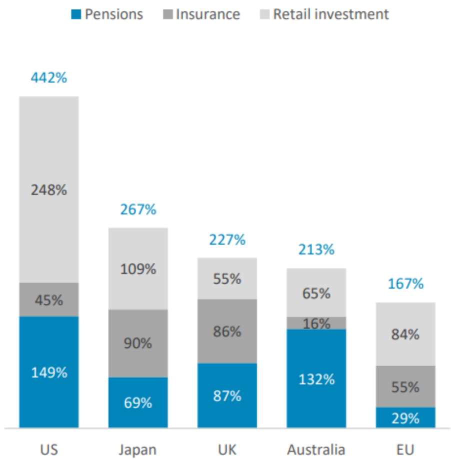
2. Stimulate investment and expand capital pools

- As part of a comprehensive EU strategy to improve competitiveness, the implementation of demand-side measures that mobilise private savings will be crucial. Expanding European long-term capital pools and channelling them into capital markets will inherently increase the depth, liquidity, and size of EU capital markets.
- European households allocate, on average, 32% of their financial assets to cash and deposits, compared to just 12% for US households. Meanwhile, US households invest nearly 50% of their savings in equities and investment funds, while European households

[4] Eurogroup, November 2024, Competitiveness of the European economy - statement of the Eurogroup in inclusive format, available here.

invest only around 30%.[5] In absolute terms, EU household cash and deposits amount to approximately €11 trillion[6], often generating inadequate returns for their holders.

Fig. 3 The size of pools of long-term capital[7]



Source: New Financial analysis of data from EIOPA, Eurostat, FSB, IMF, OECD, GPIF, and the US Treasury

- Encouraging citizens to invest in capital markets requires measures to mobilise retail investors and redirect their savings from banks to more productive capital markets, offering better returns and enabling wealth creation. As highlighted by the Eurogroup in April 2024, introducing simple, effective cross-border investment and savings products for retail investors should be a key action item.
  - For instance, citizens should have a reasonable choice of products that they can hold in an eligible account, possibly paired with targeted tax incentives. The Swedish Investment Savings Account is a notable success story which has facilitated retail investors to invest directly in shares and funds (including ETFs).
  - An upgraded Pan-European Personal Pension Product (PEPP) could also play a pivotal role by making a few, easy-to-understand and low-cost financial products, widely available cross-borders.
- Pension systems are also fundamental in building deep, long-term capital pools. The Commission can contribute by working to streamline a common policy direction for future pension systems. In our view, Member States should explore transitioning from traditional pay-as-you-go models to (partly) funded systems and promoting market-based pension fund enrolment as a standard practice. Additionally, targeted measures could provide incentives for higher investments in Occupational pension schemes (IORPs) and encouraging their use and competitive provision cross-border.
- Member States must also increase efforts to improve financial literacy across the EU (e.g. school education). Ultimately, a well-informed investor is more likely to achieve financial stability and growth, contributing to a healthier and more resilient financial ecosystem.

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[5] A. Thomadakis, et al., CEPS, October 2024, What must be prioritised for the financial sector over the next five years, available here.

[6] Eurostat, 2022

[7] New Financial, September 2024, Searching for growth: the future of EU capital markets, available here. // The size of pools of long-term capital in % of GDP in the three years to 2023 in the EU and selected comparator markets, with the number in blue showing total size. Retail investment includes direct household investments in funds, shares, bonds, and other financial investments.

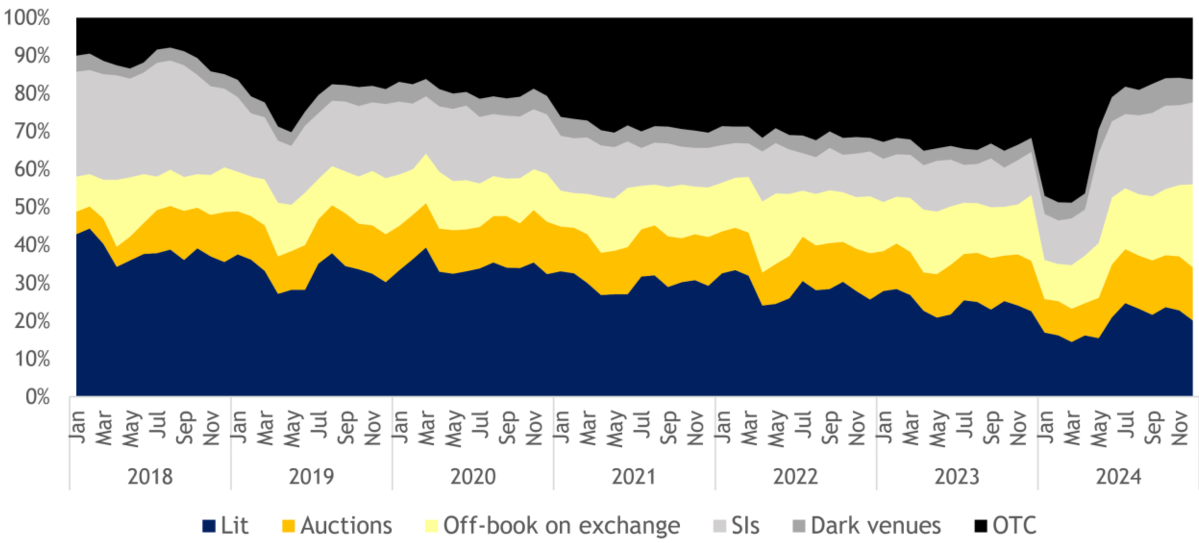
- Finally, an additional review of the prudential ratios in Solvency II and Basel II should be undertaken to further rebalance institutional investors' portfolios to increase investment in equities. In addition, a more flexible approach to the investment limits in UCITS could also enhance market liquidity and the attractiveness of EU markets.

3. Tackle liquidity fragmentation and fostering transparency in EU markets

3.1. Liquidity challenges in lit venues due to market fragmentation

- The European market structure reflects both primary and secondary markets, where securities are sold by and transferred from one investor to another. These markets share a symbiotic relationship, and their efficient functioning is essential for capital formation, liquidity provision, and risk management — key factors for an attractive business and listing environment. Therefore, attention must be given to improving the depth of liquidity pools in lit venues, where companies list and the price formation takes place. A focus on increasing liquidity will support both issuers in their quest for growth, capital, and investments, as well as investors in their access and exit strategies.
- MiFID II enabled the proliferation of alternative trading mechanisms, predominantly Systematic Internalisers (SIs) and dark pools, which together with persistent over-the-counter (OTC) trading practices, have led to an increased fragmentation of the EU equity market since 2018. While these developments have fostered competition, they have also diverted liquidity away from lit regulated markets, often with little to no transparency. Sufficient transparency, however, is crucial for the price formation process and, therefore, the well-functioning of capital markets.

Fig. 4 Evolution of European equity turnover by execution method [8]



- For example, the share of lit multilateral venues has fallen to only 40% of equity trading turnover in the EU, compared to 60% in the US (BMLL, July 2024). For FESE, a key question is how the EU can truly attract more investment into a market where only 40% of liquidity is visible to all investors. If this approach persists, accessible and visible liquidity will continue to shrink, in a clear threat to the Capital Market Union.

[8] BigXyt data on EEA shares of Stoxx 600 trading activity on EEA, UK and CH venues (2024). The graph shows both addressable and non-addressable liquidity. // The decrease in OTC trading from May 2024 is largely attributed to the UK FCA's abolition of reporting requirements for non-addressable liquidity.

- A well-functioning price formation process enables trading to take place, delivers more efficient markets, where all investors, regulators and participants can have full confidence, and also lowers capital costs for businesses. As liquidity shifts away from lit venues, the price formation process is weakened[9]. Off-exchange venues serve a critical function in capital markets, but even they rely on reference prices and make use of them from lit markets.
- The past policy debate focused on increasing the visibility of fragmented markets through the introduction of the Consolidated Tape. While useful for providing a consolidated view of market transactions, the tape cannot address what is truly needed: a market with sufficient liquidity and price formation to support investment decisions. The challenges facing European markets are deeper, stemming from underlying structural and regulatory problems that need to be addressed directly.

3.2. Transparency and oversight in the off-exchange space

- The challenge of reducing market fragmentation and fostering deeper liquidity pools lies in effectively implementing the original objectives of MiFID II/MiFIR: increasing transparency and shifting a larger share of trading flow into lit venues.
- For example, while the recently reviewed MIFID II text acknowledged the very low pre-trade transparency of SIs and the need for a level playing field between trading venues and SIs, ESMA's recent RTS 1 proposals fell short of providing effective solutions. SIs are trading in small sizes, contrary to their original purpose of facilitating large institutional orders (LIS). For instance, in 2024, 94% of total EEA SI trades in Stoxx600 components fell below the standard market size (SMS) with an average trade size of €1,500, while only 0.5% exceeded the LIS with an average trade size of €1,512,500 (BigXyt).
- Moreover, the quality of data from OTC and SI trading remains deficient due to fragmentation and exemptions from the transparency and reporting regime. Data quality, consistency and availability at the source have to be improved as a matter of priority. Strengthening and harmonising the authorisation, supervision and enforcement frameworks for SIs is also critical. This includes addressing their operational frameworks, quoting obligations, and execution practices.

[9] The Spanish regulator (CNMV) published a study in December 2024 (available here) which concludes by suggesting that it may be appropriate to initiate a debate on whether the objectives of MiFID regulation are being achieved and whether additional objectives should be considered. The study highlights that there does not appear to be a significant shift from OTC trading to on-exchange trading and raises the question of whether lit trading should be prioritised due to its central role in the price formation process.

ABOUT FESE

The Federation of European Securities Exchanges (FESE) is the unique voice of European exchanges, advocating for fair, transparent and efficient capital markets to support growth and prosperity in Europe. We are committed to financing the economy, ensuring financial stability, and fostering sustainable development.

FESE represents 17 full Members and 1 affiliate Member from 32 countries. Exchanges operate both transparent regulated markets for securities and exchange-traded derivatives, and specialised SME growth markets that allow small and medium-sized companies to access public capital markets.

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