Leaders Live Conference-Colloquium
General Council of Economists of Spain

RODRIGO BUENAVENTURA, THE CNMV CHAIRMAN
28 April 2021

Good morning.
Thank you, Valentín, for your kind words.

It gives me great satisfaction, as an economist, to be able to participate in this event. The Council and the colleges are doing a fundamental job of stimulating economic debate and the exchange of ideas, which are so necessary in such turbulent times as these, economically speaking. As someone who began studying economics almost 35 years ago, I am proud to be able to address you in this series of colloquia.

Today I would like to focus on the role of stock markets in financing our companies. In this long year of pandemic, we have faced one of the most intense global financial crises, which has affected all developed and non-developed countries, to a greater or lesser extent. But unlike after 2008, the stock markets have so far responded adequately in this crisis.

Firstly, it should be noted that markets have continued to form prices and provide liquidity even at the most stressful times. At no time, not even in mid-March 2020, did they lose their depth or become locked in.

Secondly, markets infrastructures, and especially clearing and settlement infrastructures, showed great resilience. The former supported a number of orders and trades per unit of time that far exceeded the historical peaks observed. The latter withstood, without major incidents, percentages of price fluctuations that had never been observed since modern records have been kept.

And what this fact tells us is, fundamentally, that the regulations that the European Union adopted in the 2011-2016 period, such as the EMIR or CSDR regulations or the MIFID directive, were right to design the infrastructure protection mechanisms for future crises. We economists (and jurists) rightly say that we never regulate to deal with the next crisis, but to react to the last one. While that is also true in this case, it is no less true that the precautions we introduced then have helped to ensure that in this crisis the infrastructure and the negotiation remained unscathed.

At a more macro level, Europe has a fundamental weakness in its capital markets: they are thin and weak compared with the size of its economy. Although throughout 2020 the stock markets have responded both at Spanish and global level, we continue to have a small stock market compared with other economic areas.

European companies are financed much more with bank debt than with equity or fixed income issued in capital markets. The proportion of bank loans in non-financial companies in the euro area is close to 30% of companies' total liabilities, a much higher percentage than in US companies, where it is only 8-10%. European companies' recourse to the capital markets in the form of listed shares is also lower, accounting for around 15%, while the figure for US companies is double that of their EU counterparts.

This, as is well known, has important consequences when the banking sector, for one reason or another, is forced to restrict the supply of credit or becomes more risk-averse. They may be regulatory, market or extraordinary causes. The fact is that when banks tighten access to credit, European companies suffer the impact almost immediately and this affects production and employment.

But, in addition to the sensitivity to the situation in the financial sector, the relative "rickets" in European capital markets has two other negative consequences. Firstly, it hinders investment and the growth of our companies, which suffer from a lack of size and critical mass, which in turn makes them more fragile in the face of future adverse shocks. Secondly, it prevents the business discipline and maturity factor imposed by the market (even if this is shared with venture capital) from inducing a greater professionalisation of company management.

The European Union is determined to increase capital market financing for our companies and the CNMV could not agree more with this objective.

Insofar as we are among economists and our domain is figures, let me give you some that point out, in my opinion, these differences very well:

1. If we focus on equity issuance, Europe issued slightly less than half of the US issuance in 2020, $200.4 billion compared with $448 billion in the US, and less than China, with $281 billion of issuance.

2. If we change our focus and look at the fixed income market, we reach similar conclusions. Europe issued almost $3.5 trillion in 2020 compared with $7.3 trillion in the US market. The public sector continues to be the major paper issuer, given the situation.

As can be clearly seen, the European market is less developed than the American one.

3. In the case of the Spanish market, last year closed with issues with a nominal value of €132 billion - mainly focused on bonds, securitisations and promissory notes - which represented an increase of 46% compared with 2019.

4. In terms of equity fundraising, in Spain 2020 saw 38 new issues, all of which were concentrated in capital increases, for an effective amount of €10.853 billion, up 10% on the figures for 2019.

Both figures indicate that the market has continued to provide capital and funding to listed companies, even in the year of the pandemic.

All the above figures show the reality of our market and the reality of European markets. However, our market does have a unique feature compared to other European markets, and that is the degree of participation of retail investors. In this regard, the percentage of direct equity holdings of Spanish households has traditionally been 25% higher than the Eurozone average (average figures in terms of proportion of GDP and average between 2016 and 2019). Spain is a country where the tradition of direct investment in the stock market has historically been maintained. This is probably due to the reduced weight of institutional investment in pensions funds or insurance, unlike other of our neighbouring countries.

The CNMV, in line with the rest of the European supervisors, believes that the securities markets must be one of the levers that will enable the recovery of the economic situation to be boosted. This is one of the four objectives of the European authorities through the promotion of the so-called Capital Markets Union (CMU), whose plan was updated by the European Commission in September 2020:

Firstly, the economic recovery itself. This cannot be built exclusively on the basis of traditional and predominantly bank financing, which is why the European stock markets must be an essential element in obtaining funds for companies, especially SMEs, to supplement the public effort to alleviate the current situation.

As a second objective, it aims to facilitate the green and digital transition by making stock markets the essential means of channelling private investment in both areas.

As a third objective, the CMU seeks to create a more inclusive and resilient economy and society, addressing the challenges posed by Europe's ageing population.

And as a fourth and final objective, the CMU aims to enable and promote the competitiveness of our companies and a strategic autonomy of the European Union. To this end, it seeks to increase the presence of more local companies with innovative business models who can be attractive to global investors, obtaining the financing that will allow them to accelerate their growth.

The question that arises after the above reflections is the following. **What can we do from the perspective of supervisory and regulatory institutions to make securities markets more attractive?**

In my view, there are four possible answers:

1. Reduce, very cautiously, the requirements for accessing the market;
2. Explore formulas to facilitate IPOs;
3. Encourage companies to raise equity;
4. Stimulate financial investment as opposed to real estate or bank deposits.

As for the cost of appealing to the market and its requirements, we should not delude ourselves: a substantial reduction in the information that companies must produce when listing or while listing will end up negatively affecting either market efficiency or in terms of investor protection. There should be no shortcuts in this matter. Any reduction must be done with extreme caution, almost surgically, avoiding simplistic approaches.

There is also a need to reflect on the risk of business failure and how that affects the way investors are informed. If we want stock markets, we must accept that from time to time companies fail, for multiple reasons. Sometimes there is a tendency to think, a posteriori, that these cases must necessarily involve some criminal culpability unrelated to the course of the business. Sometimes this may be the case, due to fraud or accounting misrepresentation, but most of the time there is no criminal cause, at least in developed markets.

Caution regarding potential civil or criminal liability complicates the streamlining of the information that issuers must disclose, and investors must receive. The best information to protect the investor is not that which includes a catalogue of horrors of what hypothetically can go wrong in a business in the future, thinking about avoiding possible civil or criminal liabilities, but that which clearly and specifically explains the relevant risks for that particular issuer, in that particular sector and at that particular time. ESMA and the CNMV are insisting on this aspect when reviewing prospectuses under the new Prospectus Regulation.

As a second answer to the previous question and to increase the attractiveness of the stock markets, I think we should be imaginative and look at ways to make the appeal to the market simpler or more successful. One example, although not the only one, is **SPACs,** vehicles created for the acquisition and merger with unlisted companies allowing them to go to market, as a fast-track or accelerated process.

We are obliged to explore these new formulas that allow the development and increase in size of our stock market, thereby preventing, as far as possible, the relocation of Spanish companies to other markets.

Undoubtedly, the IPO of a company involves risks in the process, some of which can be significantly reduced under this new formula. But also, this formula of appeal to the market is not free of risks such as the understanding of the scheme by investors, the possible conflicts of interest of the sponsors or the transparency of the information published. However, at the CNMV we have spent months analysing this issue, developing supervisory criteria for when these operations begin to reach the Spanish market and we consider that they can undoubtedly be a feasible and attractive way to boost the market. Accordingly, we must analyse them from an open point of view.

The third answer to the question posed is the need to promote fundraising. On the other hand, the traditional over-banking should be compensated by the use of the securities markets to obtain own resources and thus, financing structures that allow withstanding, with a higher degree of success, unexpected or crisis situations. But there is also, in the "debit column" of raising equity, a certain aversion to the loss of control by entrepreneurs when they go to the markets.

This is where legislative developments can have a favourable influence. In this regard, it is worth noting, for example, the recent legal amendment through Spanish Law 5/2021, also called the Long-Term Shareholder Involvement Act, which introduces **loyalty shares** as a possibility in the articles of association of companies.

These shares grant double voting rights to those shareholders of a listed company who can prove that they have been shareholders for two uninterrupted years, or a longer period as may be established in the company statutes. The "one share-one vote" principle is indispensable in our system, and in my opinion, it should be the rule and the norm, but it is also necessary to foresee the occasional need for different statutory set-ups in our listed companies.

Fourthly and lastly, I have referred to the stimulation of financial investment as opposed to real estate or other more traditional investments in order to increase the attractiveness of the markets. Although I have left this measure as a tool to enhance the attractiveness of stock markets until last, it is by no means the least important. On the contrary, it may be the most outstanding in the medium and long term. Stimulating financial investment as opposed to more traditional investments (such as real estate or bank deposits) requires, above all, investment in financial education that provides citizens with the necessary tools to make informed investment decisions in an increasingly changing and dynamic environment.

In fact, recently, the CNMV, the Bank of Spain and the Ministry of Economic Affairs and Digital Transformation have proposed to the Ministry of Education and Vocational Training a plan to increase the presence of financial education in the school curriculum so that students of all ages in compulsory education - both primary and secondary - cover content related to this subject.

Investment in financial education will make it possible to achieve a society that is more open to the securities markets and thus to more long-term savings products, which in turn will make it possible to meet one of the objectives set out in the CMU, namely the search for products that supplement the national pension systems. Similarly, greater long-term savings will allow us to support more decisively the transformation processes of our companies, with broader and more ambitious investment horizons.

I shall finish by saying that there is no doubt that the stock markets, like the other sectors of our economies and our own society, face important challenges in the coming years. We have the opportunity to turn them into a lever for economic recovery and to support the business sector in tackling the great transformations of our time. In this aim, within the legal framework and the priority we give to supervision, the CNMV will always be an ally.

Thank you very much for your attention.