

The next five years:

Europe at a crossroads

Recommendations to make the European economy more competitive



Executive Summary

The European Union, with its 27 members and over 450 million citizens, is a global economic power that has brought peace, prosperity, and well-being to the continent. The EU has set the standard for the free movement of people, goods, ideas, and capital, which underpin open societies and democracies.

Despite its many strengths, the challenges facing the EU will only intensify over the next five years, including technological transformation, the transition to net zero, demographic change, and the need to increase defense spending. Generating economic growth will be critical, but this will happen at a time when the capacity of European governments to borrow or raise taxes is limited.

To make Europe more competitive and help it grow faster, we recommend focusing on five areas.

First, renew and complete the Single Market, which is still a work in progress.

Second, relaunch Banking and Capital Markets Union to build a stronger and more cohesive Single Market for financial services.

Third, allow banks to play their part in supporting economic growth by recalibrating the balance between financial stability, risk, and growth inherent in financial regulation.

Fourth, make green growth sustainable by ensuring international consistency in defining the sustainability reporting and disclosure framework.

Finally, drive digital innovation by developing and implementing a "token economy" propped up by payment transactions of the future.

We are confident that the path forward for Europe lies in reinforcing its competitiveness and strategic autonomy to drive growth.

We believe a stronger, more dynamic economy is the key to creating jobs and social well-being. The next European agenda must focus on Growth and Competitiveness.

We will do our part by providing financing to help people and businesses prosper. We are a driver of the green transition and the digital transformation of our society.

Collaboration between public sector and the financial system is key to ensuring we meet the needs of the new era of high-tech industry and deliver value for citizens.



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Generating economic growth will be more critical than ever

STEP 1

Renew and complete the Single Market

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The Single Market is at the core of the European project and provides the foundation for our social market economy. Yet, it is still a work in progress.

STEP 2

Relaunch Banking and Capital Markets Union

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The more competitive, efficient and reliable our financial services are, the more European people and businesses will prosper.

STEP 3

Allow banks to play their part in supporting economic growth

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Recalibrate the balance between financial stability, risk and growth inherent in financial regulation.

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More tokenised economies will enjoy a competitive advantage over economies that are slow to adapt.



The next five years: **Europe at a crossroads**



With its 27 members and more than 450 million citizens, the European Union is a global economic power. The EU has helped ensure peace and has brought broad prosperity and well-being to the continent. The EU has set the standard for the free movement of people, goods, ideas and capital – the freedoms that underpin open societies and democracies.

Over the last few years, the EU has faced challenges created by COVID and then the Russian invasion of Ukraine. By working together, it has protected Europe's citizens, safeguarded our prosperity, and defended our shared values. Our success to date has shown the power of and business collaborating to the benefit to all.

But we know that the challenges facing the EU will only intensify over the next five years. We will have to deal with technological transformation, the transition to net zero, demographic change and the pressure that will be placed on public services, the enlargement of the EU to the East, and the need to increase defence spending.

All of this will require political will – and financing. Yet it will happen at a time when the capacity of European governments to borrow or raise taxes is limited.

That means that over the next five years, generating economic growth will be more critical than ever.

Despite Europe's many strengths, however, we seem to have become less competitive over the last fifteen years. As the European Council on Foreign Relations recently pointed out, in 2008 the EU economy (with the UK) was larger than the U.S.'s, \$16.2 trillion versus \$14.7 trillion. Today, America's economy is now nearly one-third bigger.

We stand at a crossroads: the next political cycle give us the opportunity to prioritize once again the path to growth.

The next European agenda must focus on Growth and Competitiveness.

A plan for growth

To make Europe more competitive and to help it grow faster, we believe there are five areas on which to focus.

Step 1:

Renew and complete the Single Market

The Single Market is at the core of the European project and provides the foundation for our social market economy.

Yet, it is still a work in progress. Despite a Single Market passport, a firm operating across Europe faces vast arrays of disparate national rules on everything from advertising to consumer rights.

The Commission estimates that when it was adopted 30 years ago, the Single Market project addressed 80% of regulatory barriers by adopting common rules. But many of those gains have since been eroded and will continue to be, as new barriers are created by national legislation and regulations.

European Parliament **estimates that Europe can add €2.8 trillion**¹ to its economic output by 2032 – €59,000 per capita – if it pursues strategic, collective action in the coming years:

- A reinforced single market could generate an added €644 billion a year by 2032, compared to a baseline scenario.
- The green transformation could bring in €440 billion if pursued in an ambitious and united way.
- EU support for digital transformation could yield annual benefits worth €384 billion.
- A completed economic and monetary union could add €321 billion a year.
- International cooperation, external action and global governance another €170 billion.

The same study estimates **the cost of fragmentation to be €2 trillion** in the same period.

Completing the Single Market should therefore be a central focus for the next Commission and Parliament work plan. While it remains unfinished, European companies cannot obtain the scale and efficiencies that others in the U.S. or China can.

At the start of the new political cycle, Europe's leaders and institutions should reaffirm their commitment to renewing and completing the single market under a five-year plan with detailed measures. That plan would:

- Identify barriers to the four freedoms that have emerged and secure legislation to eliminate them.
- Extend the single market for services by harmonizing the regulatory framework, including disparate rules on consumer rights, advertising and marketing, bankruptcy and dispute settlement.
- Complete the European Banking Union and the Capital Markets Union.
- Empower banks to contribute more by rebalancing the regulatory and supervisory framework toward growth and competitiveness.
- Lock in Europe's competitive edge in transitioning to a sustainable, green economy.
- Create the framework for growth through digital innovation.



¹ EPRS Study
"Increasing European added value
in an age of global challenges"



Step 2:

Relaunch Banking and Capital Markets Union

Central to building a stronger and more cohesive Single Market is making a better single market for financial services. The more competitive, efficient and reliable our financial services are, the more European people and businesses will prosper. The European economy relies overwhelmingly on financing from banks for investment and growth. With an uncompleted banking union, European financial services remain fragmented, sub-scale and inefficient.

At the same time, with barriers to the movement of capital and funds and a prudential regime that penalises market-risk, Europe's capital markets have withered since the Great Financial Crisis. The European securitisation market (including the UK) – key to unlocking financing for Small and Medium-sized Enterprises – is also in dire need of support, currently just 6% of

the size of the U.S. market, equal to about 1% of GDP compared to 18% in the U.S.

This limited financial capacity impairs the competitiveness of European companies and economies compared to the U.S. and Asia.

Recommendations

- Banking Union requires, most urgently, shared risk among European nations through a European Deposit Insurance Scheme (EDIS) that can support citizens' deposits more efficiently and forcefully than the existing series of national schemes, enabling freedom of capital and investments.
- Capital Markets Union requires, as a first step, progress to deepen Europe's securitisation market. The Commission should therefore move forward with its proposals to re-launch securitisation as a financing vehicle in the EU and eliminate barriers to the movement of funds.
- Removal of cross-border obstacles for the consolidation of the banking industry in the EU.



Step 3:

Allow banks to play their part in supporting economic growth

Financial regulation in Europe needs to balance financial stability, risk, and growth. The current bias towards risk aversion should be corrected in favour of growth and competitiveness.

Following the Great Financial Crisis of 2008, European banks exponentially increased their capital and liquidity to ensure taxpayers' money would not be used to bail out banks. Banks are subject to very close supervision and regular stress tests. Risk management is at the core of banking.

At the same time, the financial services ecosystem has also been changing profoundly. Risks in the system come from different sources, including tech companies and other financial actors – nonbank financial intermediaries. Yet highly capitalised banks provide 70% of business financing – to large corporates and SMEs – in Europe, as opposed to this same structure in the US where capital markets financing instruments play the most relevant role.

The heavy layer of regulation European banks face – together with the fragmented single market and lack of capital markets – has impaired European banks' competitiveness and held back economic growth. In addition, it has diminished the attractiveness of this sector for investors, thus hindering its ability to grow.

Recommendations

- It is important for politicians to take into account the competitiveness of the EU economy, alongside financial stability, when defining the financial regulatory framework. It would be beneficial to establish metrics to effectively measure the impact of this framework on growth.
- A review of current capital requirements and supervisory processes could, in a hypothetical scenario, provide capacity for €4-4.5 trillion in additional bank lending¹, provided that policies and measures are put in place to ensure that viable borrowers have growth opportunities. Additional lending could support the financing of the green and digital transitions, and, more generally, investments in strengthening the competitiveness of the EU economy as the aforementioned.
- Simplify the current macroprudential framework and make it more transparent and understandable for investors. Make the regulatory and supervisory frameworks more predictable.
- Simplify the current complex and costly resolution regime.
- It would be beneficial to optimise the key processes such as the Supervisory Review and Evaluation Process and stress testing.

¹ Oliver Wyman Report "The EU Banking Regulatory Framework and its impact on banks"



Step 4:

Make green growth sustainable

The European Commission estimates that €700 billion in additional annual investment is needed to finance its decarbonisation plans alone between now and 2030. Unlocking the capital required for the green transition remains a major concern.

Amongst the major trading blocks and developed nations, Europe has led the global drive to a more sustainable, net-zero economy that achieves the Paris Accord goals.

The destination is clear: a net-zero economy that is more circular, sustainable, fairer, and inclusive. That goal is undermined if Europe further erodes its competitiveness and strategic autonomy. Continued action, without regard to sequences, transition periods, overall coherence and public opinion risk impairing the project.



Recommendations

- It is advisable for leaders and governing bodies to evaluate the impact of initiatives already adopted or in the pipeline on competitiveness before proposing new ones. Unnecessary bureaucracy should be avoided
- Transition to a low-carbon economy has to be part of the EU's growth agenda. The regulatory framework must be an enabler of the transition of the different sectors and growth.
- Governments need to develop national plans that are needed to give Europe's ambitions a chance to succeed, together with the tools and incentives to implement them. We must ensure that the financial sector is able to support businesses with their own credible transition plans.
- International consistency, among jurisdictions, and among regulators, is essential in defining the sustainability reporting and disclosure framework.
- Ensure that the capital treatment linked to climate and environmental factors remains risk-based, without penalising lending in a way that could jeopardise the transition to a more sustainable economy.

Step 5:

Drive digital innovation

Digitalisation is advancing at a fast pace and in nearly all economic domains. In particular, the digital transformation of industry and the associated growing demand for automated processes. For years, consumer behaviour has also changed as digital and mobile purchasing and payment methods gain ground.

To unleash the digitalisation potential in domains such as Industry 4.0, Machine-to-Machine economy (M2M), the Internet of Things (IoT), autonomous driving, big data, decentralised finance, the metaverse, and smart cities, but also in support for the green transition, the EU needs to develop and implement a “token economy”¹, propped up by payment transactions of the future, such as those underpinned by Distributed Ledger Technology (DLT, having Blockchain type as the most known).

Tokenisation allows fast, secure and automated execution of business and financial processes with lower transaction costs and risks and higher data availability, and it also enables liquidity and transferability to liquid and illiquid assets, which will positively influence economic growth.

By 2030, asset tokenisation will grow to become a market worth at least USD 10 trillion by 2030². More tokenised economies will enjoy a competitive advantage over economies that are slow to adapt. A successful tokenisation strategy will be essential to future growth and competitiveness.

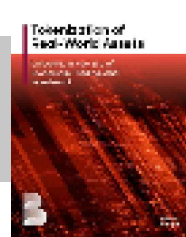
Additionally, the current datafication of the economy is marked by asymmetries and concentration. Overcoming data silos is crucial to addressing these asymmetries, promoting a healthy data economy within

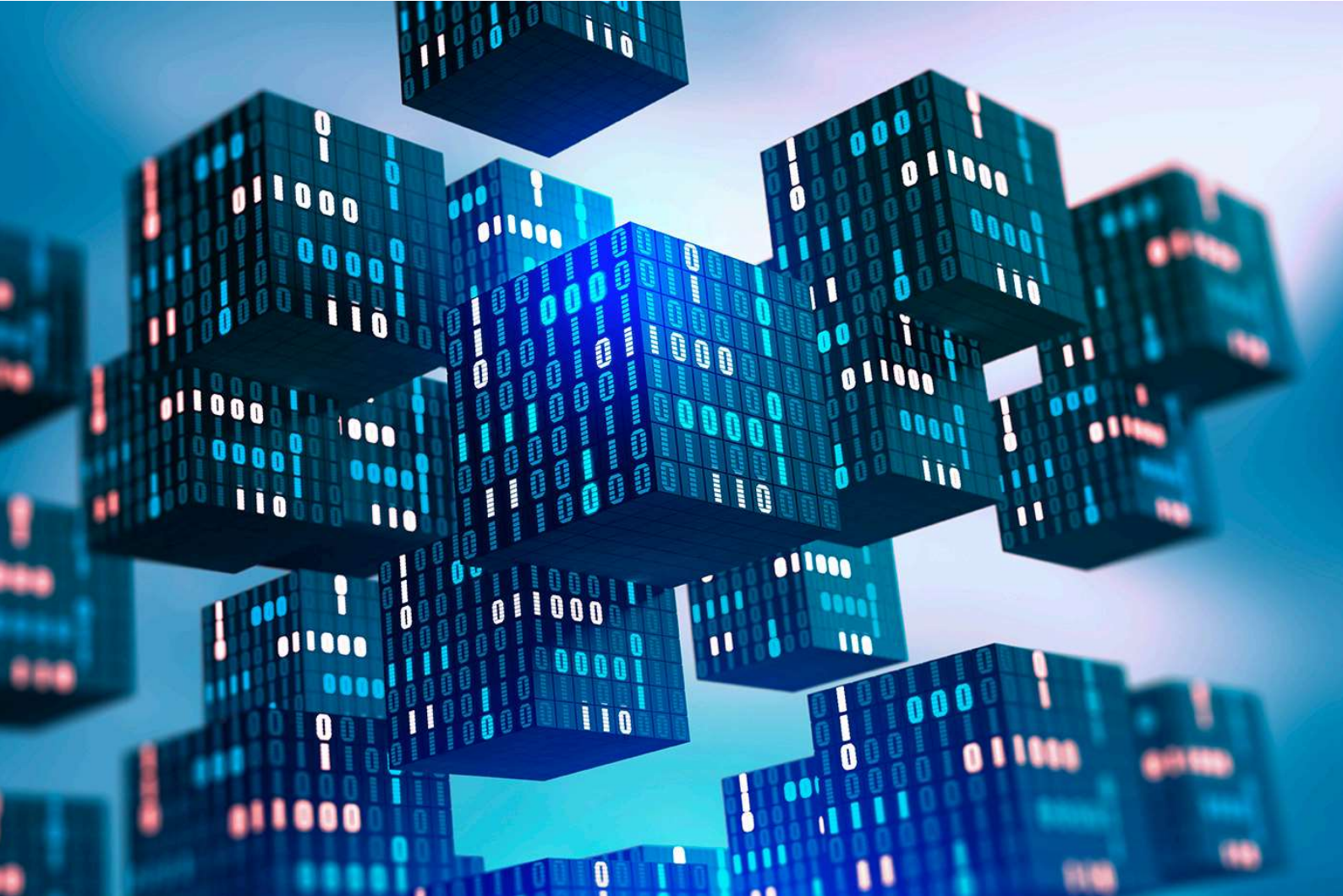


and among sectors. Data-sharing frameworks should be user-centric and cross-sectoral, grounded on users' consent and include data from all sectors (e.g. healthcare, energy, mobility, or the public sector).

¹ “A token represents a (tangible or intangible) asset in a digital form combined with information and assignable digital rights, all of which are connected in a programmable and heavily automated manner.”

² Roland Berger Global Consulting. “Tokenization of Real-World Assets: Unlocking a New Era of Ownership, Trading, and Investment”





Recommendations

- The tokenisation of finance is happening and will accelerate. Collaboration between governments, central banks, and the financial system is key to ensuring we meet the needs of the new era of high-tech industry and deliver value for citizens.
- A retail digital euro (rCBDC) should have the right design, a robust and sustainable business model and market involvement in designing payment solutions. Collaboration between authorities and market actors is crucial for achieving these conditions.
- The current wholesale central bank settlement systems should be updated to service DLT-based products and services, to better support the international role of the euro, enhance global cross-border payments and match the development of digital finance.

The needs of businesses are different from those of citizens. Tokenised commercial bank money (CBMT) could enable automation and better integration of payment transactions into operations with tokenised money under DLT-based systems (e.g. via micro and nano payments). For these types of solutions, pan-European standards will need to be defined by the market, similar to SEPA standards. CMBT generates added value for the digitalisation of the European economy and promotes Europe's competitiveness and its monetary and digital strategic autonomy.

The future data economy should be fair, competitive and safe. It should have the same rules for all participants, promote incentives for innovation – such as compensation, and fairly allocate liability to protect consumers better. This would increase innovation, investments, and legal certainty.

Europe is Santander's home

Santander believes in and is part of the European project. Founded in 1857, we have grown from a regional Spanish bank into a global financial institution with operations across Europe. The European Union has been a key factor of this growth and the jobs it has created. Europe is not only our home, but our future.

We are confident that the path forward for Europe lies in reinforcing its competitiveness and strategic autonomy to drive growth. We believe a stronger, more dynamic social-market economy is the key to creating jobs and social well-being.

We do our part by providing financing to help people and businesses prosper. We are a driver of the green transition and the digital transformation of our society. We work with more than four million SMEs worldwide and empowered 12 million people, of which 1.1 million are women entrepreneurs since 2019. We are proud to provide more support to higher education and entrepreneurship than any other company in the world. With a united, competitive Europe, we could do even more. We stand ready to work together to build a better Europe for all.



Santander's Board of Directors

"There will be no prosperity without growth, and there can be no growth without confidence, investment, innovation, and a policy framework designed to support productivity improvements, efficient resource allocation, and profitability"

Ana Botín

