Deutsches Aktieninstitut

Getting Europe Back on Track

Leveraging Capital Markets
to regain and ensure
Europe's global Competitiveness

OF DEUTSCHES AKTIENINSTITUT

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Current Challenges

Europe's global competitiveness is at stake! As the European Union is confronted with new geopolitical realities, higher inflation and the rebuilding and reorganization of supply chains, it is exposed to tremendous economic challenges.

Europe is struggling to keep up with the pro-business oriented United States and the increasingly proactive China and India, which strive for more global importance in geopolitical and economic terms. OECD data shows a clear lack of performance on a 5-year baseline for GDP growth rates:[1] the European Union (1.2%) is the low performer in comparison with other world regions. While the U.S (1.9%) is slightly improving, China (4.5%) and India (4.1%) lead the pack. The OECD forecasts no improvements in terms of strategic foresight in 2024, just a slight 1.5% growth rate is expected in the European Union.[2]

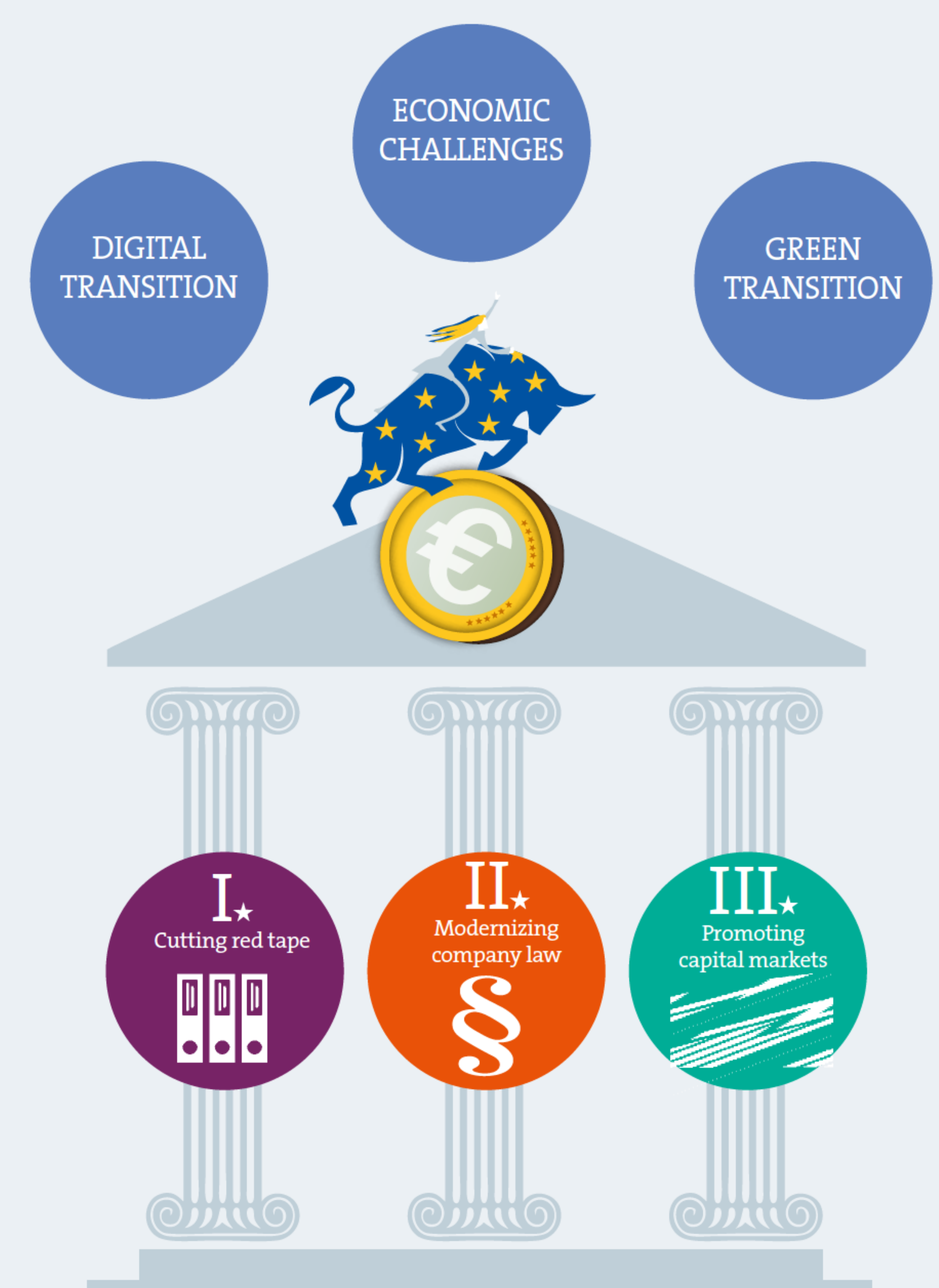
"The EU must address the current economic challenges while successfully embarking upon the digital and green transition."

The European Union must address these economic challenges while successfully embarking upon the digital and green transition ("twin transition"). This transition requires unprecedented capital and investments. The implementation of the European Green Deal alone requires approximately EUR 520 billion in investments per year from 2021-2030 and an additional EUR 92 billion from 2023 until 2030 to boost the capacity for manufacturing net-zero technologies.[3] The digital transition also requires significant investments, with the European Union committing itself to more than EUR 4.5 billion from 2023-2024 under the Horizon Europe work programme.[4]

In order to cope with the economic challenges and the twin transition, it is important that a common understanding of two aspects prevails under the next mandate.

"Institutions must understand that companies underpin the European economy and drive innovation and growth."

Firstly, institutions must commit themselves to the understanding that companies underpin the European economy and drive innovation and growth. By doing so, they automatically contribute to the wealth of the European society as employers and taxpayers. Legislative proposals should enable companies to prosper in order to pursue and promote



innovation. The reality, however, shows that the European Union is creating competitive disadvantages for itself by overstretching the regulatory framework governing the internal market. Increasingly, market mechanisms are not trusted, and companies are facing an ever-growing amount of red tape. These adverse developments must stop.

> "The private sector offers the potential to mobilize the necessary capital to drive the twin transition."

Secondly, the public sector alone cannot achieve the twin transition. The private sector offers the potential to mobilize the necessary capital to drive the twin transition, ensuring that the European Union can become carbon neutral by 2050 and is fit for the digital age. Capital markets are of key importance here because they enable positive changes for the economy and European citizens. Unfortunately, European capital markets are still underdeveloped in comparison to their international peers and are also increasingly losing ground. Although 2023 was a successful year for global IPOs, volumes were very subdued in Europe with no European market in the Top 10 globally.

> "For the prosperity of the European Union the public and the private sector must work together closely."

We call upon the incoming institutions to join their forces, to work together and commit themselves to restore the global competitiveness of the European Union! We also strongly believe that the public and the private sector must work together closely to identify problems, to fairly consider concerns and to develop lasting solutions for the prosperity of the European Union.

[1] OECD 2024 Key Short term economic indicators: OECD data explorer

[2] OECD Economic Outlook June 2023

[3] European Environment Agency, Investments in the sustainability transition: leveraging green industrial policy against emerging constraints", 7 Nov 2023, available at https://www.eea.europa.eu/publications/investments-into-the-sustainability-transition#:~:text=The%20implementation%20of%20the%20European,92bn%20from%202023%20until%202030.

[4] EU4Digital, EU to invest €4.5 billion in digital transformation for 2023-2024, 13 Dec 2023, available at https://eufordigital.eu/eu-to-invest-e4-5-billion-in-digital-transformation-for-2023-2024/

Steps Forward

Capital markets play a key role to improve the economic resilience of Europe and boost its competitiveness. They are capable of generating the tremendous funds needed to rebuild and transform the European economy and successfully deal with the massive and unique challenges outlined above. Their use needs to be optimized and their potential utilized. This will also deliver wealth for the European citizens, whom we want to enable to benefit from the use of capital markets.

In order to do so, the following adjustments to the capital markets regulatory ecosystem should be made:

I. Cutting red tape and furthering smarter regulation:

A reduction of bureaucratic burdens is needed by ensuring more principle-oriented legislation and less detailed requirements. Red tape must be cut and new bureaucracy avoided. In order to do so, a **competitiveness check** should be introduced. It is necessary to review existing legislation in order to eliminate strenuous requirements. Also, the one-in-one-out principle of the Better Regulation Agenda Guidelines should be duly observed.

> "A reduction of bureaucratic burdens is needed by ensuring more principle-oriented legislation."

II. Modernizing company law and clear focus for corporate governance:

Many companies considering going public prepare for a listing outside the EU (e.g. in the US) as the capital markets-environment is more developed and the legal situation is more flexible. The latter aspect could be tackled by the EU e.g. by introducing an optional, while genuine, European company law framework that capitalises on the best aspects from the 27 member states' regimes. This framework should be designed in a way that it is attractive to companies and should cater to their global competitiveness. Whilst the use of this "28th Regime" should be left entirely to the discretion of companies, the regulators must ensure that the key objective of Corporate Governance – ensuring the functioning and the operability of companies – are not weakened unintentionally by overloading corporate governance with ESG aspects.

> "Introduction of an optional European company law framework that capitalises on the best aspects from the member states' regimes."

III. Promoting a new equity culture and share-based retirement schemes:

"The Commission should play an active role in promoting share possession, capital markets-based pensions schemes."

A new equity culture needs to be promoted throughout Europe in order to improve the conditions for corporate finance while fostering the build-up of public wealth. The Commission should play an active role in advocating for instruments promoting share possession and for capital markets-based pensions and retirement schemes vis-à-vis the member states. Furthermore, financial literacy should be promoted.

Pursuing these objectives will contribute significantly to maintaining Europe as an attractive place for investment, business, creativity and innovation on the one hand while at the same time delivering societal wealth and a successful twin transition.

Please find concrete steps below:

I. Cutting red tape and furthering smarter regulation

In general, market mechanisms must be trusted rather than jumping to regulation and better cooperation between the regulator and the real economy is required to ensure that any proposal is principle-based and practicable. One-size-fits-all approaches are not helpful and should be avoided. An example of this can be seen in the Commission's Draft Regulation on late payments which seeks to paternalistically impose fixed deadlines for payments across all sectors and industries while disregarding industry-specific features and the need for flexibility.

Bureaucratic rules for issuers with no adequate corresponding benefits for investors need to be abolished. The EU Listing Act was a step in the right direction, but the development should not stop here. The incoming Commission should follow up in adjusting the European legal framework governing capital markets for the benefit of striking the right regulatory balance.

Areas in which cutting red tape and creating smarter regulation should occur include: (1) Corporate Reporting, (2) Sustainable Finance, and (3) Digitalisation and (4) Others.

1. Leaner and more practice-oriented corporate reporting

"Reporting requirements must be practicable, principle-based and proportionate."

Reporting requirements must be practicable, principle-based and proportionate. This should be the rationale especially with regard to sustainability reporting. Furthering the goal of reducing reporting requirements by 25% and maintaining this level of regulation by consistently applying the one in one out mechanism is needed. Companies must not be burdened with too detailed and unrealistic disclosure requirements ineffective for achieving the transition to a climate neutral economy.

Especially the complexity and granularity of the European Sustainability Reporting Standards (ESRS) must be reduced. The large number of mandatory data points (more than 800) causes major implementation problems for companies since they have to implement complex group-wide data collection processes and build up resources for sustainability reporting within their legal entities.

Against this background, it is crucial that the standard setting institutions keep track of developing guidance and support material for implementing the ESRS. As standards for sustainability reporting are issued at European and global level at the same time, interoperability of the ESRS with international standards, such as the ISSB standards or GRI standards, must be ensured.

The Corporate Sustainability Reporting Directive (CSRD), the European Sustainability Reporting Standards (ESRS), the Sustainable Finance Disclosure Regulation (SFDR) and the Taxonomy are interdependent and constitute a completely new and highly complex ESG regulatory ecosystem, which must be kept in balance and aligned as closely as possible. All information that banks and investors are required to report under the SFDR must be generated exclusively from the sustainability information disclosed by companies under the CSRD/ESRS and the Taxonomy. This principle must not be undermined. The European Commission should set up a dedicated working group of banks, investors and companies. It should analyse which data reported as part of the ESRS is relevant for the investment decisions of banks and investors.

Companies also need sufficient time to implement the reporting requirements. A more realistic time frame and better timely coordination regarding the implementation of regulation is needed in the future. At the moment, companies are e.g. confronted with the obligation to implement the Taxonomy and the CSRD/ESRS at the same time, which frequently overburdens their available resources and capacities.

Regulation aimed at introducing mandatory joint audits must be rejected. The option for a joint audit should be left entirely to the discretion of the audited entity. Up to now, the market has not shown a strong desire for joint audits, neither by companies nor by their stakeholders; thus, no member state has made them mandatory except for France. Joint audits certainly add to the complexity of the audit itself and the selection process of the auditors. In conjunction with existing audit regulation, the joint audits will further limit the auditors' choice for companies thereby limiting competition instead of improving it.

2. Sustainable Finance

The use of the financial sector to channel funds into sustainable investments is critical for a successful transition to a sustainable economy. A proportionate and realistic approach to sustainable finance is needed. Regulatory initiatives should acknowledge that companies have an interest in building a sustainable business model to remain competitive in the long term. Taking this into account, the European legislators should reward their efforts instead of imposing additional regulatory burdens on them.

"Climate transition plans of corporates should address the present shortcomings of the EU Taxonomy Regulation."

At present, the EU Taxonomy for sustainable activities does not sufficiently address the transition process, which does not happen overnight. Companies are already disclosing their Taxonomy-aligned business activities, which are currently very low. As the requirements of the Taxonomy are very complex it is not expected that the percentage of taxonomy aligned activities will rise sharply in the near future. Transition plans of corporates explaining their goals, commitments, actions and progress towards climate action should address the present shortcomings of the Taxonomy. From this perspective, they should be included to a larger extent in the political discussions on sustainable finance.

3. Digitalisation

"The right balance must be struck between protection from risk and overregulation."

Digitalisation and technological developments present an opportunity for European companies to remain competitive and to develop new businesses. Digital solutions offer incredible opportunities and Europe should be on the forefront of developments. However, it is also important to note that the right balance must be struck between protection from risk and overregulation, which threatens to stifle innovation. This would ensure that companies can benefit from the advantages presented by digitalisation.

We therefore support the Distributed Ledger Technology ("DLT") pilot regime, which allows for testing DLT-based trading and settlement facilities within a protected and flexible regulatory framework. There is potential for digitalisation steps not only in the digitalisation of securities as a financing and investment instrument, but also, for example, with regard to the interaction between companies and their shareholders. The upcoming review of the Shareholder Rights Directive thus should offer the best possible flexibility in this regard.

Another important topic with regard to digitalisation is the digital euro. The digital euro should be designed in a way that ensures Europe's competitiveness in the global digital framework also for strategic reasons. To capitalise on the potential benefits of the digital euro, the digital euro must be developed to best serve the needs of people, banks, and businesses in the EU. From the perspective of companies, it is therefore essential, that the digitalisation of the European currency does not stop with the development of the retail digital euro, but also an efficient solution for a wholesale digital euro will be created. We therefore support, that the ECB has picked up this necessity by testing possible solutions which should be supported by the legislator.

4. Other

"Cutting red tape and strengthening shareholder culture should persist when creating legislation that impacts the Capital Markets Union."

Other requirements to cutting red tape and ensuring better regulation include unrestricted access to corporate finance as a guarantor to foster corporate investments in R&D. This is necessary for boosting innovation and effectively furthering the twin transition.

It is also necessary to recalibrate the Capital Markets Union. The CMU needs to be understood as a project that makes it easier for companies to do business in the European Union and to cover their financing needs for innovative and long-term projects, while at the same time ensuring that investors have appropriate incentives to invest funds in shares, bonds and other capital markets products. The EU Listing Act itself was not sufficient, and the Commission must explore further means to lower the barriers for the use of capital markets, e.g. by implementing the recommendations put forward in 2017 by the European Commission's expert group on liquidity of European corporate bond markets.

Regulatory burdens and inconsistencies hampering the objectives of the CMU need to be identified and dismantled to unleash the CMU's full potential. Accordingly, the ideas outlined in the Franco-German Roadmap on the CMU from September 2023 should be followed to take the project forward. Particularly, the focus on cutting red tape and strengthening shareholder culture should persist when creating legislation that impacts the CMU.

Additionally, the better regulation agenda should be thoroughly pursued and not set aside for the sake of political compromise; the same goes for the attempt to reduce reporting obligations for companies by 25 percent. We applaud the Commission for this initiative, which is a welcome contribution to maintain the global competitiveness of European companies.

Moreover, and in this context, a competitiveness check for existing and new legislation under preparation should be introduced in accordance with the Franco-German proposal for cutting red tape from October 2023.[5]

II. Modernizing company law and clear focus for corporate governance

"A revision of the current SE regulation could be a starting point."

The development of an optional while genuine European company law regime requires its inalterability by the member states. This is a precondition for ensuring a barrier-free operability throughout the EU. Companies throughout the EU should be enabled to opt for this voluntary regime. In order to guarantee their free choice, it is essential to preclude any interference with any field of member state law (e.g. taxation law) capable of limiting the companies' true and independent decision.

This voluntary 28th regime should be simple and practicable and should represent a true alternative to third country company law regimes that European companies are often opting for today. The 28th regime should thereby cater to the competitiveness of European companies. A revision of the current SE regulation could be a starting point with the objective to retain existing provisions and to delete member state options. In addition, minor adjustments could be made where this is required by the case law of the European Court of Justice.

"The key objective of corporate governance – ensuring the functioning and the operability of companies – must be maintained."

We are concerned that the corporate governance systems in the European Union with its proven checks and balances could be weakened unintentionally through the debate on "sustainable corporate governance" by giving additional stakeholders an explicit role in corporate governance legislation. This approach does not take into account that there are distinct differences between "E", "S" and "G" factors. "G" refers to the way corporate objectives are accomplished and seeks to achieve procedurally correct results, meaning better decisions and more efficient decision making. This difference should be kept in mind when legislative proposals are drafted. The key objective of corporate governance – ensuring the functioning and the operability of companies – must not be undermined. A clear focus for corporate governance is needed.

[5] French-German Government Communication, Reducing bureaucracy in these unprecedented times - French-German Paper on Better Regulation and Modern Administration in Europe, 12 Oct 2023, available at 12/10/2023 - Reducing bureaucracy in these unprecedented times - French-German Paper on Better Regulation and Modern Administration in Europe - Presse - Ministère des Finances (economie.gouv.fr)

III. Promoting capital markets and equity culture

Capital markets and equity culture is underdeveloped in many parts of the European Union. The insufficient use of shares by the population has two negative consequences: people are missing out on attractive returns from instruments for long-term wealth building and the old-age provision. Furthermore, as a side effect, companies are missing out as well. Investment in long-term wealth building instruments benefits companies as this ensures more available capital with which companies can finance innovation, growth and employment.

In order to achieve the goal of financial participation in capital and equity markets several measures are needed both on the European and the national level:

We welcome that the European legislator has started to acknowledge that overly burdensome regulation could disincentivise banks and other market participants to actively offer certain financial products to people or increase capital market entry barriers. Therefore, we welcome for example efforts to clarify the scope of the Packaged Retail and Insurance-based Investment Products Regulation (PRIIPs) with regards to corporate bonds and reintroduce access for retail investors in that asset class. Nevertheless, the legislator does not act consistently in that respect. For example, under the Retail Investor Strategy also additional bureaucracy is created, which would make the offer of investment advice more and more costly and unattractive, while bringing no additional benefit for the investor.

"We welcome any initiative for promoting and furthering financial literacy throughout Europe."

We also believe that the EU institutions can and should take a moderating role in policy areas that are mainly in the national competence in order to keep the important issue of capital market participation on the agenda. This could be achieved by providing best practice examples and promoting peer-to-peer learning. Against this background, we welcome any initiative for promoting and furthering financial literacy throughout Europe.

"Every action by the EU Commission promoting more shares in the pension system is welcomed."

Similarly, we welcome every action taken promoting more shares in the pension system, as broadly diversified, long-term equity investment have generated average annual returns of six to nine percent in the past. The introduction of tax incentivised investment saving accounts especially for shares, and employee share-ownership which increases familiarity among workers with shares in particular. Some EU member countries made significant progress in this area. The remaining member states should follow. The Commission should promote this progress and elaborate best practice examples which could be taken as role models.

Finally, the tax discrimination of equity compared to interest payments must be ended. Even though tax policy is national competence, the proposal for a "debt-equity bias reduction allowance" of the European Commission approach is a good starting point for a broader debate on this issue. However, reducing the tax discrimination of equity must not be take the form of less favourable tax treatment of interest income, as proposed by the Commission, but a more favourable treatment of equity as otherwise the taxes on investments would increase on average. Furthermore, equal tax treatment of equity should be achieved on investor level and not on company level, which would directly incentivise people to invest in shares and other equity.

Summing Up

"Attractive capital markets are crucial for raising the massive funds needed for a successful twin transition."

Europe is facing unique and unprecedented challenges at present, especially when it comes to its economy. These challenges threaten the European Union's global competitiveness and we risk falling behind. The key to retaining our attractiveness and competitiveness are the capital markets. Capital markets are crucial for raising the massive funds needed for a successful twin transition. The regulatory framework governing capital markets should be recalibrated to unfold their full potential. In order to do so, red tape must be cut to achieve an unrestricted and easy access to capital. This will deliver growth and innovation and thereby improve Europe's global competitiveness, which should be a clear priority in the forthcoming legislative cycle.

Moreover, the reduction of bureaucratic burdens should be flanked by modernization efforts for company law and initial steps to create a new equity culture to enable the build-up of public wealth. Institutions, member states and the private sector alike should join their forces and act as a team in order to get Europe back on track!

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