NEW FINANCIAL
Rethinking capital markets

A RENEWED VISION FOR EU CAPITAL MARKETS

UPDATE OF OUR ANALYSIS OF THE STATE OF PLAY AND GROWTH POTENTIAL IN EU CAPITAL MARKETS

January 2024

By Christopher Breen, Maximilian Bierbaum, and William Wright

> *This report paints a renewed and ambitious vision for EU capital markets and identifies the potential for game-changing growth to support investment, innovation, and prosperity. We estimate that an additional 4,400 companies in the EU could raise an extra €470bn every year in the capital markets, and that an additional €12tn in long-term capital could be put to work in the EU economy to help boost sustainable growth.*

A renewed vision for EU capital markets

It is well known that EU capital markets are not as developed as they could or should be, but what is often overlooked is the vast growth potential that they have. With a busy election year ahead and a new European Commission and European Parliament coming in 2024, this report outlines a bold and ambitious but realistically achievable vision for capital markets across the EU and highlights the potential benefits of deeper capital markets to the EU economy and national economies in concrete and practical terms.

It paints an optimistic vision of the sort of capital markets the EU needs (and could have) to fully support the sort of growth, investment, and prosperity that it wants. And it shows how capital markets can help address some of the biggest social and economic challenges facing the EU such as financing the transition to net zero and providing a more secure retirement for millions of European citizens.

The report builds on our [recent analysis of the state of EU capital markets] and measures the growth potential in capital markets across the EU. We express this growth in concrete terms: how many more companies in each country could potentially access the capital markets, and how much more money would they be able to raise? To pick one example: we estimate that around 475 additional companies in Germany could benefit from an additional €9bn in venture capital each year. Another way of looking at this is that every year 475 high growth companies in Germany are not getting that investment today.

What if…?

The report demonstrates an ambitious but achievable growth scenario. We measure the size of capital markets relative to GDP in each EU member state, rank them, divide them into quartiles, and ask, 'what if capital markets in each country were as developed as the average of the more developed countries in the quartile above?' While this growth may seem improbable from where we are today, it is based on what other member states in each sector have already shown is perfectly possible. Even modest progress towards this growth will have a significant impact - but this requires a renewed commitment from EU policymakers, national authorities, and market participants.

We hope this research provides relevant insights and we are always interested in your thoughts and questions. I would like to thank Christopher Breen for collecting and analysing the wealth of data that underpins this report, William Wright for his guidance and feedback, Dealogic and Preqin for providing access to their data, and our members for supporting our work on bigger and better capital markets. Any errors are entirely my own.

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NEW FINANCIAL
Rethinking capital markets

New Financial is a think tank that believes Europe needs bigger and better capital markets to help drive growth and prosperity.

We think this presents a huge opportunity for the industry and its customers to embrace change and rethink how capital markets work.

We work with market participants and policymakers to help make a more positive and constructive case for capital markets around four main themes: rebooting UK capital markets; reforming EU capital markets; driving sustainability; and driving diversity.

We are a social enterprise funded by institutional membership from different sectors of the capital markets industry.

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Here is a short summary of the report:

1. **A bigger role:** this report outlines a bold and ambitious vision for capital markets across the EU. It highlights the potential benefits of deeper capital markets to the EU economy and national economies and shows the huge potential for growth in capital markets in each country.

2. **A renewed vision:** with a new European Commission and European Parliament coming in 2024, there is a big opportunity to refocus capital markets union on a smaller number of key challenges. Five structural forces that could shape that vision include i) consolidation of supervision ii) a 'bottom up' approach iii) the transition to net zero iv) consolidation of market infrastructure v) digitisation and technology.

3. **Game-changing growth:** there is huge potential for growth in capital markets across the EU. We estimate that an additional 4,400 companies in the EU could raise an extra €470bn every year in the capital markets - nearly doubling current levels of activity. This growth (and any progress towards it) would reduce the reliance of the EU economy on bank lending, drive innovation, and boost investment in jobs and growth.

4. **A more sustainable future:** our analysis shows the potential to transform pools of long-term capital (pensions and insurance assets) that the EU needs to provide for a more sustainable future. An additional €12tn in long-term capital could be put to work in the EU economy - roughly double today's levels - with the average value of long-term savings per household rising from around €69,000 today to €128,000.

5. **Ringing the bell:** there could be an additional 230 IPOs in the EU raising an additional €40bn in capital every year. Italy could see an additional 95 companies that go public every year; the emerging EU (including Poland, Hungary, and the Czech Republic) an additional 45 companies raising €4bn per year.

6. **Fuelling the growth economy:** the EU does not have a start-up problem but it does have a problem channelling investment into high potential companies that drive job creation. We estimate that 3,245 additional companies in the EU could benefit from an extra €41bn in venture capital funding every year, nearly double current levels, and the number of companies listed on growth stock markets could quadruple.

7. **Five big challenges:** in the coming decades the EU will need to i) successfully transition to net zero ii) better support innovation and growth iii) give companies better access to more sources of funding iv) support an ageing population v) secure and advance its role on the global stage. These challenges are complex but present a once-in-a-generation opportunity to transform the lives of millions of EU citizens.

8. **Not quite there yet:** more developed capital markets are not the obvious answer to all of the challenges the EU is facing, but the EU will not be able to address its biggest challenges without them. Relative to GDP, EU capital markets have grown by nearly 50% since 2014 and are deeper than ever, but they are still not as developed as they could or should be.

9. **The global perspective:** one of the most concerning but often overlooked developments in EU capital markets is that they are shrinking in a global context. The EU's share of global activity has fallen from 18% in 2006 before the financial crisis to just 10% today. In the longer term, without urgent reform, the EU's share will shrink to single digits.

10. **A new sense of urgency:** to build bigger and better capital markets, member states, EU authorities, and the wider banking and finance industry should focus on i) building deeper pools of long-term capital ii) rethinking the supervisory and regulatory framework iii) simplifying market infrastructure iv) ensuring the EU's international competitiveness and attractiveness v) embedding political support across the EU.

The growth potential in EU capital markets - and where we are today

This section provides key takeaways on the growth potential in EU capital markets and their state of play today.

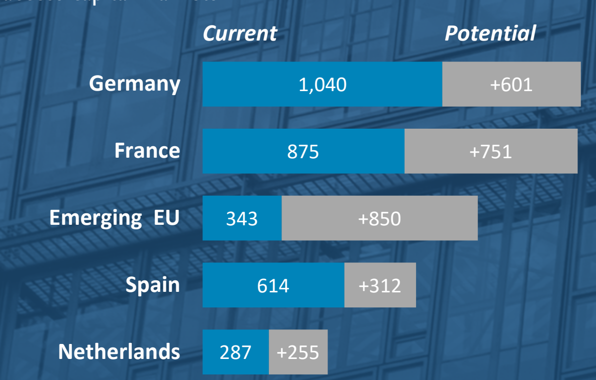
>>> DRIVING GROWTH

4,400 The number of additional companies in the EU that could use capital markets for funding every year

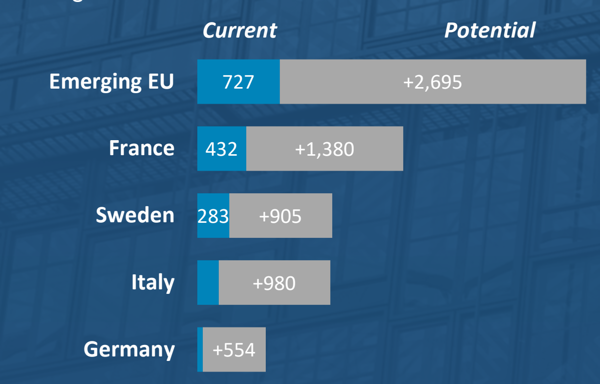
More than 4,400 additional companies per year could access capital markets to raise money in the equity, venture capital, corporate bond, or leveraged loan markets.

This is a 90% increase from where EU capital markets are today and would significantly reduce the reliance of companies in the EU on bank lending. This increase in capital markets funding would play a vital role in helping Europe boost economic growth and help member states and the EU achieve ambitious goals in the areas of sustainability and digital innovation.

i) Potential growth in the number of EU companies that could access capital markets



ii) Potential growth in the number of EU companies listed on SME & growth markets



>>> A SHOT IN THE ARM

€470bn Additional amount of funding from capital markets for EU companies every year

Companies in the EU could realistically raise an additional €470bn in funding every year from the capital markets. That represents a 67% increase on current levels of activity and a shot in the arm of almost 3% of EU GDP a year.

>>> THE 'C IN CMU'

€12tn The potential increase in pools of long-term capital in the EU

Pools of long-term capital (pensions and insurance assets) in the EU could nearly double. This capital would support the European economy and translate into an increase in long-term savings per household from around €69,000 today to €128,000.

>>> THE POWER OF EQUITY

230 Additional IPOs raising an extra €40bn every year

The number of companies listed on stock markets in the EU could more than double from current levels of around 6,200 to 14,000. This would add nearly €11tn in market capitalisation.

>>> INNOVATION AND GROWTH

3,245 The number of high potential firms in the EU missing out on venture capital funding

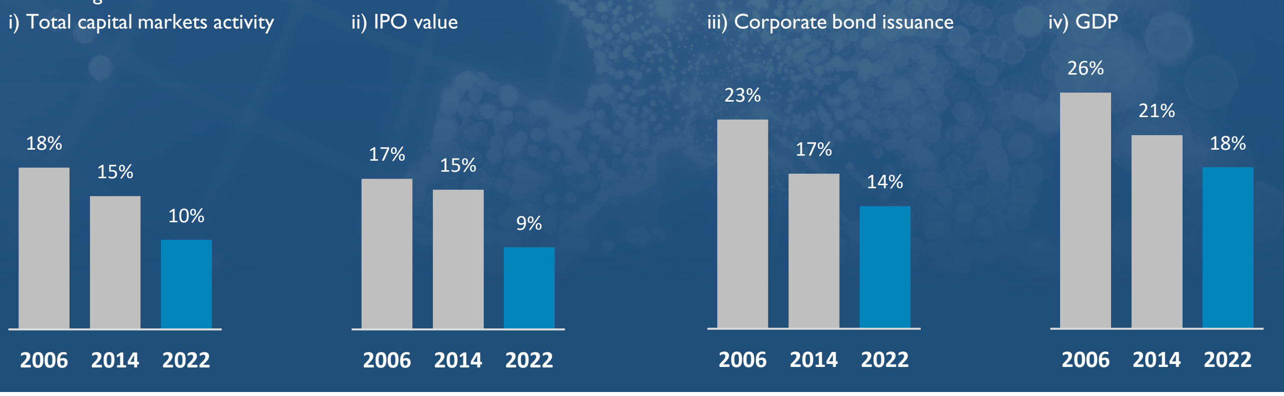
The 3,245 additional high growth companies in the EU could access an extra €41bn per year in venture capital funding. This kind of growth is not unrealistic: from 2014 to 2022, venture capital funding in the EU increased from €4bn to €51bn per year.

KEY TAKEAWAYS: EU CAPITAL MARKETS TODAY

>>> THE GLOBAL PERSPECTIVE

One of the most concerning but often overlooked developments in EU capital markets is that they are shrinking in a global context. The EU's share of global capital markets activity has declined at a faster rate than the EU's share of global GDP.

The EU's global market share in:



>>> NOT THERE YET

½ The depth of capital markets in the EU relative to the UK

Capital markets in the EU are less than half as large relative to the economy as in the UK, which in turn is around half as developed as the US across 26 sectors of capital markets activity. While capital markets in the EU have grown rapidly since the financial crisis, there is still significant scope for growth.

>>> CAPITAL MARKETS WITHOUT CAPITAL?

46% The size of pools of long-term capital as a % of GDP in the EU relative to the US

Deep pools of long-term capital are the starting point for deep and effective capital markets, but they are much smaller in the EU than in comparable markets. Pension assets and direct investment in funds, stocks, and bonds in the US combined are nearly four times the size as in the EU.

>>> OLD HABITS (1)

76% Bank lending as a share of corporate borrowing in the EU in 2022

Companies in the EU are still heavily reliant on bank lending for their funding and it is often the only choice rather than one of a range of financing options. In the face of economic headwinds and structural challenges, banks on their own will be unable to provide the necessary funding that European companies need.

>>> OLD HABITS (2)

34% The share of household financial assets in the EU that are held in bank deposits

Households in the EU keep a third of their financial assets in cash. If they increased their asset allocation to investments such as stocks, bonds, or funded pensions by just five percentage points this would unlock an extra €1.8tn (11% of EU GDP) that could support investment, innovation, jobs, and growth.

For more detail see our report from 2023 on 'EU capital markets: a new call to action' that benchmarks the size and depth of EU capital markets.

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A renewed vision

Building bigger, deeper, and more integrated capital markets in Europe cannot be magically achieved overnight. Capital markets union (CMU) is a long-term project that will take decades to achieve. But the EU cannot tackle the biggest challenges it is facing without more developed capital markets. With elections looming, conversations about the future of EU capital markets must be part of the political debate. The good news is that strong foundations have been laid over the last decade to strengthen the EU's capital markets, built around reforms put forward by the European Commission and regulators, efforts by individual member states, and support from Europe's financial industry.

With a new European Commission and European Parliament coming in 2024, there is a big opportunity to refocus CMU on a smaller number of key challenges. We also think that policymakers and industry leaders can and should paint a bolder and more aspirational vision for CMU. This section outlines five structural forces that could shape that vision, and what different sectors of EU capital markets could look like in the next few decades.

1) Structural forces

i) Towards single supervision: you cannot magic a single capital market in the EU out of thin air by creating a single markets supervisor, but ultimately you cannot have a genuine single market without one. The first step of ensuring single supervision across the EU would be to significantly reduce the fragmentation of EU capital markets. The next step of creating a single central supervisor for larger firms and international activities is a long-term prerequisite for anything resembling a single market. This supervisor would pool expertise from across the EU, have independent governance and accountability to the European Parliament, and work closely with the other European single supervisors with similarly enhanced mandates for banking, pensions, and insurance. It would also work closely with national authorities, who would continue to oversee smaller companies and more domestic activities.

ii) A bottom up approach: while top down measures are critical to building out deep and liquid capital markets in the EU, much can be done on the member state level using what we call a bottom up approach toward capital markets development (and some areas such as reforming pensions, tax, and insolvency, are areas that are almost entirely a national economic and social issue in the first place). Whenever we ask what can be done at an EU level to boost capital markets development, we also need to ask what member states can do to support and develop capital markets given that comparable economies within the EU have already shown what can be achieved. They would coordinate with each other to share best practice, build out regional capital markets, and support the overall goal of building a CMU through synchronisation of policies and initiatives. The Commission and each member state would work together as well, with the Commission providing member states with the know-how and resources to implement specific regulations and policies.

iii) Towards net zero: the transition to a more sustainable economy and net zero will require more capital over the next few decades than bank lending and public money can provide on their own. Capital markets will be crucial to source the necessary amount of funding, but in their current form capital markets in the EU are not able to address this challenge. Europe would build on its successes in sustainable finance activity and set a global example in sustainable financial regulation, building on policies such as the Sustainable Finance Disclosure Regulation, the EU green taxonomy, and the EU green bond standard.

The EU would also channel trillions of euros from pensions, insurance and individuals into tackling climate change to avoid stressing government budgets and relying too much on bank lending. The ambition must be that at some point in the near future there will not be a distinction between 'sustainable finance' and finance anymore but that any finance flows will be aligned with the EU's ambitious climate and net zero goals.

Fig.1 A single market?

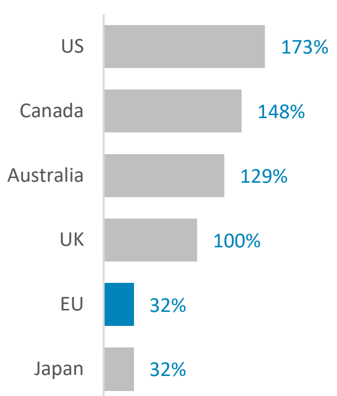
Comparison of EU and US market structure in equities in 2022

Metric	EU	US
Market value	€10 trillion	€36 trillion
# Exchange groups	22	7
# Listings exchanges	31	3
# Trading exchanges	34	16
# CCPs	17	1
# CSDs	22	1

Source: New Financial

Fig.2 The 'C in CMU'

The average size of pension assets in % of GDP in the three years to 2022



Source: OECD, New Financial

iv) Consolidated market infrastructure: one of the main keys to unlocking a single capital market is the radical simplification of market infrastructure. Instead of a complex patchwork of national infrastructure with limited competition (which repeats across equity and bond markets, derivatives, and regulation - see our report from 2021 on *'The problem with European stock markets')*, the EU would migrate towards a series of three to five competing blocks of market infrastructure and exchange groups with a more consolidated post-trade infrastructure, perhaps with each group having its own CCP and CSD.

Each of these groups would not only merge the exchanges within them but also the markets they operate, creating a small number of genuine single markets that would be deeper, more liquid, and more efficient. The recent initiative by the European Council and Parliament to create a consolidated tape for equities and ETFs is an important step toward spurring consolidation in infrastructure, but more work could be done toward additional initiatives such as creating a single open data source for financial and non-financial information on all issuers across the EU.

v) Digitisation and technology: digitisation and the exponential progress in technology will transform the economics and processes of banking, finance, and capital markets in the coming decades. The emergence of artificial intelligence over the past two years has allowed for greater automation of tasks and the ability to extract, analyse, and produce information on vast amounts of financial data. Other technologies such as cryptocurrencies have disrupted the market, demanding regulators and financial actors to innovate and develop new policies.

Technologies such as cryptocurrencies and artificial intelligence would drive efficiency in the markets and open up the financial system to new investors, stakeholders, and clients. For the EU to be ready for this transition toward digitisation, it will need to open up pools of risk capital that companies can access in order to expand their businesses.

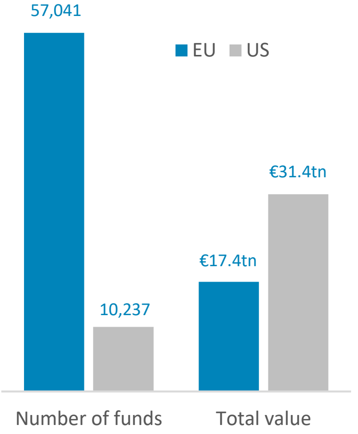
2) A sector-by-sector vision

i) Pools of long-term capital: you cannot have deep capital markets without deep pools of capital, but pools of capital in the EU are much smaller than in comparable economies such as the US, UK, Canada, or Australia.. The introduction of a comprehensive pensions dashboard across the EU would highlight the long-term unsustainability of pay-as-you-go pensions provision in many of the largest economies in the EU. This in turn could lead to the gradual introduction of auto-enrolment workplace pensions across the EU, ideally based on the large, collective, low-cost industry-wide model used in the Netherlands or Denmark.

Increasing the availability of workplace pensions would help EU citizens have more opportunities to connect their wealth with investments that they care about. And a new retail investment culture could provide even more long-term capital – see Sweden, where retail investment has been fostered through tax incentives and supportive regulatory and structural conditions.

Fig.3 More fragmentation

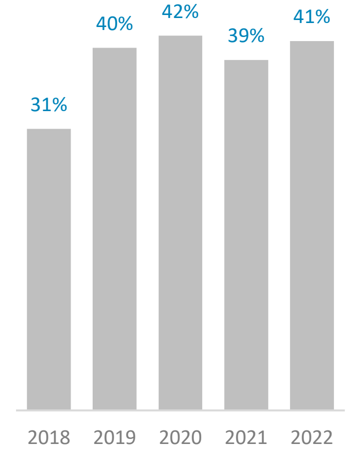
Comparison of investment funds in the EU and US in 2022



Source: EFAMA, ICI, ESMA

Fig.4 A world leader

EU activity as a percentage of global ESG activity from 2018 to 2022



Source: Dealogic, New Financial

ii) Investment funds: in the past decade, the value of investment funds in the EU has more than doubled in nominal terms but with more competition, the roll-out of auto-enrolment pensions, the creation of a single supervisor, and the removal of cross-border barriers to distribution, this would easily triple in the coming decade. That would translate into a little more than €50 trillion in investment funds in today's money.

This would be accompanied by radical consolidation and massive reductions in costs. There are more than five times as many investment funds in the EU today as there are in the US, although the US market is nearly twice as large by value. If the number of funds in the EU halved (to a mere 28,500), the average fund size would double, which in turn would improve the efficiency of the industry. This would be combined with technology and more competition to significantly reduce the fee gap on funds between the EU and the US. EU citizens pay billions of euros a year in fees that eat into their long-term returns: EU investors pay more than double the fees as their US counterparts (roughly 1.2% vs 0.4%).

iii) Asset management: the surge in pensions assets and investment funds in the EU would fuel rapid growth in the EU asset management industry, with assets under management potentially increasing from €19 trillion in 2022 in line with the growth in pools of long-term capital. EU asset managers would no longer be able to rely on captive distribution networks or the protection from national barriers to support their business model, which would encourage consolidation.

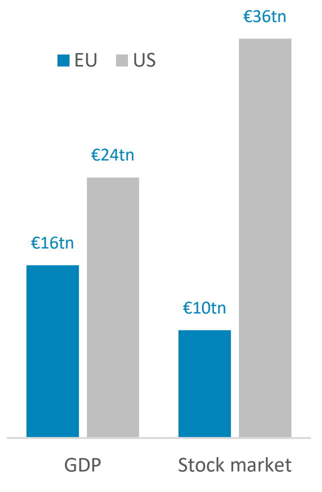
This could reduce the number of asset management firms in the EU by more than a third from today's level of 3,300 to (just) 2,000. This consolidation would benefit large EU asset managers giving them a stronger foothold for their global business (in much the same way that US asset managers today enjoy a home market advantage). Paris could overtake London as the main centre for managing investment fund assets by 2030 and as an overall asset management centre by 2040.

iv) ESG capital raising: over the last five years, ESG capital raising (particularly in the form of ESG labelled bonds) has increased in terms of value and number of issues across the EU. This has made the EU a world leader in ESG capital raising, reaching nearly €700bn in total ESG capital by 2021 and maintaining that into 2022. If the EU wants to retain this position, it will need to provide further clarification around what exactly 'ESG' means and ensure that the EU's green taxonomy is fair yet specific when it comes to identifying green investments.

A worrying recent trend is the 'ESG backlash', particularly in the US. To avoid a repeat of the heated US debate around ESG on the European continent, the EU will need to provide clear definitions and ensure that ESG is not a meaningless word. Ensuring that high emitting companies who are not serious about the transition of their own businesses are not included in ESG indices, and making sure ESG ratings are credible and comparable and perhaps based on a double material approach, would be a good start.

Fig.5 A transatlantic divide

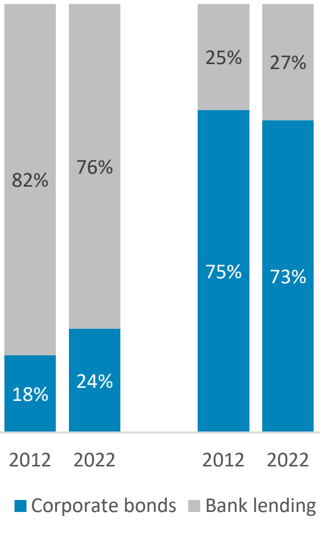
Comparison of GDP and stock markets in the EU and US in 2022.



Source: IMF, FESE, WFE

Fig.6 Old habits

Stock of bank lending and corporate bonds as a share of corporate borrowing in the EU and the US from 2012 to 2022



Source: ECB, BIS, Dealogic, US Treasury, New Financial

v) Stock markets: the most obvious shift in EU capital markets by the 2030s would be the rapid growth of stock markets. Today, the US economy is one and a half times larger than the EU, but its stock markets are more than three times bigger. The consolidation of European stock exchanges and market infrastructure, growth in the domestic investor base, and gradual abolition of the tax differential between debt and equity funding would mean that the value of EU stock markets would more than double in the next decade to around €20 trillion. The EU could use the reforms suggested above to boost the number of listed companies to the pre Covid peak of 6,000 and bring smaller yet high-potential companies into European growth markets (with the potential cumulative value of growth market listings being more than €600bn.)

vi) IPOs: the shift in scale and structural changes in EU stock markets would provide much deeper, more efficient, and more liquid markets for companies to raise money. After a glut of IPOs in 2021, the market collapsed in 2022, leaving a significant amount of room for growth: the annual value of IPOs could reach more than €60bn a year (up from an average €26bn a year as of 2022). If that sounds unlikely, it is in line with the surge that occurred in 2021, which saw €49bn raised via IPOs. This surge would provide the largest tech companies in the EU with a big enough listing venue, removing the need to list in the US, and dozens of the roughly 150 unicorn tech firms in the EU today would list in the coming decades. The new depth and scale of EU markets would also attract international issuers.

vii) Corporate bonds: EU companies have been reducing their reliance on bank lending and embracing the corporate bond market over the past decade, but progress has been painfully slow. Bank lending accounted for 76% of all corporate borrowing in 2022, down from 82% ten years earlier. If this progress accelerated over the next decade or so, EU companies would be raising more than €500bn a year in the corporate bond market (almost double the amount in 2022), and the split between bank lending and bonds would be closer to 60/40 (roughly where France is today). This would enable banks to clear their balance sheets of loans that could be more sensibly provided by capital markets and focus instead on SME lending. It would also encourage the consolidation of the EU's fragmented and inefficient banking system, which would be boosted by the completion of banking union, the creation of a pan-European deposit guarantee scheme, and a single agency and management company for legacy non-performing loans.

viii) Venture capital: since 2021, the venture capital (VC) industry in EU has had a bit of a renaissance. EU member states such as Sweden and Finland have been the drivers of this growth, but the industry is still held back by fragmentation and a lack of scale. Backed up by more local pension fund money, tax incentives, and widened access to private capital for retail investors, the VC industry could roughly double to an average investment value of €90bn per year. This growth would enable European companies to access growth capital at scale in later stage rounds of fundraising, helping to drive the pipeline of EU scale up companies. If that sounds ambitious, it is in line with the kind of growth that VC investment activity in the EU experienced over the last three years when it increased from €26bn to more than €60bn between 2020 and 2022.

The growth potential in EU capital markets

It is well known that EU capital markets are not as developed as they could or should be, but what is often overlooked is the vast growth potential that they have. This section highlights the potential benefits of deeper capital markets to the EU economy and national economies in concrete and practical terms. It paints an optimistic vision of the sort of capital markets the EU needs to fully support the sort of growth, investment, and prosperity that it wants.

We analyse the huge but realistically achievable opportunity for growth in selected sectors of EU capital markets and in selected countries. We also take a look back and compare our current growth projections with those we made in previous reports.

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Fig.7 The growth opportunity for EU capital markets in selected sectors

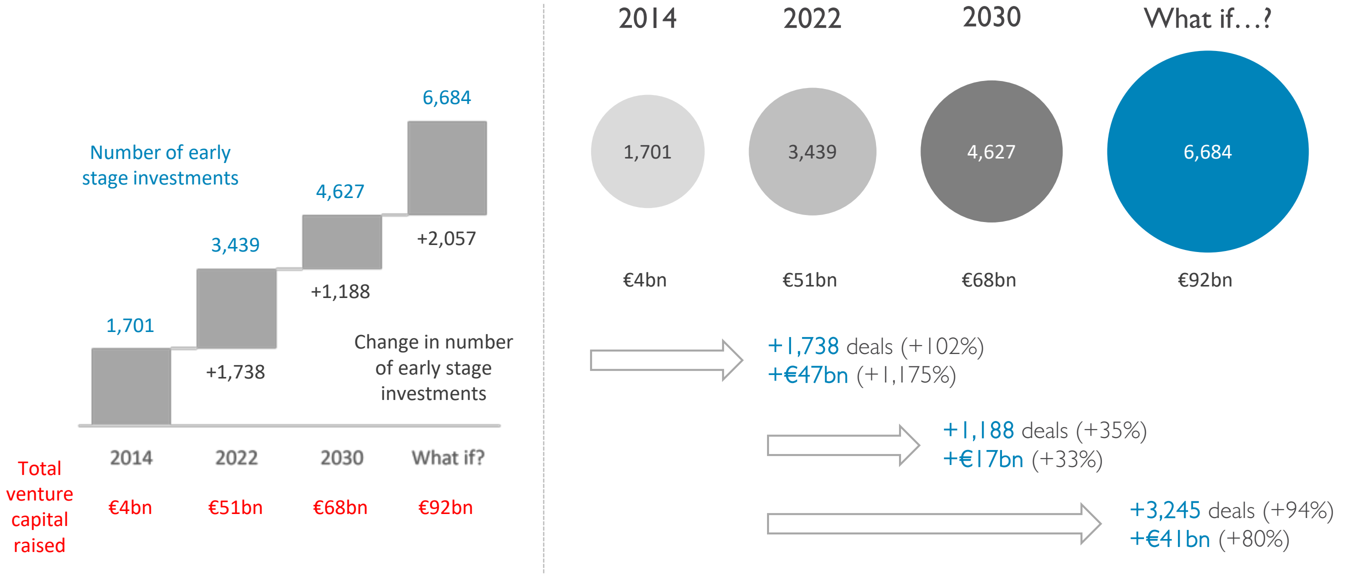
This chart shows the projected and potential growth in the number of capital market deals (IPOs, issued bonds, VC investments etc) in the EU and how much money they could raise per year in key areas of the capital markets.

		2014	2022	2030	What if?
IPOs +230 deals +€40bn per year +154%	*Number of deals* >>>	152	100	117	330
	Value >>>	€17bn	€26bn	€31bn	€66bn
Corporate bond issuance +277 deals +€202bn per year +61%		632	428	551	705
		€264bn	€330bn	€418bn	€532bn
Venture capital +3,245 deals +€41bn per year +80%		1,701	3,439	4,627	6,684
		€4bn	€51bn	€68bn	€92bn
Capital markets financing (Corporate bonds, equities, leveraged loans & VC) +4,425 deals +€468bn per year +67%		3,272	4,870	6,374	9,295
		€505bn	€698bn	€854bn	€1,166bn
Stock market +7,821 listed companies +€10.8tn in total value +104%		8,192	6,192	7,145	14,013
		€6.5tn	€10.3tn	€11.9tn	€21.1tn
Pools of long-term capital (Pensions & insurance assets) +€59,229 for each household +€11.8tn in total value +87%		€48,809	€68,777	€81,505	€128,006
		€9.3tn	€13.6tn	€16.2tn	€25.4tn

Source: New Financial

Fig.8 An example: measuring the growth potential for venture capital activity in the EU

This visualisation shows how we estimate the growth potential for venture capital activity in the EU.
Note: we use a three year rolling average for 2014 and 2022



Source: New Financial analysis of Preqin data

A focus on the potential

To measure the potential in terms of the number of additional companies raising capital and the total value raised, we start from how EU capital markets looked in 2014 (the year before CMU was launched). Fig.8 shows that the average number of companies raising VC money in the three years to 2014 was 1,701 with a total average EU-wide annual value of €4bn. In the three years to 2022, there were an average additional 1,738 companies raising venture capital with an average total value of just over €50bn.

Using these benchmarks, we estimate what EU capital markets would look like in 2030 based on the rate of growth between 2014 and 2022. For venture capital, we estimate that if it would continue to grow at the rate it has been growing, there would be an additional 1,188 companies raising capital per year with an average annual increase of €17bn (which would be 33% more than in 2022). This would be a significant increase, but it would not completely capture the potential that EU capital markets have when it comes to VC activity, and it limits our understanding of where EU capital markets are heading.

In order to fully capture what might be possible, we estimate the potential growth opportunity for capital markets in each economy and call this our 'what if?' scenario. We measure the value of deals (in this example, of VC deals) as a percentage of GDP for each EU member state and divide the 27 economies into quartiles. Within each quartile we calculate the weighted average value of activity as a percentage of GDP and assume that in each sector activity increases relative to GDP to the average level of the quartile above. For example, France is in the second quartile with a venture capital market of 0.4% of GDP. If it were to increase French VC activity to the average of the first quartile at 0.8% of GDP, it would see an increase in funding of around €9bn per year and 582 additional French companies raising venture capital. We repeat this exercise across countries and sectors to create a more ambitious but achievable vision for capital markets across the EU. For more detail, please click here.

A deeper pool

While the relatively small pools of long-term capital in many countries across the EU present challenges for policymakers, they also represent a huge opportunity for growth.

We analyse the potential growth in pools of long-term capital (funded pension assets and insurance assets) for each member state. To make this growth more tangible, we express it in long-term savings per household.

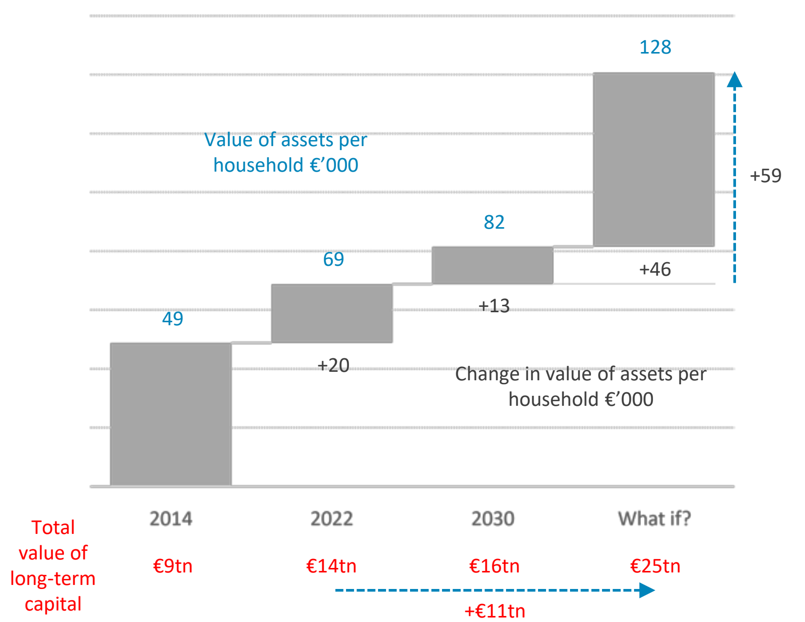
Fig.9 i) shows the growth potential in pensions and insurance assets in the EU. In the three years to 2014, the average value of assets per household was €49,000, increasing to around €69,000 in 2022. By 2030, we estimate that average long-term savings per household will grow by nearly a fifth to €82,0000. That is an additional €13,000 for each household in today's money.

But if each country had pools of capital as large as those a quartile above it, pension and insurance assets would nearly double to €128,000 per household (an increase of €59,000 per household compared to 2022). This translates into an additional €11 trillion in long-term capital in the EU that would significantly lower the future pensions burden on taxpayers and could be put to work in the wider EU economy.

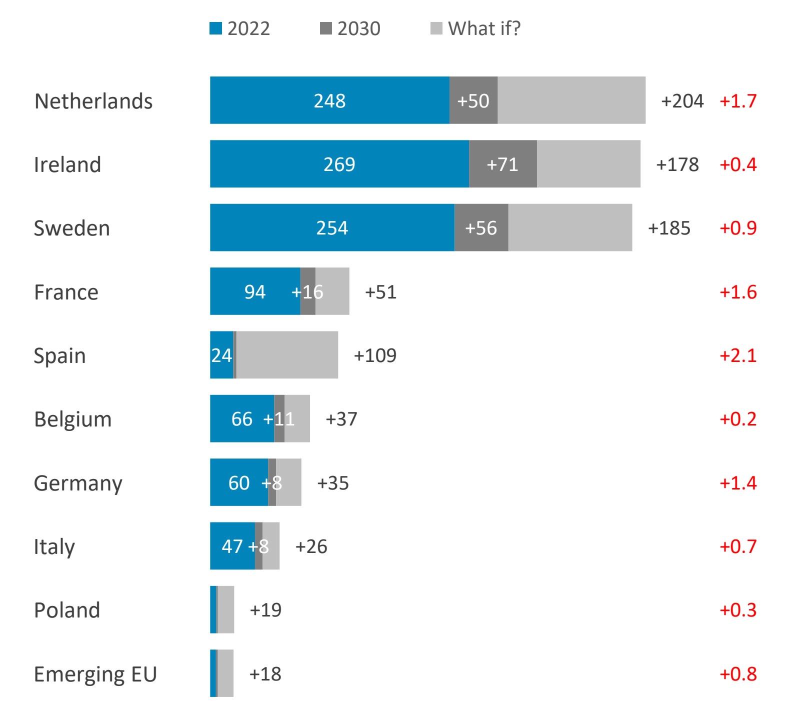
Fig.9 ii) shows that at a country level there is a wide range in the growth potential. Long-term assets per household would increase in today's money by €35,000 in Germany and €109,000 in Spain, while even the countries who are already in a good position (Netherlands, Ireland, Sweden) would see substantial growth ranging from €185,000 to €204,000 per household. In France, where the government tried to relieve the pension burden by raising the age of retirement, each household could benefit from an additional €51,000 (a total increase of €1.6 trillion in long-term capital).

Fig.9 The growth opportunity in pools of long-term capital

i) The growth opportunity in EU pensions and insurance assets, expressed in terms of additional average long-term savings per household in thousands of euros



ii) The growth opportunity in EU pensions and insurance assets, expressed in terms of additional average long-term savings per household in thousands of euros in a selection of countries, with the number in red showing the total additional capital in €tn under our 'what if' scenario



Source: New Financial analysis of OECD data

Ringing the bell

The number of new companies listing on stock markets is a simple but useful (and much used) indicator of the health of capital markets, and our analysis shows there is huge potential in the EU. Fig.10 shows the growth potential in the IPO market in terms of additional billions in funding and additional number of companies raising funds per year in the EU and in different countries.

As seen in Fig.10 i), the three years running up to 2022 saw a decrease in the number of companies issuing IPOs compared to 2014. At the same time, the value of deals increased by nearly €10bn. Based on the current rate of growth, only 17 more companies per year would IPO in the EU by 2030. The average value of total capital raised per year would increase by €5bn.

While this growth would be welcome, particularly after a couple of dismal years for the European IPO market, it is not really going to move the dial. In our 'what if?' scenario, the EU could see an additional 230 companies per year choosing to list on EU stock markets, translating into an additional €40bn in raised capital per year. This potential growth is larger than the total combined annual value for IPOs that we would see in 2030.

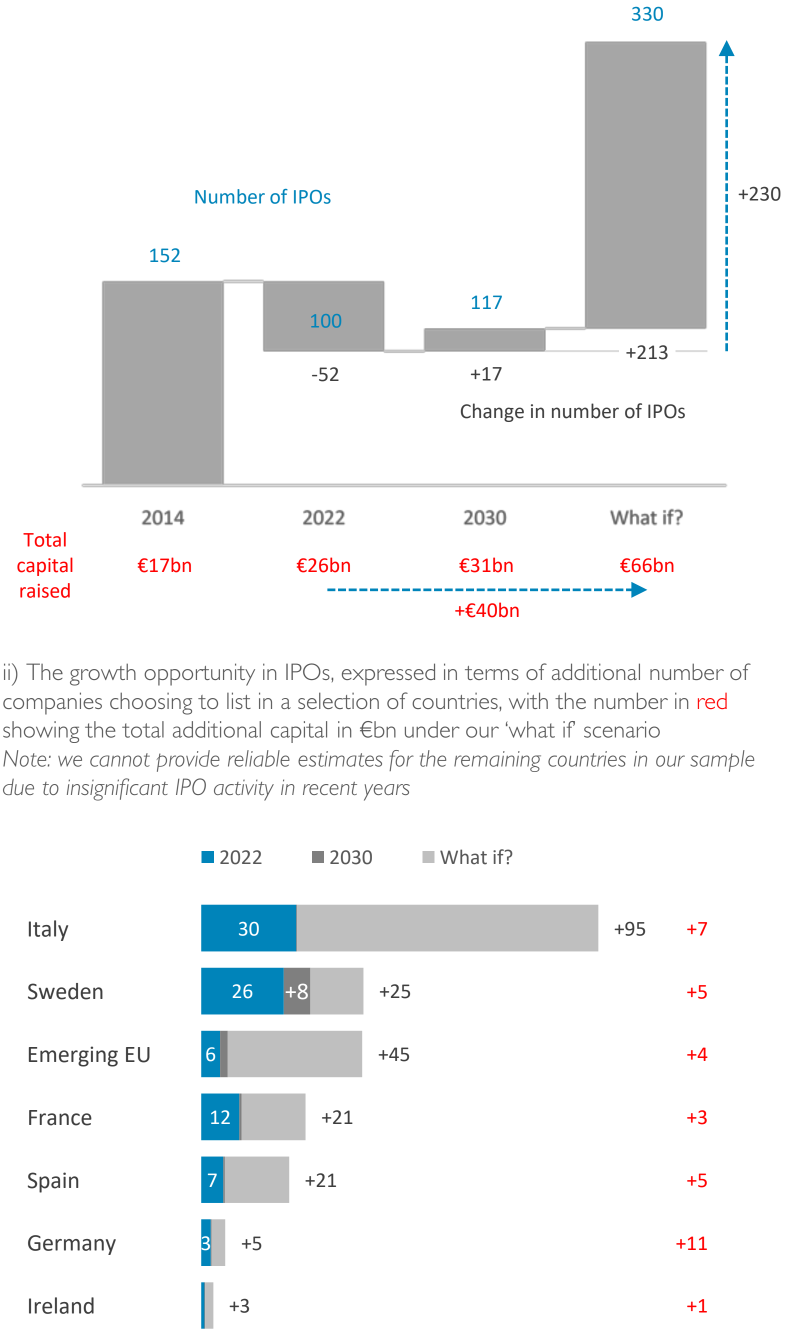
The potential for big EU economies is huge. Fig.10 ii) highlights how Italy could see an additional 95 companies per year raise an IPO, with an extra €7bn in value of annual issuance. Spain, France, and Germany could each see an additional number of IPOs ranging from 5 to more than 20, with the value going up to around €11bn. Smaller EU economies could benefit as well: the emerging EU including Poland, Hungary, and the Czech Republic could see an additional 45 companies raise an IPO with an extra €4bn in annual value.

Fig.10 The growth opportunity in IPOs

i) The growth opportunity in IPOs in the EU, expressed in terms of additional companies choosing to list

ii) The growth opportunity in IPOs, expressed in terms of additional number of companies choosing to list in a selection of countries, with the number in red showing the total additional capital in €bn under our 'what if' scenario

Note: we cannot provide reliable estimates for the remaining countries in our sample due to insignificant IPO activity in recent years



Source: New Financial analysis of Dealogic data

Room for growth

EU capital markets would look very different if more companies tapped into the corporate bond market rather than relying on bank lending alone. In the three years to 2022, the EU corporate bond market experienced a boom and then a bust, with a large increase in issuance in 2021 followed by a sharp decrease in 2022. Fig.11 shows how although corporate bond issuance has suffered due to rising interest rates, there is room for growth, along with significant opportunities for value creation for firms throughout the EU.

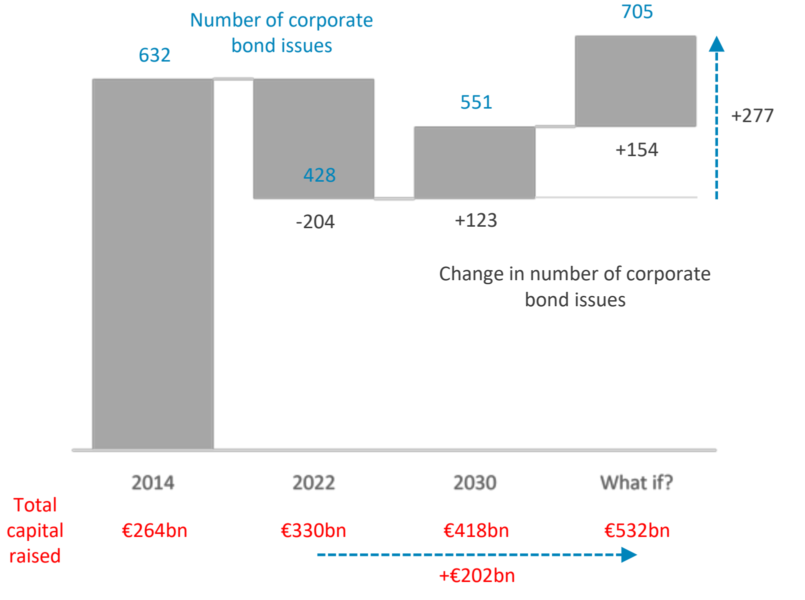
Fig.11 i) shows that in the three years to 2014, there were an average of 632 corporate bond issues in the EU raising nearly €264bn a year. In the three years to 2022, an average of 428 corporate bonds raised nearly €330bn a year. This is roughly a 25% growth in value but a decrease of a third for the number of corporate bond issues.

If the EU's corporate bond markets continues to develop at the same pace it has in recent years, there would be an additional 123 corporate bonds raising an extra €88bn per year by 2030. In our 'what if?' scenario, however, we estimate that nearly 300 extra corporate bonds could raise an additional €200bn per year. This would be more than a 60% increase in the value of corporate bond issuance, which would significantly reduce the EU's reliance on bank lending and free up bank balance sheets for lending to SMEs.

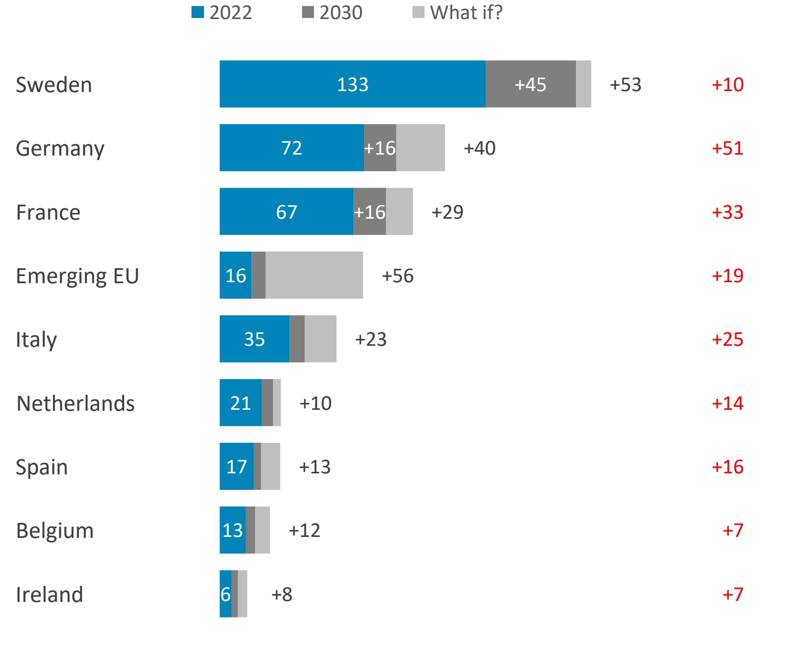
The number of bonds issued by companies in Germany and France could grow by 30 to 40 per country, with an additional combined value of more than €80bn between the two countries. In the emerging EU, an extra 56 corporate bonds could raise nearly €20bn per year. For companies in both small and large economies, having different sources of funding to finance borrowing would make for more flexible economies and distribute risk currently concentrated in banks.

Fig.11 The growth opportunity in corporate bonds

i) The growth opportunity in corporate bond issuance in the EU, expressed in terms of additional deals



ii) The growth opportunity in EU corporate bond issuance, expressed in terms of additional deals in a selection of countries, with the number in red showing the total additional capital in €bn under our 'what if' scenario



Source: New Financial analysis of Dealogic data

Solid foundations

Venture capital is a valuable source of funding for new and high potential companies, and the EU over the last few years has created a healthy environment for venture capital and early-stage investment. The EU's growth in venture capital proves that there is plenty of opportunity to grow across various sectors of the economy.

Fig.12 i) shows that in the three years to 2014, 1,701 companies closed VC deals and on average raised a total of €4bn across the EU. By 2022, the number of VC deals more than doubled to 3,439, with a whooping 1,175% increase in value to €51bn.

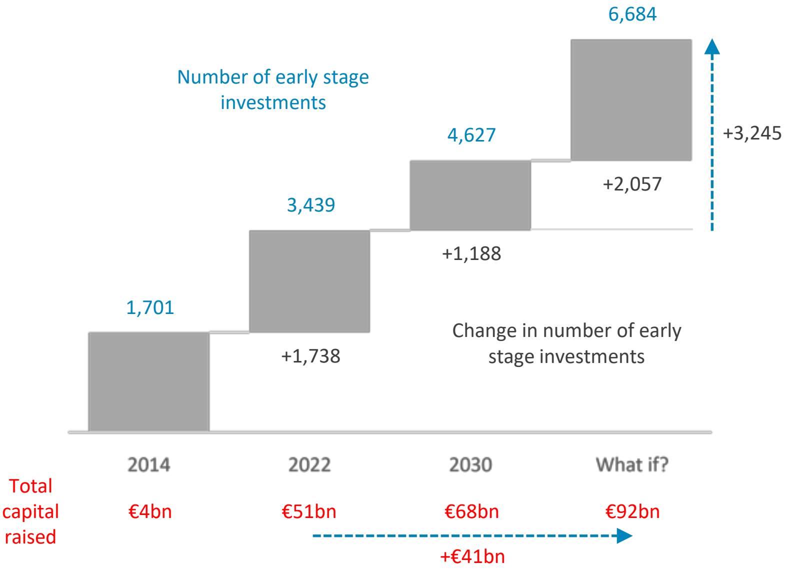
This dramatic increase in VC deals proves that the EU is capable of expanding capital markets financing at a quick rate. Driven by a healthy innovation culture in countries such as Sweden, the EU increased its global market share of venture capital investment and created the foundations for further growth in the years ahead.

If this growth continues, the EU could see an additional 1,188 VC deals raising an average EU total of €68bn per year by 2030. While this is a significant increase from 2014 (and even 2022), the EU can shoot higher and make itself an attractive location for not only home grown but foreign companies as well.

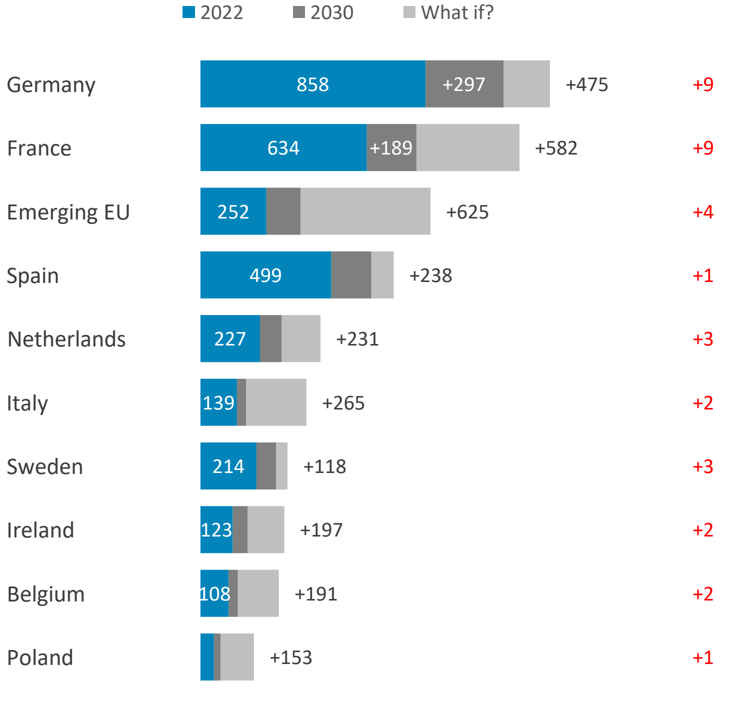
In our 'what if' scenario, nearly 6,684 companies across the EU could raise more than €92bn in VC money every year. Italy could see an additional 265 companies raise more than €2bn per year, while France could see an additional 582 companies raise nearly €10bn in additional venture capital. The room to grow for EU member states is significant, even after already impressive growth.

Fig.12 The growth opportunity in venture capital activity

i) The growth opportunity in venture capital activity in the EU, expressed in terms of additional deals



ii) The growth opportunity in EU venture capital activity, expressed in terms of additional deals in a selection of countries, with the number in red showing the total additional capital in €bn under our 'what if' scenario



Source: New Financial analysis of Preqin data

Bridging the gap

One of the main goals of CMU is to promote SME and growth markets so that it becomes easier for small and medium-sized companies to raise capital in public markets. In our 'what if?' scenario, we identify significant but realistically achievable growth potential in these markets for every country in the EU.

Fig.13 i) shows that there were nearly 2,000 companies that were listed on SME and growth markets across the EU in the three years leading up to 2022. In terms of value, those markets were worth on average of €126bn per year. The reason we do not include the three years to 2014 in our analysis is due to the minimal presence of SME and growth markets in the EU during those years.

If SME and growth markets continue to grow at the pace they did in recent years, they could see an additional 936 companies listed on them. Their value would be €50bn higher than currently. While this growth would be notable and build on good progress over the last few years, it is nowhere near the vast potential that we see for SMEs in the EU.

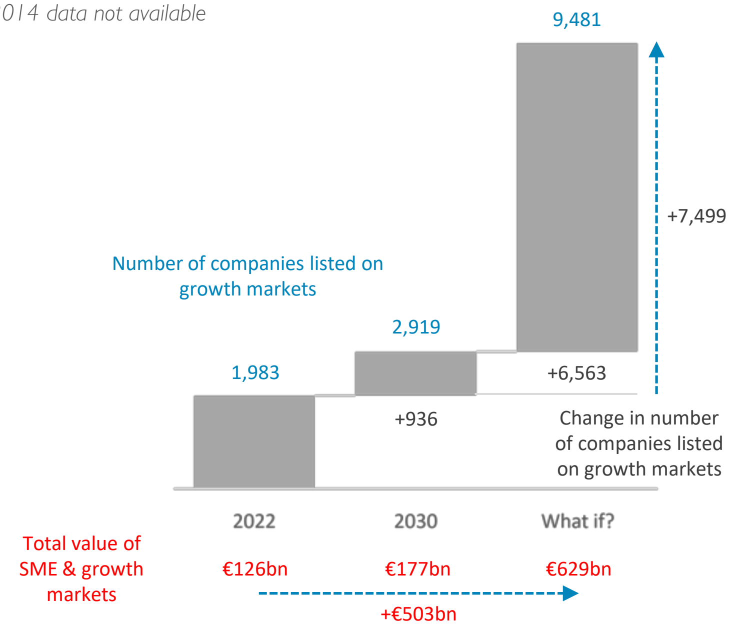
Our 'what if?' scenario shows that European SME and growth markets could be worth €500bn more than they are now with nearly 7,500 more small and medium-sized companies listed on those markets throughout the EU.

At a country level, Poland and France could each see around 1,400 more SMEs listed on their exchanges. They would have an additional combined value of more than €100bn. This kind of growth is possible even in countries like Sweden, where there already is a vibrant early-stage and start-up culture. In our 'what if?' scenario, Swedish growth markets could see an additional 905 companies and an extra €122bn in value.

Fig.13 The growth opportunity in SME & growth markets

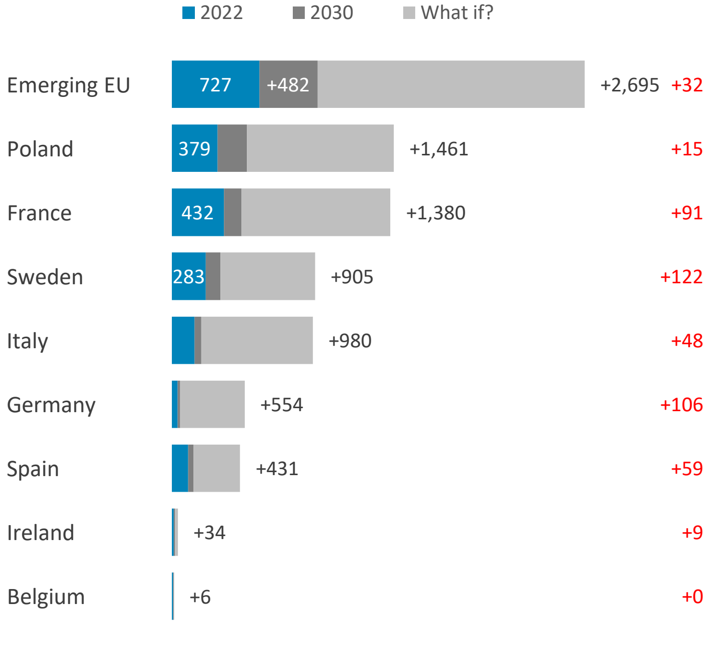
i) The growth opportunity in SME & growth markets in the EU, expressed in terms of additional companies choosing to list

Note: 2014 data not available



ii) The growth opportunity in SME & growth markets, expressed in terms of additional number of companies choosing to list in a selection of countries, with the number in red showing the total additional capital in €bn under our 'what if' scenario

Note: we cannot provide reliable estimates for the remaining countries in our sample due to insignificant SME & growth market activity in recent years



Source: New Financial analysis of data from the WFE and national stock exchanges

Accelerating the transition

The EU will need to raise significant amounts of capital to meet its ambitious net zero transition goals. This money cannot come from governments and bank lending alone. Companies in particular will need to make use of capital markets financing to fill the gap. The good news is that since 2014, ESG corporate bonds (which historically have mainly consisted of labelled green bonds) have exploded in issuance - but there is still room for growth.

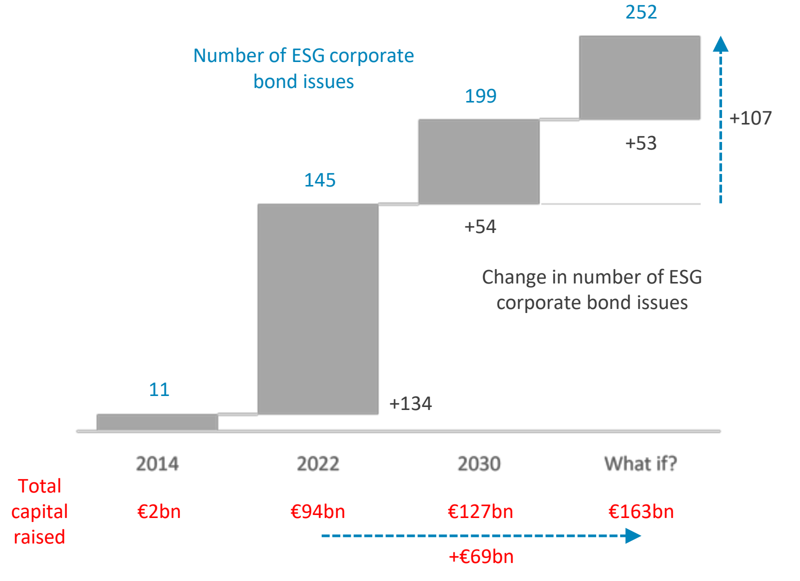
From 2014 to 2022, the average annual number of ESG corporate bonds increased from a little more than 10 to nearly 150 per year. That is an increase of more than €90bn that is raised every year across the EU via ESG corporate bonds. Most of this growth can be attributed to labelled green bonds, which raise capital for clean energy projects and for lowering carbon emissions. Social bonds and sustainability-linked bonds have also driven this growth.

If ESG corporate bond issuance were to keep growing at the rate it has, we would see an additional 54 ESG corporate bonds with an additional total value of more than €30bn per year by 2030. This increase in issuance is much needed for the EU to meet its climate goals, but more can and should be done.

In our 'what if?' scenario, the EU could see an additional 107 ESG corporate bonds raising an extra €69bn per year directly supporting the transition and building a more just society. At a country level, France and Germany combined could raise an additional €26bn in ESG corporate bonds per year. This sort of financing could remove stress on government budgets. And in the emerging EU markets, there could be an additional 5 ESG corporate bonds raising €4bn in transition, green, and social capital per year - helping to transform coal-dependent countries such as Poland into centres of renewable energy production.

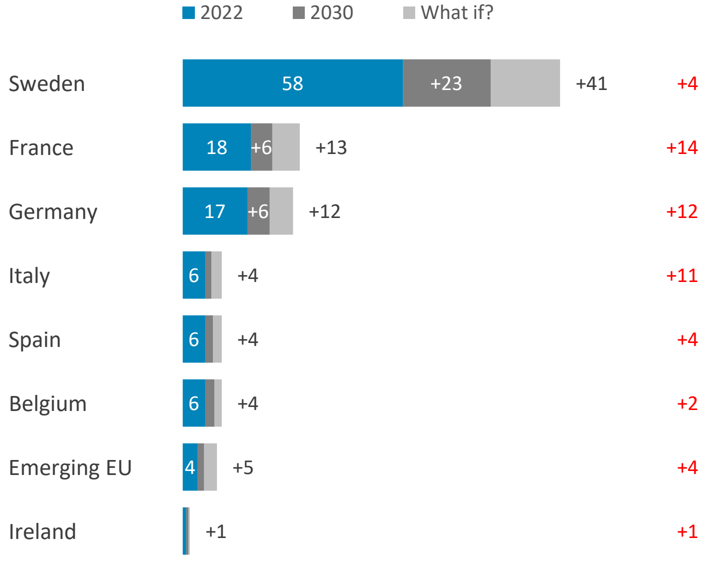
Fig.14 The growth opportunity in ESG corporate bonds

i) The growth opportunity in ESG corporate bond issuance in the EU, expressed in terms of additional deals



ii) The growth opportunity in EU ESG corporate bond issuance, expressed in terms of additional deals in a selection of countries, with the number in red showing the total additional capital in €bn under our 'what if' scenario

Note: we cannot provide reliable estimates for the remaining countries in our sample due to insignificant ESG corporate bond issuance in recent years



Source: New Financial analysis of Dealogic data

The road not taken

In previous reports we made various projections about what capital markets in the EU would and could look like by 2030 and beyond. After a number of 'once-in-a-generation' events that have shaken the EU (and the world) in recent years, we thought it would be interesting to take a look back at our previous projections and see how they have fared.

Fig.15 shows our current 'what if?' projection for two critical areas of the capital markets (the potential total value of long-term capital and annual value of IPOs in the EU) and how they compare with our 'what if?' projections that we made in 2022 and 2019.

Fig.15 i) shows that the steady growth in long-term capital in the EU seems to be slowing. Our projection for the value that long-term capital in the EU could reach, now at €25tn, is lower than in 2022 and 2019. This is not great news, as pools of long-term capital are a key building block for well-functioning capital markets.

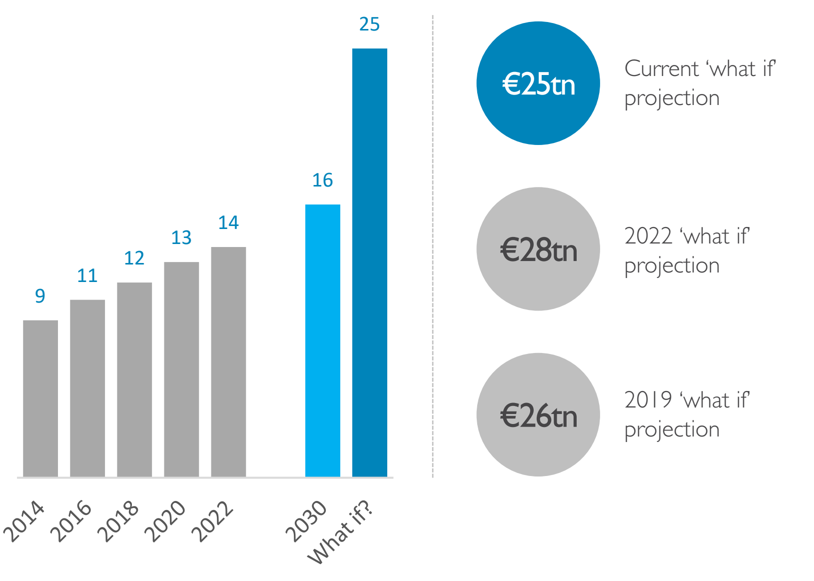
Fig.15 ii) shows that while our current 'what if?' projection for the annual value of EU IPOs at €66bn is a little lower than it was in 2019, it is twice the size it was in 2022. This is because of the breakout year that was 2021 which showed that there is appetite, demand, and even excitement in European equity markets when the conditions are right.

Both charts show that current growth rates and the levels of activity that we might reach by 2030 will not move the dial. More ambition is needed for the EU to have the capital markets it needs to support the European economy along with companies in all corners of the continent, jobs, innovation, and growth.

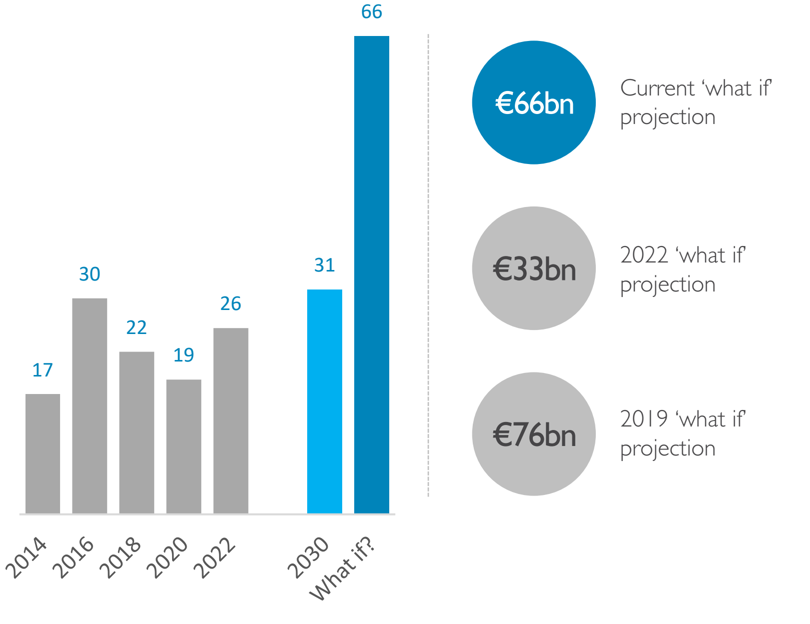
Fig.15 How have previous projections fared?

The two figures below compare our current and previous growth projections for two critical areas of the capital markets in the EU.

i) Pools of long-term capital: historic growth, current projections for 2030 and our 'what if' scenario, and previous projections, in €tn

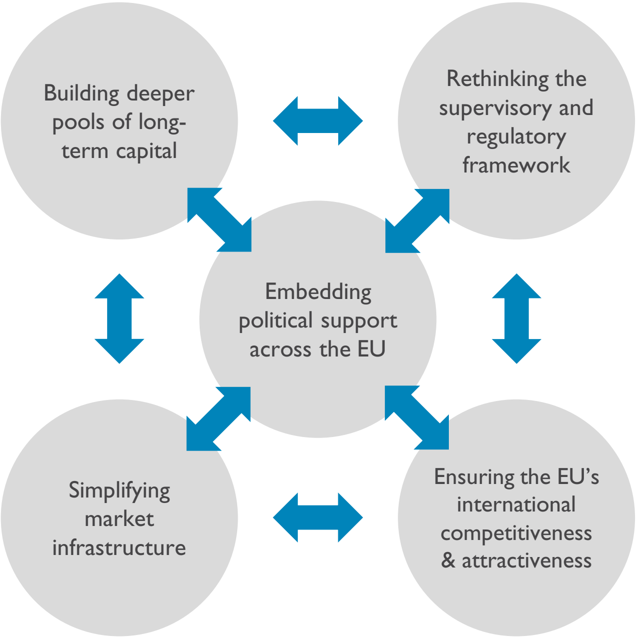


ii) IPOs: historic growth, current projections for 2030 and our 'what if' scenario, and previous projections, in €bn



Source: New Financial analysis of OECD and Dealogic data

Fig.16 How to drive growth and integration



A new sense of urgency

The EU cannot sit back and relax. It is time for member states, EU authorities, and the wider banking and finance industry to inject more urgency across Europe into building bigger and better capital markets. This report has highlighted the huge growth potential for EU capital markets. In order to achieve this growth, we think the EU should focus on five 'first principle' problems (Fig.16) as part of a potential CMU 3.0 over the next decade:

1) **Building deeper pools of long-term capital:** deep pools of long-term capital such as pension and insurance assets are the starting point for deep and effective capital markets, but pools of capital in the EU are much smaller than in comparable economies.

2) **Rethinking the supervisory and regulatory framework:** the EU cannot have the capital markets it needs with 27 different versions of the single rulebook or 27 different markets supervisors working on reforms at sometimes such a slow pace that often the problem has moved on by the time the EU is ready to implement any changes.

3) **Simplifying market infrastructure:** if you were designing the European market from scratch, it probably would not look like it does today. With too many stock exchanges, trading venues, and clearing and settlement houses, it is not a surprise that it is difficult for EU capital markets to achieve scale.

4) **Ensuring the EU's international competitiveness and attractiveness:** bigger and better EU capital markets do not just make it more attractive for European companies to use the capital markets - the EU cannot be a global superpower without them.

5) **Embedding political support across the EU:** the EU needs a concerted push for a better understanding of why bigger and better capital markets are a must, not an option, and combine EU-level actions with member state engagement to accelerate reforms and build capacity from the bottom up.

1) Building deeper pools of long-term capital

Deep pools of long-term capital such as pensions, insurance assets, and direct retail investment are the starting point for deep and effective capital markets, but pools of capital in the EU are much smaller than in comparable economies and concentrated in just three EU economies. Shifting more savings from bank deposits to investments and starting to build pension assets would deploy more capital to support the economy, jobs, and growth.

The European pensions problem: the EU's problem with long-term capital is first and foremost a pensions problem. Insurance assets in the EU are roughly comparable in size to other economies and account for nearly two-thirds of the long-term capital in the EU. The real problem is that pension assets, which face far fewer restrictions on what they can invest in, are tiny in the EU. A few common essential building blocks could make a difference such as introducing mandatory funded pensions and auto-enrolment, offering good (tax) incentives to get people to save more for their retirement, adopting a collective approach with efficient vehicles, and building political and public support for reform. With the Netherlands, Denmark, and Sweden there are three really good examples of countries in the EU that have developed deep pools of long-term capital thanks to healthy and sustainable pension systems.

A shift in culture: widening retail participation in European equity markets presents a huge opportunity for individuals to increase their long-term financial wellbeing; for issuers and the economy to connect with households in a new way; and for the capital markets and the financial services industry to reconnect with millions of households in every corner of Europe and help them make the most of their money. Retail participation can help create a virtuous circle of investment and growth. The EU's retail investment strategy is an important step in empowering retail investors, but it needs more ambition to change the European culture around money and finance rather than just focusing on consumer protection. There is an opportunity to think about retail investment and private pensions saving as two sides of the same coin.

Unlocking tied-up capital: member states and the EU parliament should swiftly vote through the changes to Solvency II that were provisionally agreed on and published following the trialogue negotiations last year. Cutting the risk margin for insurers will unlock billions of euros that insurers can invest in equities as well as key projects such as infrastructure or green technology. By creating the right vehicles, the reforms can also give access to private capital and other illiquid assets for individuals and smaller schemes. Returns from those assets can be as much as 5% a year higher than public markets but they are still off limits to most individuals.

The right balance: too often, a narrow understanding of consumer protection leads to the exclusion of retail investors from very sensible assets and activities in the capital markets. The good news is that policymakers and regulators appear to be moving on the issue and actively consult on removing barriers to retail participation. There will be some stumbling stones and pushback, as more people taking more risk will lead to some people losing money on an investment, but there are sensible balances to be struck.

Better understanding and better access: better financial literacy and education on its own will not automatically lead to more engagement by individuals and households with the capital markets, but wider retail participation in equity markets is impossible without it. Three quarters of EU citizens are unable to answer more than three of five financial knowledge questions correctly, there is a lack of trust in banking and finance, and a lack of understanding of how the industry works and its impact on people's everyday lives. A concerted programme at scale at all levels (in schools, in workplaces, and at important moments in lives via financial health checks); a better understanding of basic concepts of (inflation-adjusted) returns, investment, and risk; and a change in the way the industry talks about itself would increase levels of engagement in investment and capital markets.

2) Rethinking the supervisory and regulatory framework

One of the inconvenient truths of deeper and more integrated capital markets in the EU is that while you cannot magic them out of thin air with the creation of a single market supervisor, you cannot also have a fully integrated market with 27 different versions of the single rulebook or 27 different markets supervisors. Given the clear political decisions taken in recent years, in most areas of activity supervision will remain at a national level, but that should not stop the EU from creating a framework that is fit for purpose.

Rethinking the point of regulation: the EU needs to change its overall approach to what regulation can and cannot do. Regulation is not an end in itself and not all problems are regulatory in nature or can be solved only by regulation. For example, establishing uniform requirements for issuers of green bonds is helpful, but what matters more is making it easier for companies to raise green capital and deploy this capital via 'oven ready' projects that are part of a healthy project pipeline. And while complex markets may need complex regulation, focusing too much on the detail can make regulators and policymakers miss the bigger picture - see MIFID II's rules around the unbundling of research costs reducing the availability of research overall.

Redefining the overall framework: the EU needs to make its framework fit for a new world. Technologies such as artificial intelligence are changing the digital landscape, Russia's aggressive actions in Ukraine and other geopolitical tensions caused shockwaves across Europe and the world, and the climate crisis paired with issues around energy security are already requiring the banking and finance industry to play a much bigger role. The future regulatory framework of the EU should assess the cumulative impact of reforms that followed the 2008 global financial crisis, be more flexible, ensure stronger cooperation between national and EU-level supervisors, and have regular formal reviews rather than the constant and ongoing tweaking of every little corner of the framework.

A new strategy: any new legislation and regulation should be (i) tested against a set of objectives and desired outcomes (ii) combined with non-legislative measures which nudge individuals and firms - particularly where barriers are cultural and behavioural, such as (private) pensions saving and retail participation in the capital markets and (iii) focus on interoperability and on ensuring regulation converges between the EU and critical third countries such as the UK and US.

Tracking and reviewing progress: mechanisms that effectively monitor progress against objectives and promote accountability are key. So far, volume of legislation and regulations has often been used to benchmark progress. It is much more relevant to track outcomes (which the European Commission does in its regularly published set of CMU indicators). However, more formal monitoring mechanisms could be set up to measure progress and ensure accountability at both an EU and national level. Ecofin or another group could regularly monitor a clearer and shorter set of targets with defined milestones and deadlines, and the EU could work with member states to benchmark them against their neighbours and peers around the world.

More agility: there needs to be better alignment between the speed of regulatory changes and the speed at which the markets move and (digital) innovation is taking place. For example, when the EU announced its markets in crypto-assets regulation (MiCA), it aimed for the directive to be technology neutral, but this meant 'technology neutral in two years from now because that is how long the process will take'. In the meantime, decentralised finance and new digital assets emerged. The EU should follow a more dynamic and proactive approach to regulation and reform by establishing an ongoing review and accountability mechanism and streamlining the process of reforms.

And yet…: given the clear political decisions taken in recent years, in most areas of activity, supervision will remain at a national level for the foreseeable future. But the EU cannot have the capital markets it needs with 27 different versions of the single rulebook or 27 different markets supervisors. The focus of ESMA and EIOPA should for now be on the supervisory convergence agenda, particularly in terms of ensuring a more consistent application of the single rulebook, developing a stronger common supervisory culture, better supervisory coordination, and improving risk prioritisation and outcomes-based supervision. But the relative novelty of sustainability and digitisation presents an opportunity for national supervisors across the EU to work more closely together and with ESMA and EIOPA to develop entirely new frameworks. Then, discussions should start on which sectors, firms, or activities need to be supervised at an EU level and which at a national level.

3) Simplifying market infrastructure

The complex patchwork of European equity markets is a huge obstacle to building bigger and better capital markets. We can tinker at the edges with the detail of regulation, but so as long as Europe has 22 different stock exchange groups operating 31 different exchanges for listings, 34 exchanges for trading, and 39 different central clearing counterparties (CCPs) and central securities depositories (CSDs), not much will change.

A full audit: EU capital markets are on the whole small and fragmented. A more integrated market infrastructure with more transparency and competition would increase efficiency, liquidity, economies of scale, and lower costs for companies, investors, and market participants. The EU should work together with member states to conduct a comprehensive audit of the inefficiencies and barriers to competition in different markets at both a national and cross-border level.

Consolidation and competition: for as long as there are 22 different stock exchange groups in the EU operating 31 different exchanges for listings, 34 exchanges for trading, and 39 different CCPs and CSDs, CMU is little more than a pipedream. There is not enough competition in the right places, and between exchanges it is mainly restricted to trading volumes in the largest stocks. A small number of exchange blocs each having an umbrella operator with a series of 'local' markets like Nasdaq or Euronext, and a system of cooperation like airline code-sharing, would boost efficiency and competition for listings, trading, data and clearing. At the same time, policymakers should lift any barriers to competition and harmonise the rules between and within each block. These decisions will be tough but are necessary.

A single platform: the key to well-functioning markets is consistent and timely information and there is plenty of room to improve, centralise, standardise, and simplify information. The move toward a consolidated tape is a big step forward, but the EU needs to ensure that its ambition does not stop there. Ultimately, the EU needs a single pan-European platform for filing and distributing comparable information on issuers (including data on SMEs and growth companies). Over time, this platform could be expanded to a central portal for corporate governance and shareholder voting, reducing the bureaucracy and costs of cross-border investing.

A single information hub: setting up a single pan-EU information hub for funds and other financial services such as crowdfunding or insurance would increase transparency, efficiency, competition, cross-border activity, and reduce fragmentation. The platform could also provide asset managers and other market participants a single point of entry for registration, notification, marketing, and tax reporting for all their operations across the EU. The EU should also push forward with an EU wide shareholder definition and utilise technology for exercising voting rights.

The wider ecosystem: the EU and member states should also focus on improving the ecosystem surrounding the different markets by working more closely with existing providers. Targeted public co-investment, perhaps in the form of a pan-European pre-IPO / IPO fund, would add critical mass to the smaller end of equity markets and help recapitalise companies in the wake of Covid and Russia's war in Ukraine. In the meantime, developing a new regime for direct listings and exploring the concept of 'hybrid markets' would provide companies with a wider range of options.

4) Ensuring the EU's international competitiveness and attractiveness

The EU has an ambition to be a global superpower, but the EU's capital markets are punching below their weight. Bigger and better EU capital markets do not just make it more attractive for European companies to use the capital markets and provide funding and capital to help meet the big challenges the EU is facing - the EU cannot be a global superpower without them.

Striking the right balance: in a new global reality of deglobalisation and rising geopolitical tensions, the EU needs to strike the right balance between protecting its interests and autonomy and remaining open. A strong internal capital market and capital markets that are open to the world and global investors do not have to be mutually exclusive. The EU needs remain open to international investment and capital flows and ensure a level playing field for its companies and markets at the same time. This is not easy, but getting it wrong would send the wrong message to global investors (and, possibly, undermine the international role of the euro).

A new world order: despite a decrease in its share of global GDP and global capital markets activity, the EU remains one of the three global economic superpowers along with the US and China. The EU is leading in areas of capital markets activity such as sustainable finance, investment funds, and insurance and should build on these existing strengths and expand its cooperation with other countries where it has less capacity. The response to Russia's invasion of Ukraine showed that the EU can achieve a lot on its own but it can achieve even more when it collaborates with partners such as the UK or the US. As during the immediate post-Brexit era, the EU finds itself with an opportunity to reconsider its strengths and weaknesses around banking, finance, and capital markets.

The wider world: the EU cannot solve all of its problems on its own and will need partnerships with other markets. It should continue to cooperate and strengthen its relationship with other developed markets such as the US, UK, Japan, and Canada; rebuild its relationship with Switzerland; and increase its financial, trade, and economic diplomacy and 'soft power' offensive with faster growing markets like China and India where possible. The EU should resurrect its work on reforming equivalence to develop a more consistent, predictable, and sustainable global framework. The work could build on existing international working groups bringing together supervisors, regulators, and industry representatives and focus on economics and outcomes rather than politics. In particular, the EU should work closely with markets like the UK and Switzerland on a co-ordinated response to the shift to T+1 settlement in the US. And, in time, it might consider allowing firms in other like-minded markets such as Switzerland and the UK to 'opt-in' to CMU and other EU initiatives.

A pressing matter: the EU is an effective force on the global stage. It is the world's largest trading bloc, the world's largest single market, and the euro is the world's second most used currency for trade, finance, and reserve building. But a lot of this is at risk if Europe becomes a continent that cannot maintain high living standards for its citizens, cannot support high growth companies and innovation, and misses its own ambitious climate targets. Bigger and deeper capital markets in the Europe are directly linked to the EU's position on the global stage.

5) Embedding political support across the EU

Not enough politicians are aware of the crucial role capital markets can play, and those who know do not talk enough about it. The EU needs a concerted push for a better understanding of why bigger and better capital markets are a must, not an option, to build political support across the continent. The EU and individual member states have all the tools that they need to build bigger and better capital markets at their disposal - they just need to stop admiring the problem and start doing something about it.

A thorough plan (and a commitment to delivering it): the long-term commitment of members states is key for progress as building deep and integrated capital markets takes time and requires well-functioning national markets. While CMU has become more of a priority in recent years, there still seems to be a disconnect between what is said when national leaders meet in Brussels and what they deliver when they are back in their capital. Moving the dial on capital markets in the EU will require concrete proposals, clear deadlines, monitoring and enforcement mechanisms, and collaboration with national governments, regulators, and other stakeholders. The heads of states should clearly endorse agreed measures, implement them, and explain to their citizens in simple terms why they are important and how people, households, families will benefit.

A better case: over the past year, the conversation around CMU has moved up the political agenda with leading regulators, policymakers, and politicians highlighting the importance of bigger capital markets in achieving the EU's goals - see Christine Lagarde's much-cited speech on the need to developing capital markets in Europe. But the European banking and finance industry needs to double down on its efforts to show how capital markets can work for the overall economy. CMU seems to be everyone's fourth priority, but without bigger capital markets, many of the EU's other priorities and problems will not get solved.

A better narrative: CMU is one of our favourite topics at New Financial, but to most people in the EU, it either means nothing or remains an abstract, complex, and technical project. There needs to be a better narrative that frames the benefits of bigger and better capital markets more in simple and accessible terms along the lines of 'what does CMU mean for jobs, investment, and growth in your country / region / constituency'.

Building capital markets from the bottom up: many of the big levers to drive growth in capital markets across the EU can only be pulled at a national and not an EU level. These areas include pensions, taxation, and addressing the debt / equity bias. Building bigger, deeper, and more integrated capital markets in Europe requires a combination of EU-wide 'top down' measures to encourage harmonisation and national-level 'bottom up' measures to increase capacity. The EU cannot build capital markets union on its own, but it can help facilitate - perhaps with the help of multilateral organisations such as the Eurogroup - for example by evaluating where every member state stands and sketching out sensible next steps for them.

A different approach: the EU needs to change the way it does policy and takes decisions. For many years this has involved very technical and specialist work isolated from the political reality in member states and the day-to-day priorities and policies of national governments leading to unintended consequences and contradicting outcomes. The EU should do better in identifying what is realistically and politically achievable in each country and within which timeframe; what are the concerns of different member states; and how EU policies in in banking and finance fit with other policy areas at the EU and national level and with the priorities of national governments. At the current pace, it will take decades for CMU to become a reality, but the EU does not have that kind of time. That said, CMU has always been a long-term project and much of the criticism reflects the fact that in the EU there can be a tendency to overestimate what can be achieved in a year but to underestimate what member states can achieve over a longer timeframe when they work together.

A complementary role

Bigger and deeper capital markets can bring many benefits to the European economy and citizens in terms of investment, jobs, and growth. In the face of current social, economic, and geopolitical challenges, this has become even more urgent. Here is a selection of some of the potential benefits of bigger capital markets in Europe:

1. **A wider range of funding:** capital markets provide a valuable additional source of financing for EU companies that complements traditional bank lending and provides companies with a wider range of sources of potential funding. This reduces the economy's reliance on bank lending and enables companies to diversify both the sources of the capital they use and the terms over which they borrow.

2. **Economic resilience:** capital markets help increase the 'shock absorption' capacity of the economy. The impact of any downturn is transmitted less quickly and directly to individuals in economies with more developed capital markets than those that rely more on bank lending, and they tend to recover quicker.

3. **Access to capital:** capital markets offer the right companies the ability to raise a larger amount of capital at a lower cost and for a longer period than borrowing from their bank. Through equity financing they provide high potential companies - the sort of companies that Europe needs to drive growth, innovation and jobs - with risk capital that banks are not equipped or designed to provide.

4. **Increase bank lending capacity to SMEs:** capital markets are not a realistic option for most SMEs, but wider use of capital markets by companies that are large enough to access them can help free up bank balance sheets and enable banks to focus on lending to smaller companies that need it the most.

5. **Capital allocation and standards:** capital markets improve the 'allocative efficiency' of capital by effectively crowdsourcing funding to a wide range of investors and channelling investment to those companies that can make the best use of it. The need to compete for capital and to be accountable helps improve discipline, operational standards, corporate governance, performance, and transparency.

6. **More flexible:** while market disruption can make capital raising come to an abrupt halt, capital markets rebound faster than bank lending. The flow of gross new bank lending in the eurozone fell by a nearly a fifth from 2008 to 2022, but issuance in European bond markets has doubled relative to GDP since 2007.

7. **Long-term returns:** markets can be volatile in the short term but investing in capital markets across a range of assets over the long term generates higher returns than keeping savings in the bank, providing a better future income in retirement. Long-term pension savings also reduce the future economic burden on taxpayers and government budgets and help address the demographic time bomb faced by the EU.

8. **Longer-term investing:** capital markets provide long-term investors such as pension funds and insurance companies with a wider range of assets to invest in that better match their liabilities. Annual pension contributions by employers and employees add up to billions a year that can be put to work supporting the economy in much needed areas such as investment in infrastructure and innovation.

9. **Wealth creation:** capital markets democratise wealth creation by enabling a wider range of people to invest in high growth and successful companies through their investments and pensions.

10. **Sustainable growth:** Europe needs to invest around €1 trillion a year over the next few decades to address climate change and finance a transition to a more sustainable economy. Capital markets can close the funding gap by providing capital at scale through a wide range of instruments.

NEW FINANCIAL
Rethinking capital markets

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Building EU capital markets from the bottom up

Our sample:

We analyse size and depth of capital markets in the following 26 different sectors of activity in all EU member states.

- **Pools of capital:** pensions assets, insurance assets, household retail investments (excluding pensions, insurance, cash deposits & unlisted equity)
- **Equity markets:** stock market value, initial public offerings, secondary equity issues, convertible bonds, SME growth markets, equity trading volumes
- **Bond markets:** corporate bond market value, bond market value, investment grade bond issuance, high-yield bond issuance, bank lending relative to corporate bonds
- **Loans & securitisation:** value of outstanding securitisation, securitisation issuance, leveraged loan issuance
- **Assets under management:** assets under management, all investment funds by domicile, domestic investment funds by domicile
- **Corporate activity:** M&A by target nationality, M&A by acquiror nationality, domestic M&A
- **Private equity, venture capital & crowdfunding:** private equity activity, venture capital activity, private equity fundraising

Measuring depth: in each sector and country we measure the value of activity as a percentage of GDP on a three-year rolling basis from 2004 to 2022 to iron out the annual volatility in capital markets. To enable a comparison in depth between different sectors, we rebase these percentages in each sector to the EU28 average. We then again rebase the average of all sectors to the EU27 average. We call this the 'EU' average and do this to allow for comparisons with previous reports where we used the EU28 average. For example, the value of stock markets in the EU in the three years to 2022 is 71% of EU GDP. We rebase this to 100, meaning that a country with a score of 50 has a stock market that is half as deep relative to GDP as the EU average, and one with a score of 200 is twice as deep. To reduce distortions, we cap each metric at two standard deviations from the mean for every country.

Measuring growth potential: in each sector and country we estimate the growth potential in terms of the number of additional companies that could get funding, how much they could raise, and as a percentage increase on the current level of activity. In each sector we rank each member state by the value of activity as a percentage of GDP and divide them into quartiles.

- **2030:** for each country we estimate the growth in selected sectors of capital markets until 2030 based on a combination of the historical annual growth rate in real GDP over the past 20 years and the historical annual change in the depth of capital markets relative to GDP over the past 15 years (depending on data availability).
- **What if?** We then estimate the potential growth opportunity for capital markets in each economy by assuming that in each sector activity increases in depth to the average level of the quartile above. For countries already in the top quartile in a particular sector, we assume that activity has the realistic potential to grow at half the weighted average rate of less developed markets. For example, if a country was in the third quartile for IPOs, what would its IPO market look like if it were as deep as the average of countries in the second quartile? We then translate this growth into the potential number of additional IPOs a year based on the average value of IPOs across the EU in the past.

There is no perfect way to estimate growth potential in capital markets and our approach has obvious limitations. However, we think our approach creates a simple, realistic, and achievable benchmark for potential growth. There is no reason why a country should not be able to move up into the quartile above in a particular sector. We think this methodology may underestimate the growth potential for countries that are towards the top of their quartile and overstate the growth potential for countries towards the bottom of each quartile. In any case, we would stress that these numbers are not a growth forecast but a directional and realistic indicator of what could be achieved.

Fig.17 The growth opportunity in pools of long-term capital

The growth potential in pools of long-term capital (pensions and insurance assets), by country

	2014		2022		2030			What if…?		
Country	€bn	Assets per household (€)	€bn	Assets per household (€)	Growth (€bn)	Growth (%)	Additional assets per household (€)	Growth (€bn)	Growth (%)	Additional assets per household (€)
Austria	121	31,747	154	37,651	23	15%	5,501	262	170%	64,066
Belgium	298	63,328	341	66,468	57	17%	11,087	191	56%	37,202
Bulgaria	6	2,108	13	4,447	7	57%	2,537	75	576%	25,619
Croatia	12	7,988	23	15,711	8	35%	5,503	69	294%	46,159
Cyprus	5	15,756	8	22,697	2	20%	4,492	29	371%	84,187
Czech Rep.	28	5,928	38	7,936	13	34%	2,727	110	290%	23,051
Denmark	831	350,142	1,304	419,104	287	22%	92,288	975	75%	313,554
Estonia	3	6,084	7	10,024	4	55%	5,517	33	473%	47,445
Finland	176	67,074	258	89,229	26	10%	8,872	304	118%	105,127
France	2,047	70,667	2,944	93,663	488	17%	15,533	1,598	54%	50,832
Germany	1,895	47,067	2,480	60,135	345	14%	8,375	1,433	58%	34,734
Greece	13	2,996	19	4,671	3	18%	835	86	447%	20,865
Hungary	11	2,691	14	3,373	2	15%	502	20	146%	4,933
Ireland	341	196,823	551	268,769	145	26%	70,807	365	66%	178,237
Italy	693	26,880	1,219	46,620	209	17%	7,981	671	55%	25,641
Latvia	1	786	4	4,424	2	44%	1,964	3	90%	3,999
Lithuania	2	1,535	7	4,695	4	56%	2,607	8	112%	5,237
Luxembourg	142	620,154	224	823,566	76	34%	278,128	135	60%	495,693
Malta	11	66,014	13	61,063	6	45%	27,402	9	72%	43,779
Netherlands	1,419	186,127	2,117	248,484	429	20%	50,379	1,735	82%	203,689
Poland	97	6,903	90	6,276	24	27%	1,679	267	297%	18,618
Portugal	65	15,971	98	23,582	12	12%	2,922	261	267%	62,982
Romania	6	793	22	2,926	13	59%	1,723	32	147%	4,289
Slovakia	14	7,345	22	11,684	9	43%	4,977	105	487%	56,895
Slovenia	8	8,960	12	14,606	3	27%	3,924	20	158%	23,088
Spain	383	20,825	460	24,096	62	13%	3,252	2,079	452%	108,878
Sweden	685	134,327	1,209	253,774	267	22%	56,049	879	73%	184,648
EU	9,311	48.809	13,650	68,777	2,526	19%	12,728	11,755	86%	59,229
Developed EU	9,110	62,346	13,378	87,191	2,433	18%	15,855	10,926	82%	71,206
Emerging EU	201	4,499	271	6,024	93	34%	2,070	829	306%	18,413
Eurozone	7,635	51,417	10,937	70,374	1,904	17%	12,252	9,326	85%	60,009

Source: New Financial analysis of OECD data

Fig.18 The growth opportunity in capital markets financing

The growth potential in capital markets financing (corporate bonds, equities, leveraged loans, and venture capital), by country

	2014		2022		2030			What if…?		
Country	€bn	Number of deals	€bn	Number of deals	Growth (€bn)	Growth (%)	Additional deals	Growth (€bn)	Growth (%)	Additional deals
Austria	6.5	51	8.4	92	2.3	28%	29	9.0	107%	110
Belgium	17.0	92	17.6	146	4.7	27%	42	15.2	86%	222
Bulgaria	0.6	8	1.0	13	0.4	41%	8	1.6	161%	21
Croatia	1.1	14	0.9	21	0.3	32%	6	1.3	152%	21
Cyprus	0.5	8	0.4	12	0.1	32%	3	0.4	110%	9
Czech Rep.	5.3	30	9.9	37	4.9	50%	18	6.8	68%	58
Denmark	10.7	101	15.5	159	4.0	26%	47	11.1	72%	133
Estonia	0.2	17	1.2	83	0.7	60%	49	1.1	93%	46
Finland	10.5	136	14.5	163	3.9	27%	53	9.8	67%	105
France	117.2	644	148.4	875	26.6	18%	217	78.9	53%	751
Germany	128.3	715	176.1	1,040	34.8	20%	329	121.2	69%	601
Greece	8.2	62	5.6	39	0.9	16%	6	4.9	88%	83
Hungary	1.9	23	1.7	13	0.6	35%	4	3.0	174%	36
Ireland	11.4	111	20.5	147	7.8	38%	66	16.0	78%	224
Italy	51.2	239	71.7	286	12.9	18%	56	50.3	70%	429
Latvia	0.0	11	0.1	12	0.0	50%	7	1.0	1348%	51
Lithuania	0.1	7	1.1	18	0.7	69%	11	1.9	175%	27
Luxembourg	7.5	22	13.1	41	4.8	37%	17	6.1	47%	22
Malta	0.1	0	1.5	12	0.8	55%	6	0.7	45%	7
Netherlands	38.7	181	65.5	287	12.9	20%	93	30.0	46%	255
Poland	7.8	82	8.4	72	4.5	53%	36	13.2	157%	190
Portugal	10.4	48	5.5	49	0.7	12%	15	6.9	126%	57
Romania	1.6	24	1.9	25	1.2	66%	12	7.5	396%	258
Slovakia	1.9	9	0.5	7	0.3	57%	3	2.3	491%	34
Slovenia	0.5	11	0.1	3	0.0	44%	1	0.9	931%	24
Spain	47.3	346	55.8	614	9.2	16%	169	38.3	69%	312
Sweden	18.8	280	51.4	604	15.4	30%	201	28.7	56%	338
EU	505.4	3,272	698.2	4,870	155.6	22%	1,504	467.9	67%	4,425
Developed EU	476.1	2,974	666.0	4,527	141.0	21%	1,343	422.6	63%	3,575
Emerging EU	29.2	298	32.2	343	14.6	45%	162	45.4	141%	850
Eurozone	457.5	2,710	607.7	3,926	124.2	20%	1,173	394.9	65%	3,369

Source: New Financial analysis of Dealogic and Preqin data