The Future of Europe's Capital Markets

It is a pleasure to be here today in the company of so many distinguished colleagues and friends.

Over the last decade, Europe has faced a number of economic challenges.

Wages that are too low.

Unemployment, particularly youth unemployment, that is too high.

And economic growth that is too sluggish.

As Vice President Katainen and his team have recognised, these are not cyclical factors that are the ebbs and flows of an economy. Nor are they simply remnants of a crisis a decade ago.

Rather, they are symptoms of structural problems which have undermined, and continue to undermine, the future of Europe's economy.

Mr. Vice President, I applaud your determination to address them.
I cannot claim to see the whole pitch, but I do want to address one issue in particular – how businesses are financed here.

Put simply, we must broaden the means through which businesses and entrepreneurs access capital and other forms of financing. For too long, growth in Europe has been largely financed directly by banks, through lending on their balance sheets.

Because banks in Europe have traditionally acted as the actual provider of credit, when European banks became troubled investment capital dried up. As a result, Europe's economic fortunes have been too tightly intertwined with those of its banks.

We must transition the European economy away from this dependence on bank balance sheets. Growth in the future must be built on financing from healthy, diverse capital markets which allow businesses and entrepreneurs to access a broader range of investors, such as pension funds, insurance companies and investment funds. This would decouple the European economy from bank balance sheets. A broader financing base will create a much more reliable foundation for economic growth in the future.

The solution to these problems - to how we fund growth, to how we break this unhealthy linkage, and to how we position Europe for success in the long-term – lies in a centuries old innovation, born in Europe, but which has flourished in America and remains underdeveloped here: capital markets.

I spent most of my career in the United States. I've been a corporate banker, and an investment banker, yet always felt that my customers had one huge advantage over their European rivals.

They had access to a far deeper and more diverse range of finance.

We, as bankers, were an important source of financing. But we weren't the only game in town.

Non-bank finance permeates the American financial system. Major corporates issue debt and equity in a variety of forms to a diverse pool of investors to finance everything from new facilities to strategic acquisitions to working capital. Finance in America means far more than just bank loans. And, as a result, bank balance sheets in the US are relatively smaller in relation to the broader economy, as compared to other developed countries.

Europe should embrace these innovations, much the same way the US economy has, by promoting strong, stable, capital markets.

Capital markets provide a broader array of instruments than banks alone. As a result they can address the specific needs of issuers and investors more effectively.

It means access to the equity markets and early stage investment, both key to unlocking the potential in Europe's growth companies.

And it means corporations have access to the global debt markets, the largest financial markets in the world.

This is not to say that banks will not continue to play a critical role, but it will be a different role. Banks will be primarily intermediaries, bringing together the providers of credit with those seeking financing, rather than always being the direct lenders.

It only seems right that Europe embraces these markets; after all they were invented here in Europe.

The first equities were issued in France to fund a mill on the River Garonne.

The oldest stock market in the world was formed in Amsterdam to trade stocks in the Dutch East India Company.

And the first ever bond was issued by the English Government to fund a war with France.

The experience and sophistication of the European economy gives us an opportunity to create one of the largest global capital markets on the planet, right here.

That is why I am so delighted to see the Capital Markets Union project take shape.

Already, progress has been made, and Vice President Katainen and his colleagues in the Commission should be commended. But, there is more to do.

We must standardise the rules critical to strong capital markets so that they are both consistent and predictable across Europe.

As an example, insolvency law varies greatly from jurisdiction to jurisdiction. These differences make it more challenging for investors to evaluate investments and effectively restrict the pool of financing available to corporations.

As a result, the disparate insolvency regimes across Europe limit cross-border growth, particularly for smaller companies, helping to explain why Europe has such a stark lack of recent high growth firms.

Standardisation is also critical for early stage risk finance, which could transform the growth chances of our highest potential businesses.

At the moment it is difficult for a business in Cambridge to raise venture capital in Frankfurt, or vice versa.

That restricts venture investment to each country's borders.

And it means that investors cannot adequately diversify their portfolio without reaching beyond their core sectors.

It dilutes the expertise the investor can bring.

It raises the cost of finance for businesses, and stops clusters developing.

It is inefficient.

So we need to help growth business and their backers reach each other, developing a shared set of rules around capital markets activities, so that complying with one country's rules doesn't exclude you from another.

Finally, and importantly, we need to recognize that there are aspects of bank regulatory reform that undermine efforts to promote capital markets in Europe.

Largely by accident, some aspects of reform have disincentivised banks from converting businesses they lend to, into users of the capitals markets.

Public policy has made bank loans more flexible and cheaper, through friendlier legal regimes and lower capital requirements, and as a result, banks over promote bank loans to compete for wider business.

In contrast, public policy has made capital markets financing more onerous both for businesses and bank intermediaries.

Businesses seeking financing face complex regulatory issues and varying public disclosure requirements before they can access the markets. And bank intermediaries face their own numerous new regulatory requirements which, while in most cases absolutely necessary, need to be implemented in such a way that they do not inhibit necessary economic reforms.

The Capital Markets Union project needs to take account of these factors and ensure that bank regulatory reform works in harmony with the Capital Markets Union, without undermining the much needed reforms that have been implemented to make the financial system safer.

Investment Banks like Barclays play a critical role in strong capital markets.

We connect users of capital to holders of capital.

And we provide liquidity for securities to trade and for the hedging of risk, creating efficient markets.

I'm not suggesting a return to pre-crisis levels of risk-taking – those days are thankfully behind us. But, Europe will have a more dynamic and more stable economy if financing for its businesses shifts from bank balance sheets to capital markets. And, for capital markets to work efficiently and foster economic growth, capital markets intermediaries - the investment banking industry – must be healthy.

Yet years on from the financial crisis, the trend for European investment banks continues to be towards shrinkage – not growth – of strategic capacity.

There are a variety of reasons for this, from low interest rates to changing regulatory and capital requirements and historical conduct matters that we as an industry must make right.

But the cumulative impact has been substantial and many European firms are at the brink. Ultimately, banks incapable of making profits are not safe and not sustainable.

Whether intentional or not, European policymakers have a decision to make, and it is a decision that needs to be taken quickly.

That is, they must determine whether they care who owns, runs and manages the capital markets intermediaries that we depend on.

Ten years ago, European institutions accounted for well over half the European investment banking market.

Today that share is down by 20 per cent and the three biggest investment banks in Europe are all American. US banks now account for half the market, up from a third 10 years ago.

We are about to tip over into American dominance, and, if this trend continues, we risk a very near future in which Europe's capital markets are almost entirely dependent on firms domiciled elsewhere.

To my mind, that is a problem.

There is an alternative prospect – a prospect whereby EU managed and domiciled banks play a major role in the capital markets and compete with others from around the world.

Not as direct suppliers of capital – we'll leave that to the buy-side. But as intermediaries.

This means strong European institutions headquartered here.

Employing hundreds and thousands of people here.

Paying taxes here.

Committed to corporates here.

This is not about protectionism. It is about ensuring a level playing field that does not make it harder for European firms to compete with non-EU firms in their home markets. But regardless, Europe should not be reliant on foreign institutions to provide access to the capital markets union we hope to create.

What is required now is for governments across Europe to work together to establish the regulatory cohesion and consistency needed to ensure the best conditions for economic growth and a financial system that leaves nobody behind.

Of course, if we are to act together, we need to stick together, and nobody in this room needs reminding that the UK is about to make an important decision about its role as a member of the European Union.

As an American, I'm not going to stand up here and tell anybody in the UK which way they should vote.

But the UK's role in Europe's capital markets is critical. In my judgment, it can only be bad for Europe and bad for the UK if its role as a European financial centre is diminished.

And I can say with confidence – whatever the outcome – that economic resilience and prosperity across this continent will be interlinked with the resilience and prosperity of the banks that operate here.

Sustaining that resilience and prosperity is the aspiration of all of us here today.

Thank you very much.