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ISTITUTO DI CULTURA BANCARIA «FRANCESCO PARRILLO»

Gennaio-Aprile 2024

1-2

Tariffa Regime Libero:-Poste Italiane S.p.a.-Spedizione in abbonamento Postale-70%-DCB Roma

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RIVISTA BANCARIA
MINERVA BANCARIA
ANNO LXXX (NUOVA SERIE) GENNAIO-APRILE 2024 N. 1-2

SOMMARIO

ISSN: 1594-7556 **La Rivista è accreditata AIDEA e SIE** **Econ.Lit**

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Editrice Minerva Bancaria srl

DIREZIONE E REDAZIONE	Largo Luigi Antonelli, 27 – 00145 Roma redazione@rivistabancaria.it
AMMINISTRAZIONE	EDITRICE MINERVA BANCARIA S.r.l. presso PtsClas, Viale di Villa Massimo, 29 00161 - Roma amministrazione@editriceminervabancaria.it

Autorizzazione Tribunale di Milano 6-10-948 N. 636 Registrato
Proprietario: Istituto di Cultura Bancaria "Francesco Parrillo"
Spedizione in abbonamento postale - Pubblicazione bimestrale - 70% - Roma

Finito di stampare nel mese di aprile 2024 presso Press Up, Roma

Segui Editrice Minerva Bancaria su:

EUROPEAN EQUITY MARKETS, SMES AND THE GROWTH CHALLENGE◊

NICOLA BORRI*
GIORGIO DI GIORGIO**

Abstract

This study investigates factors influencing market capitalization and investment opportunities for smaller firms in European equity growth markets. Focusing on Italy, France, Germany, Sweden, and Spain, with the UK for comparison, the analysis uncovers substantial disparities in market capitalization, listed firms, and household portfolios across these nations. Variations in both capital supply and demand factors are highlighted to rationalize these dynamics. Sweden emerges as a leader in growth markets due to lenient IPO requirements and lower costs, while household portfolio allocations significantly affect capital supply. Higher financial literacy, found in Sweden and Germany, leads to more sophisticated portfolios. The Capital Markets Union (CMU) initiative's role in supporting SME growth is acknowledged, with room for improvement. Additionally, sovereign wealth funds' potential as significant investors in SMEs is discussed, bolstering their chances of listing on growth markets.

◊ We express our gratitude to Franco Gaudenti for his invaluable contributions to this study and acknowledge the financial support provided by EnVent Capital Markets through the structural partnership with CASMEF on research projects focusing on European capital markets. The partnership with EnVent was crucial in driving this research forward. We also thank Carmine Di Noia and Luca Filippa for very helpful comments. Alessio Barbalonga, Diana Lagravinese and Federico Kirschen provided excellent research assistance. Obviously, we are the sole responsible for the opinions expressed in this paper.

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Mercati azionari europei, PMI e la sfida della crescita – Sintesi

Questo studio analizza i fattori che influenzano la capitalizzazione di mercato e le opportunità di investimento per le PMI nei mercati azionari europei "growth". Concentrandosi su Italia, Francia, Germania, Svezia e Spagna, con il Regno Unito a scopo di confronto, l'analisi rivela notevoli disparità nella capitalizzazione di mercato, nel numero di imprese quotate e nei portafogli delle famiglie in questi paesi. Vengono evidenziate variazioni nei fattori di offerta e domanda di capitale per razionalizzare queste dinamiche. La Svezia emerge come leader nei mercati growth grazie a requisiti IPO più flessibili e costi inferiori, mentre le allocazioni dei portafogli familiari influenzano in modo significativo l'offerta di capitale. Una maggiore alfabetizzazione finanziaria, riscontrata in Svezia e in Germania, porta a portafogli più sofisticati. Viene riconosciuto il ruolo della Capital Market Union (CMU) nel sostenere la crescita delle PMI, con spazio per ulteriori miglioramenti. Inoltre, viene discussa la potenziale partecipazione dei fondi sovrani come investitori significativi nelle PMI, rafforzando le loro possibilità di quotazione sui mercati growth.

Parole chiave: *Struttura Finanziaria; Capitalizzazione di Mercato, Mercati Azionari Growth, Capital Market Union*

Codici JEL: G1; G3.

Keywords: Financial Structure; Market Capitalization; Equity Growth Markets; Capital Markets Union.

1. Introduction

Small and medium enterprises (SMEs) play a vital role in today's economy, driving innovation, fostering competition, and contributing to overall economic growth. These businesses, typically characterized by their modest scale and workforce, are essential for a variety of reasons. First, SMEs are major creators of employment opportunities, particularly at the local level, where they often serve as the backbone of communities, providing jobs to a significant portion of the population. Second, SMEs foster entrepreneurship and innovation by offering a fertile ground for new ideas and experimentation. Their agility and flexibility allow them to adapt quickly to changing market demands, driving technological advancements and contributing to the overall dynamism of the business landscape. Furthermore, SMEs promote market diversity and competition, preventing monopolies and fostering fair pricing and quality of products and services.

When comparing the importance of SMEs in the United States and Europe, some similarities and differences emerge. In both regions, SMEs hold significant value by contributing to job creation, innovation, and economic development. However, there are some variations in the scale and structure of SMEs between the two.

In the United States, SMEs have long been recognized as a key driver of the economy. They account for a substantial portion of employment, with small businesses often being the primary source of jobs. The entrepreneurial culture in the U.S. promotes innovation and risk-taking, leading to the emergence of many successful startups and the continuous evolution of SMEs across various sectors.

In Europe, SMEs also play a critical role, although the landscape may differ in some aspects. Many European countries have a strong tradition of family-owned businesses, with a focus on craftsmanship and specialized industries. SMEs in Europe often have closer ties to their local communities, emphasizing regional development and sustainability. Additionally, European

SMEs benefit from robust support networks, including dedicated government programs and initiatives designed to foster their growth and competitiveness.

This paper centers on the critical role of European SMEs, which serve as the foundational pillar of the European economy. The significance of SMEs becomes evident when considering key statistics: an astounding 99% of businesses and an overwhelming 99.8% of all non-financial businesses fall within the SME category, constituting a staggering total of approximately 24 million enterprises. Moreover, SMEs contribute significantly to Europe's GDP, accounting for more than half of its total output with a remarkable value added of approximately 3.9 trillion euros. Notably, these dynamic businesses also play a pivotal role in employment generation, responsible for the creation of 85% of new jobs across the region.

Both the U.S. and Europe recognize the importance of SMEs in driving economic growth and employment. However, some differences arise due to variations in market size, regulatory frameworks, and cultural factors. The U.S., with its vast domestic market and emphasis on entrepreneurship, tend to have a higher number of rapidly growing startups. Europe, on the other hand, may have a larger proportion of established SMEs operating in specialized niches, benefitting from a strong focus on quality and craftsmanship. This study aims to comprehensively examine the factors that contribute to enhancing growth opportunities for SMEs, while also delving into the key inhibiting factors that impede their growth trajectory. By conducting a thorough analysis, we seek to identify the drivers and barriers that shape the growth landscape for SMEs. Through this examination, we aim to provide insights and recommendations that can facilitate the creation of a supportive environment for SMEs to thrive, ultimately fostering their sustained growth and development.

Enabling the growth of SMEs is crucial, considering the unique challenges they encounter due to their smaller size (see, e.g., Love and Roper (2015) for a review of the literature and Di Giorgio and Murro (2021) for the case of Italy). First, accessing financing becomes a daunting task for these firms as they often face tighter credit conditions and higher funding costs. Second, their relative lack of resources hampers productivity, impeding investments in research and development and hindering their ability to leverage economies of scale. Finally, governance and control issues can arise, particularly in cases where family management is involved, adding complexity to decision-making processes. Recognizing and addressing these multifaceted challenges is essential to empower SMEs, allowing them to unlock their full potential and contribute significantly to economic growth and job creation.

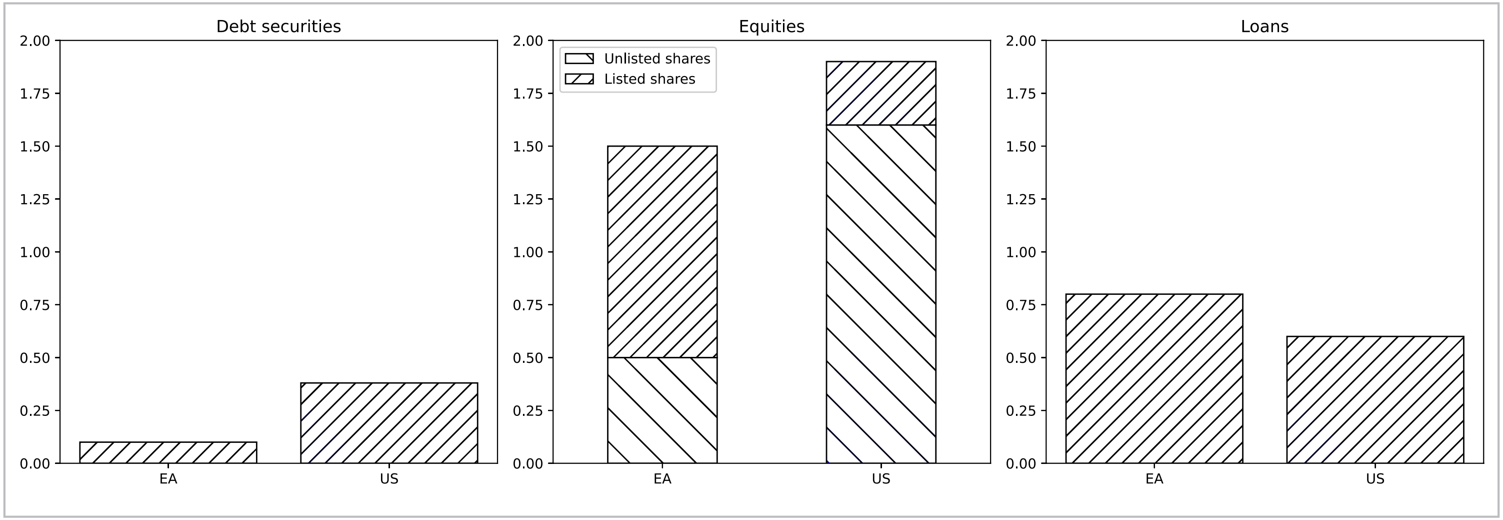
In this paper, we focus on the financial structure of European SMEs and try to understand why only a few of them (with respect to the US) find useful to go public and be listed on regulated exchanges and multilateral trading facilities (MTFs). We start from documenting data on 5 EU countries (France, Germany, Italy, Spain and Sweden) plus UK, given the historical relevance of London as a prominent financial center. We observe relevant differences in the dimension of growth equity markets, that is the natural segment form SMEs to go public. Large variations emerge in the number of listed firms, their average number of employees and the overall value of listed entities. We then try to highlight factors affecting both the demand and the supply of capital that might be responsible for such diverse performance across countries. And we finally offer some recipes to further promote market development and integration along the auspices of the Capital markets union.

The organization of the paper is the following: in section 2, we start by comparing the financial structure of US and EU firms and describe some recent relevant dynamics observed in their financial markets. We also investigate the composition of EU equity markets between regulated exchanges and multilateral trading facilities and describe the main differences arising in terms of markets dimension. Section 3 investigates the main factors affecting the demand and the supply of capital highlighting some relevant differences at the country level that might determine the different performance we observe in growth equity markets, a natural first shore for SMEs willing to access public markets characterized by the presence of a variety of investors that rely on rigorous standards in terms of accounting and reporting, available information, governance rules and so on. In Section 4, we recognize the important role that the Capital markets union (CMU) and other adequate public, regulatory and supervisory actions may have on a more rapid and efficient development of equity markets in the EU and we advance some further proposals and lines of intervention in this direction. Finally, in Section 5 we summarize our findings and provide our conclusions.

2. Financial Markets across the Atlantic Ocean

A notable and widely acknowledged distinction between the U.S. and the EU lies in their divergent approaches to financing. Specifically, a stark disparity emerges regarding the predominant sources of funding for non-financial corporations (market- vs bank-based economies): in the US about 65% of the financial liabilities of non financial corporations is accounted by equities with respect to only 56% in the EU. Also, the weight of bonds is much higher (7% of total liabilities in the US versus 4% in the EU), while loans are much more relevant in Europe (28% versus only 12% in the US). Figure 1 confirms the paramount position of equities as the primary source of funding for non financial firms in the US and reveals further that unlisted shares account for less than one-third of the total, whereas they account for two thirds in the Euro area. Conversely, the Euro area showcases a contrasting landscape, wherein bank loans surpass many other forms of financing and encompass over a quarter of the total funding pool. This discrepancy highlights the differing financial ecosystems between the two regions, emphasizing the significance of understanding and addressing the variations in funding structures when examining policies and strategies to support businesses in each context. Furthermore, the figure reveals that equity financing is tightly associated with listed companies, highlighting the importance of listing to raise new capital.

Figure 1 - Sources of External Financing of Non-Financial Corporations in the U.S. vs Euro Area (2022) (Data are from ECB euro area accounts and OECD; see Panetta, 2023)[1]



Source: ECB blog available at : https://www.ecb.europa.eu/press/blog/date/2023/html/ecb.blog230830~cfe3be0960.en.html

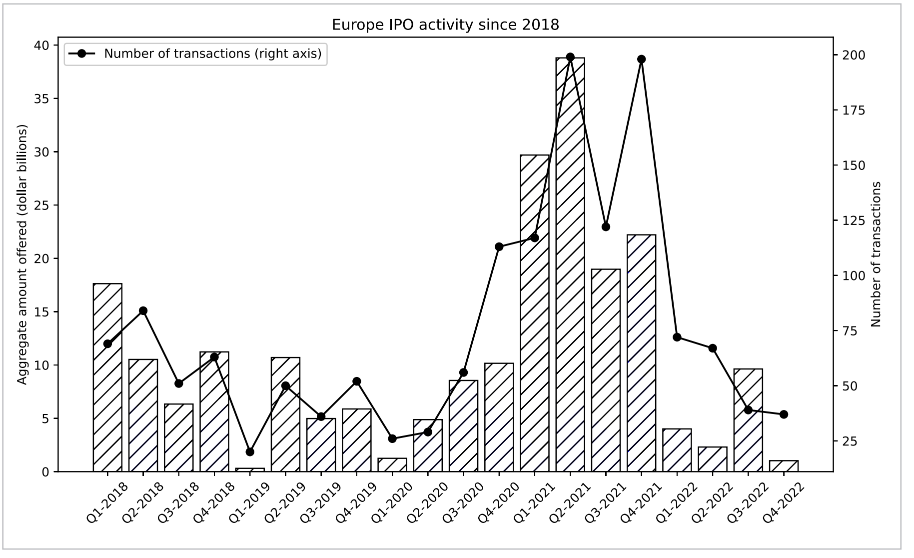
1 For further details, see Panetta, "Europe needs to think bigger to build its capital markets union", August 2023, available at: https://www.ecb.europa.eu/press/blog/date/2023/html/ecb.blog230830~cfe3be0960.en.html.

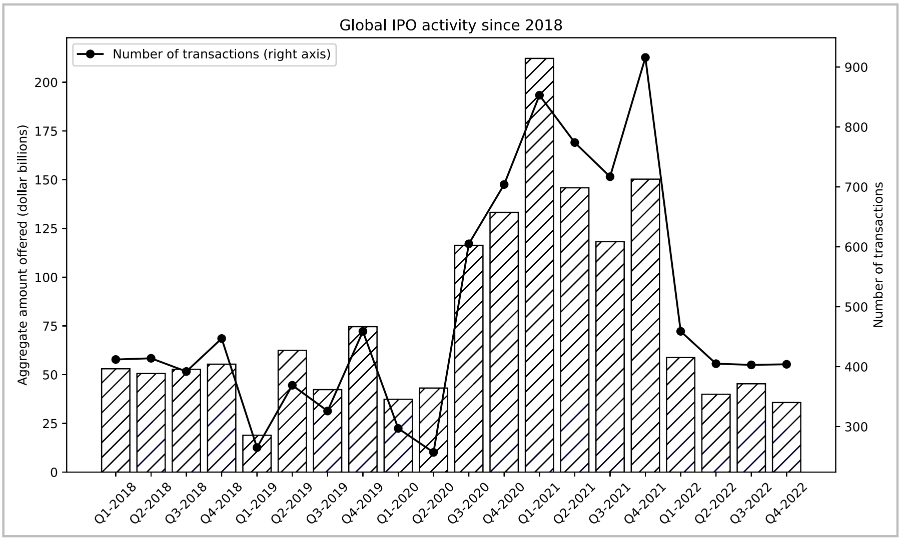
Public markets present a distinctive ecosystem for SMEs, encompassing a range of invaluable growth prospects. Foremost among these is the unparalleled opportunity for expansion and growth. By listing on public markets, SMEs gain visibility and prestige, bolstered by the associated media coverage. Moreover, public markets provide a gateway to diverse forms of capital, comprising both equity and debt financing options. Crucially, these markets also offer liquidity, a vital attribute enabling venture capitalists (VCs) and initial investors to exit and monetize their investments efficiently, often after an intermediate step involving private capital (equity funds and/or club deals). Simultaneously, shareholders benefit from the ability to actively manage their investments and diversify their overall risk. Lastly, public markets are intrinsically linked to enhanced transparency and corporate governance standards, ensuring greater accountability and control for listed firms. Embracing public markets can empower SMEs with the resources, exposure, and frameworks necessary for their sustainable growth and success.

2.1 A quick look at recent trends in Europe

In recent years, the European Union (EU) has witnessed a concerning decline in the number of Initial Public Offerings (IPOs). This trend stands in contrast to other global markets, exemplified by the recent figures from 2022. Notably, the EU accounted for a mere 11% of global IPOs during that year, while the United States claimed a substantial 38%, China accounted for 18%, and even the United Kingdom independently captured 4% (Figure 2). This disparity underscores the pressing need to address the underlying factors that have contributed to the diminished IPO activity in the EU. By exploring potential policy changes, we can hope to provide solutions to reinvigorate the EU IPO landscape, facilitating capital formation, business growth, and fostering a favorable investment climate.

Figure 2 - IPOs in Europe lagging behind Global IPO activity

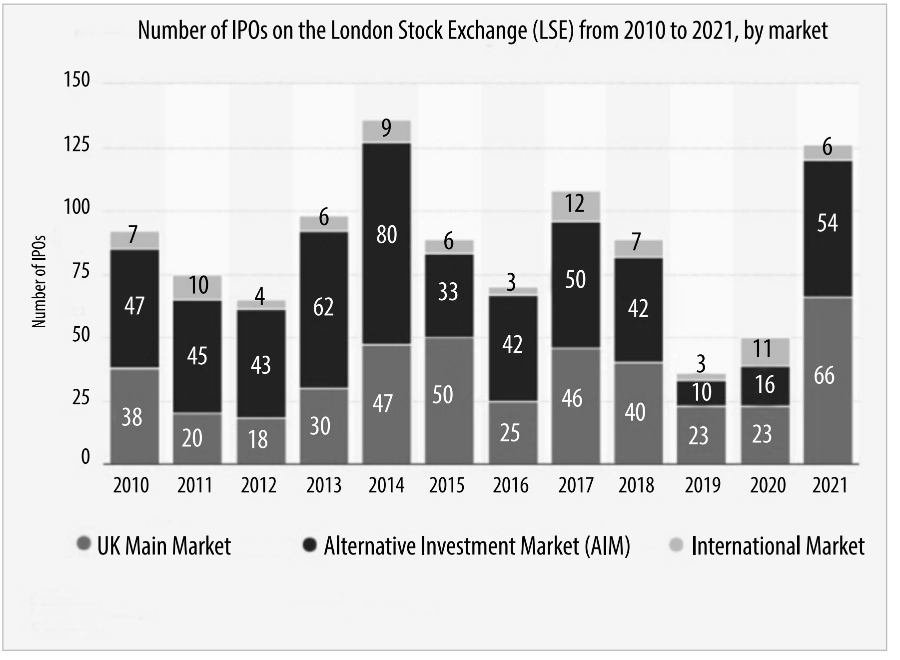


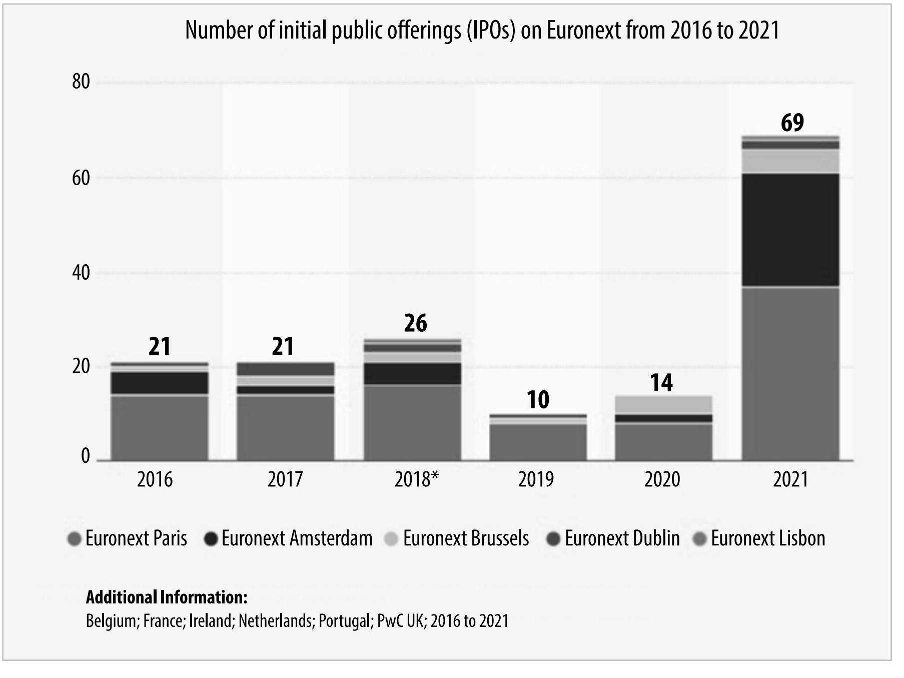


Source: S&P Global Market Intelligence (available at: https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/global-ipos-in-q2-2023-hit-lowest-level-since-2020-as-interest-rates-soar-76667496)

The IPO landscape in Europe has exhibited notable disparities even within EU markets. Notably, Figure 3 underscores a significant gap between European markets and the UK market in terms of IPO activity.

Figure 3 - IPOs in European Markets (not limited to growth markets; London Stock Exchange and PwC UK from Statista)

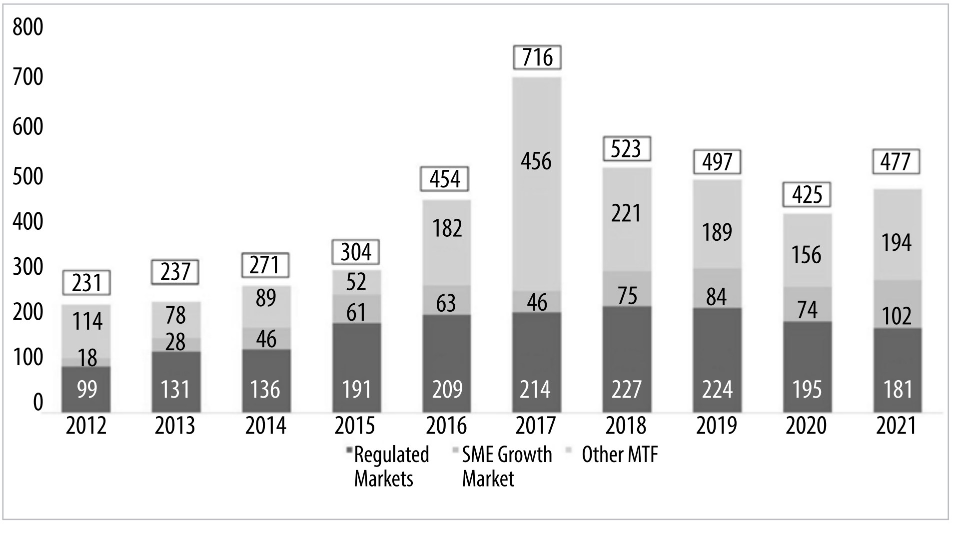




Source: Statista

Moreover, recent data reported in Figure 4, reveal a concerning trend of escalating delistings from public markets within the European Union (EU). Specifically, the number of companies choosing to delist has more than doubled since 2012, highlighting a growing phenomenon that demands attention. The significant surge in delistings necessitates a thorough examination of the underlying factors contributing to this trend. Addressing the causes behind this upswing is crucial to preserving the vibrancy and attractiveness of EU public markets, as well as ensuring that companies can access the capital and visibility they require for sustainable growth and long-term success.[2]

Figure 4 - Annual number of delistings in the EU in regulated markets, SME growth markets and other MTFs



Source: EU Commission Staff Working Document, 2022 available at: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52022SC0762.

The increasing number of delistings in European markets, discussed above, can be attributed to a set of interconnected factors, which are commonly cited by observers. Among these factors, the challenges of meeting regular financial

2 The recent trend associated with an increase in delistings is not limited to the EU. In fact, delistings in the US have experienced a qualitatively similar trend. Therefore, it is likely that the trend is partially explained by global factors, like the prolonged period of very low interest rates which ended with the recent and unexpected increase in inflation in many countries. For example, Robert Armstrong ("The small-cap blued", *Financial Times*, 28 September 2023) argues that, in the period of very low interest rates, private equity companies might have bought several good quality small listed companies to make them private.

reporting requirements stand out prominently. The time and costs associated with compliance and administration pose significant burdens, which often drive firms to make the decision to delist. Compliance costs, in particular, can become prohibitively high, creating a disincentive for continued listing. Additionally, the annual fees paid to advisors, brokers, and exchanges further contribute to the financial strain experienced by SMEs, influencing their delisting decisions. Furthermore, the disclosure requirements mandated by the Market Abuse Regulation (MAR), which necessitate the divulgence of sensitive information, have also been identified as a deterrent for SMEs. The combined impact of all these factors underscores the need to properly evaluate pros and cons of listing regulations and associated costs to alleviate the burden faced by SMEs and encourage their continued participation in public markets.

The reluctance of SMEs to pursue public listings has been extensively observed, with analysts attributing this trend to a common set of explanations.[3] Primarily, the inflexible nature of listing requirements has emerged as a key factor hindering SMEs. This is particularly evident in the divergent regulations pertaining to multiple voting rights (MVR) across EU countries, leading to regulatory arbitrage wherein certain firms opt to change public markets in search of a more conducive environment. An EU survey conducted recently shed light on this matter, revealing that 76% of stakeholders believe that MVR shares could serve as a catalyst for SME listings, particularly among family-owned and high-growth enterprises.[4]

Additionally, analysts have identified the burdensome regulatory framework stemming from the regional fragmentation of EU markets as another significant deterrent to SMEs considering going public in the area. The unnecessary complexity and regulatory burden associated with fragmented markets compound the challenges faced by SMEs, discouraging their pursuit

3 See also Caccavaio et al. (2012) and Di Giorgio and Murro (2021, in Italian).

4 A recent government proposal is under discussion in the Italian Parliament that, among some other interventions, opens the door to such possibility.

of public listings. Relevant differences existing in both listing requirements and supervisory approaches could limit the dimension of domestic markets and their efficiency in providing valuations that properly reflect firms' characteristics and perspectives. This might be due to the limited number of local specialized professional and institutional investors, to the presence of excessive relationship-behavior among investors, and to business concentration.

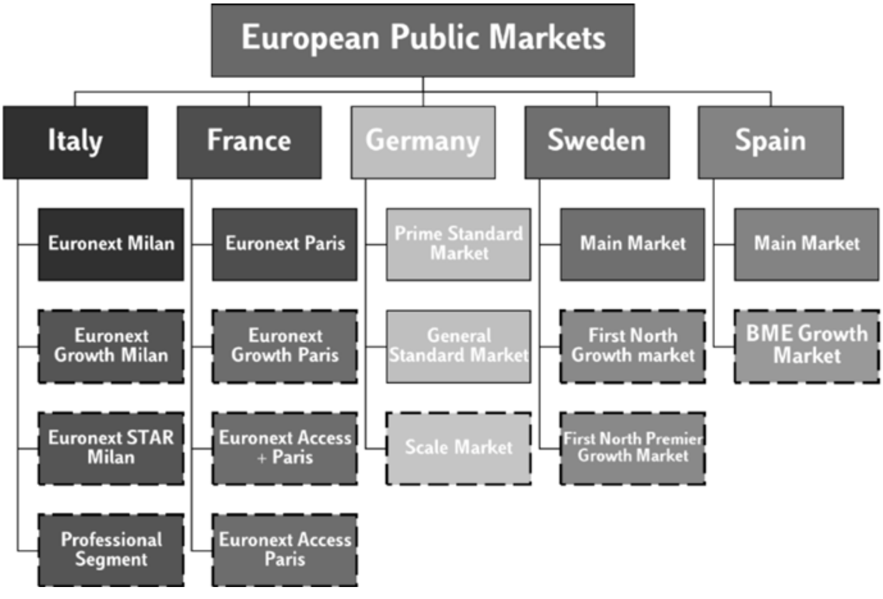
The Action Plan for a Capital markets union in Europe established ambitious targets in terms of market developments and elimination of domestic barriers. However, this plan has not yet been coupled with the attribution to a single European Authority of strong cross-border regulatory and supervisory powers, so that the current role of ESMA—limited to guidelines and technical standards for the European Commission—cannot be compared with that of the EBA and the ECB for the banking and financial sector. Addressing these concerns, and streamlining adequate interventions, could encourage greater SME participation in public markets, fostering economic growth and strengthening the investment landscape. We note that a similar concern has been vigorously expressed by Christine Lagarde, the ECB president, who called for "creating a European SEC" to replace the patchwork of national markets watchdogs (see "Europe needs its own SEC, says Christine Lagarde" on the *Financial Times* of November 17 2023).

2.2. Public Markets in Europe

This section aims at providing an overview of the principal public markets in the EU, with a specific focus on Italy, France, Germany, Sweden, and Spain. To provide additional context and comparative insights, we include the United Kingdom as a benchmark due to its significant position as a long lasting prominent financial center. By incorporating the UK in our analysis, we aim at enhancing our understanding of the dynamics and peculiarities within the financial ecosystems of the five aforementioned EU countries. Figure

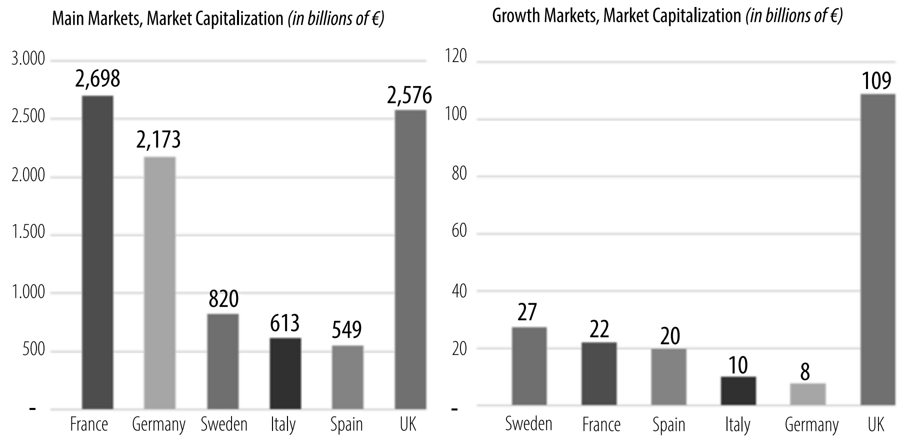
5 offers a concise summary of these countries' public markets, highlighting the distinctions in terms of the size and nature of companies typically listed. For instance, in Italy, the primary market is Euronext Milan, while Euronext Growth and Star (actually, a "quality" subset of Euronext Milan listed firms) properly cater to smaller and medium firms. The subsequent part of this section concentrates on public markets tailored for smaller enterprises, as these markets serve as the primary avenues where SMEs are likely to seek listing opportunities. By examining these markets in depth, we can gain valuable insights into the avenues available for SMEs to access public capital and facilitate their growth and development. It is important to stress that, even within a giving country, these markets are subject to partially different regulations. For example, in Italy the largest market is subject to regulation from the market "watchdog", the Consob. In contrast, smaller markets like euronext growth is subject to the regulation issued by the market sponsor (Borsa Italiana). The latter type of market is referred to as MTF, or multilateral trading facility in Europe, and as ATS, or alternative trading system in the U.S.

Figure 5 - Public Markets in Selected EU Countries



An intriguing observation that emerges as a key stylized fact is the significant disparity in size, as measured by total market capitalization, among the countries under consideration. Figure 6 depicts the market capitalization, as of the end of 2022, for the main markets (left panel) and the growth markets (right panel), which specifically cater to SMEs. Notably, the ranking of EU countries varies considerably between the main and growth markets. France claims the top spot for main markets, boasting a market capitalization of 2.7 trillion euros, closely followed by Germany at 2.1 trillion euros. Conversely, the main markets in Sweden, Italy, and Spain each exhibit a market capitalization below 1 trillion euros. As expected, growth markets exhibit smaller capitalizations, with Sweden hosting the largest growth market at 27 billion euros. It is noteworthy that Sweden, despite having the smallest GDP among the considered countries, accommodates the most substantial growth market. On the other hand, growth markets in Italy and Germany possess the smallest market capitalizations, hovering around 10 billion euros. Consequently, the subsequent analysis aims to delve into the institutional factors that have propelled Sweden to host the largest growth market, shedding light on the unique dynamics that have shaped its thriving SME ecosystem. The UK's main market stands as the second largest among the main markets of the five EU countries, trailing closely behind France. Nevertheless, the UK's growth market outshines all others by a considerable margin, surpassing the second largest growth market in Sweden by more than threefold. This observation underscores the critical role of the UK in facilitating the listing of SMEs, which, despite Brexit, has remained unaffected thus far.

Figure 6 - Market Cap of Main and Growth Markets



Source: Data is from Bloomberg

It is imperative to dig into the underlying factors that contribute to such substantial variations in market capitalization, both in the main and growth markets. Understanding these reasons holds significant importance, as the divergent market sizes among countries can yield substantial disparities in productivity, growth potential, and investment opportunities. The size of the market directly influences the scale of economic activities, the level of competitiveness, and the potential for attracting investments. By comprehending the drivers behind these discrepancies, policymakers can devise targeted strategies to address inequalities, foster equitable growth, and cultivate an environment that encourages robust productivity, investment, and entrepreneurial activities across countries.

3. Understanding differences in growth equity markets in Europe

In order to highlight the potential factors contributing to the observed variations in market capitalization among public markets tailored for smaller firms (referred to as growth markets) in Europe, we proceed by presenting an economic "classic" analysis based on a comprehensive array of elements that pertain to both the demand and the supply side of the market for capital. We hope to gain valuable insights into the underlying dynamics shaping market capitalization disparities. Understanding the drivers from both the demand and supply perspectives is indeed crucial to advance proposals for effective policies and strategies that can address any existing gaps and improve the growth potential of these markets.

3.1 Demand Factors

Our analysis commences by examining descriptive statistics pertaining to the demand side in the market for capital. Table 1 presents an overview of the number of listed firms in the growth markets of the five EU countries under consideration, as of the end of 2022. Notably, the growth market in Sweden stands out with the highest number of listed firms, totaling 561, which is nearly double the count in France, the second-largest growth market in terms of listed firms. In stark contrast, the growth market in Germany accommodates a mere 50 listed firms. These substantial variations in the number of listed firms shed light on the varying significance and prominence of these markets across countries. Such disparities underscore the diverse levels of participation and emphasize the need to explore the underlying factors influencing the attractiveness and accessibility of these growth markets for SMEs. Consistent with the findings regarding a greater market capitalization, the UK also leads in terms of the number of listed firms, boasting a remarkable 816 listed companies.

Table 1 - Number of Listed Firms in Growth Markets

	Italy	France	Sweden	Germany	Spain	UK
2022	183	290	561	50	133	816

Source: Data is collected by the authors from the websites of the different marketplaces

Turning our attention to the workforce composition within the firms listed in the growth markets, we examine disparities in terms of average employee numbers. Table 2 presents the average number of employees in the top and bottom five companies based on market capitalization. Notably, Sweden emerges as a unique case, as it houses both the firms with the highest and lowest number of employees among the considered countries. This finding implies that the growth market in Sweden fosters a diverse ecosystem encompassing a wide range of firms, in contrast to other countries where listed firms tend to be predominantly larger in scale. For instance, in France, even the smallest firms exhibit relative sizeable employee figures, as evidenced by an average of 234 employees. This divergence highlights the distinctive composition of firms in the growth market of Sweden and underscores the importance of exploring the underlying factors driving this heterogeneity, which can offer valuable insights into the dynamics of SMEs within these markets. The UK growth market closely resembles the Swedish growth market in terms of the average number of employees in listed firms. Similarly to Sweden, the UK growth market accommodates a diverse range of firms, encompassing both large-scale enterprises and smaller companies with a limited number of employees.

Table 2 - Number of employees. Top (bottom): average of the top (bottom) 5 companies by market capitalization in 2022

		Italy	France	Sweden	Germany	Spain	UK
# of employees	Top	1031	997	3504	1764	996	4957
	Bottom	45	234	9	60	99	7

Source: Data is collected by the authors from the websites of the different marketplaces

To ascertain whether the observed differences, as discussed in Table 1 and 2, stem from institutional factors, we delve into the examination of initial public offering (IPO) requirements within the growth markets. Table 3 presents a snapshot of these requirements, offering valuable insights into the varying regulatory frameworks. Notably, the IPO requirements in Sweden appear to be the most lenient. They do not entail any stipulations regarding the minimum floating share, market capitalization, or the number of available financial statements. Conversely, the other markets impose more stringent criteria. For instance, in Italy, a minimum float of 10 percent is required, along with an additional prerequisite of five institutional investors. Germany and Spain impose even higher minimum float requirements, coupled with minimum market capitalization prerequisites, which are absent in Italy, France, and Sweden. Moreover, with the exception of Sweden, all countries have certain requirements pertaining to financial statements and accounting standards.

Overall, an analysis of the IPO requirements highlights that one of the reasons behind the larger size of the growth market in Sweden, in comparison to other countries, could be attributed to the relatively lower IPO costs associated with its less stringent requirements. These disparities underscore the significance of regulatory frameworks in shaping the attractiveness and accessibility of growth markets for SMEs across different countries. Similarly to the Swedish growth market, the UK growth market exhibits minimal IPO requirements. It shares resemblances such as the absence of requirements regarding minimum float or market capitalization. Additionally, the UK growth market imposes a relatively short duration of six months for the submission of financial statements, aligning with the Swedish market's lenient approach.

Table 3 - IPO Requirements

	Italy	France	Sweden	Germany	Spain
Float	≥10 % + 5 inst. inv.	€ 2.5 M	0 %	≥ 20 %	≥ 25 %
Market capitalization	Not Req.	Not Req.	Not Req.	≥ € 30 M	≥ € 6 M
Previous Financial Statement	1 (if existent)	2 years (audited)	Not Req.	1 year	3 fiscal yeras
Accounting standard	Local GAAP or IFRS	Local GAAP or IFRS	Standard of choice	Local GAAP or IFRS	Local GAAP or IFRS
Website	Required	Required1	Not Req.	Not Req.	Not Req.

Source: Data is collected by the authors from the websites of the different marketplaces

In order to comprehensively assess the overall costs involved, we conduct a simulation to estimate the potential IPO costs associated with listing both small and large firms. For this purpose, we consider two hypothetical firms as examples. The first is a small firm projected to have a market capitalization of 10 million euros, with 1 million admitted shares and a share price of 10 euros. The second is a large firm with a market capitalization of 500 million euros, 50 million admitted shares, and a share price of 10 euros. Tables 4 (for the small firm) and 5 (for the large firm) provide an overview of the approximated costs associated with various stages, from admission to potential delisting.

In analyzing the costs for a small firm, we observe that the fixed costs of admission are highest in Sweden, while they are lowest in Spain (refer to Table 4). Notably, both Sweden and Germany do not impose any variable costs for admission. Conversely, markets in Italy, France, and Spain entail additional variable costs during the admission process. All markets have fixed annual fees, ranging from 3,000 euros in France to 20,000 euros in Germany, along with minimal or no variable annual fees. Lastly, in the event of delisting, the most substantial cost is incurred by firms listed in France, with a delisting cost of 10,000 euros.

By these cost considerations, we can gain valuable insights into the financial implications faced by firms seeking to list in different markets. Such analysis helps us understand the variations in the cost structures across countries and enables us to assess the impact of these costs on the attractiveness and viability of growth markets for SMEs.

Table 4 - Costs from Admission to Delisting of a Small Firm

	Italy	France	Sweden	Germany	Spain	UK
Admission (fixed cost)	15’000	12’000	30’000	20’000	6’000	Ø
Admission (variable cost)	1’800	6’000	0	0	500	19’479
Annual fees (fixed cost)	16’000 (annualized)	3’000	10’100 (min fee)	20’000	6’000	10788
Annual fees (variable cost)	400 (annualized)	0	0	Ø	Ø	0
Delisting	1’000	10’000	4’730	-	-	-

Source: Data is collected by the authors from the websites of the different marketplaces

Table 5 presents a comprehensive overview of the costs associated with the admission to delisting process for the large firm. Notably, we observe that the fixed costs of admission increase only in the Italian growth market, rising from 15 to 25 thousand euros. Moreover, there is a substantial escalation in the variable cost of admission, reaching over 400 thousand euros in the case of France. While the variable cost in France stands out as significantly larger than in other markets, there are also notable increases in variable costs for Italy, Germany, and Spain. In contrast, Sweden maintains a relatively small variable cost of 6 thousand euros. It is worth noting that, apart from the variable cost, all other costs in Sweden remain consistent between the small and large firm scenarios. This observation indicates that the costs from admission to delisting in Sweden are comparatively lower than in other countries, presenting an additional factor contributing to the larger size and number of listings in Sweden's growth market.

Table 5 - Costs from Admission to Delisting of a Large Firm on the regulated marke

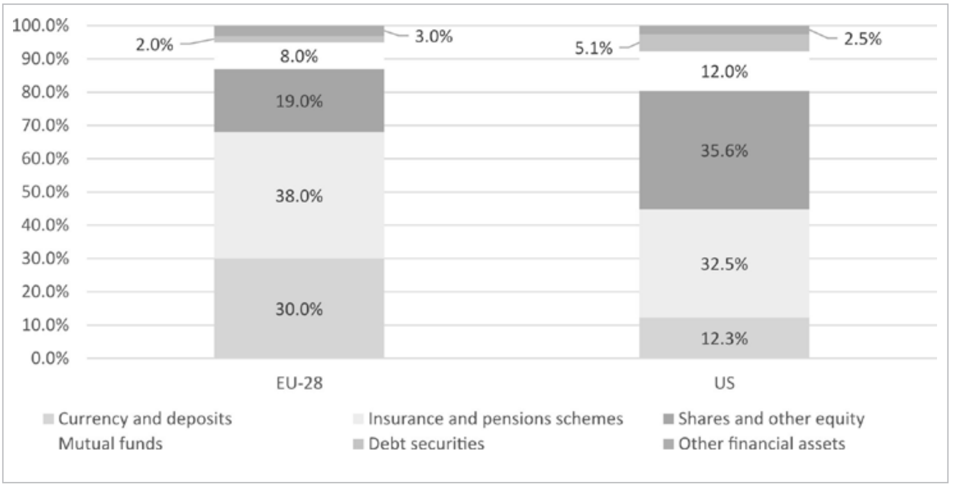
	Italy	France	Sweden	Germany	Spain	UK
Admission (fixed cost)	25'000	12'000	30'000	20'000	6'000	Ø
Admission (variable cost)	90'000	422'500	6'000	69'000	25'000	156.948 (max)
Annual fees (fixed cost)	16'000 (annualized)	3'000	10'100	20'000	6'000	10788
Annual fees (variable cost)	10'000 (annualized)	15'500	32'400 (max fee)	Ø	Ø	7276,10
Delisting	1'000	10'000	4'730	-	-	-

Source: Data is collected by the authors from the websites of the different marketplaces

3.2 Supply Factors

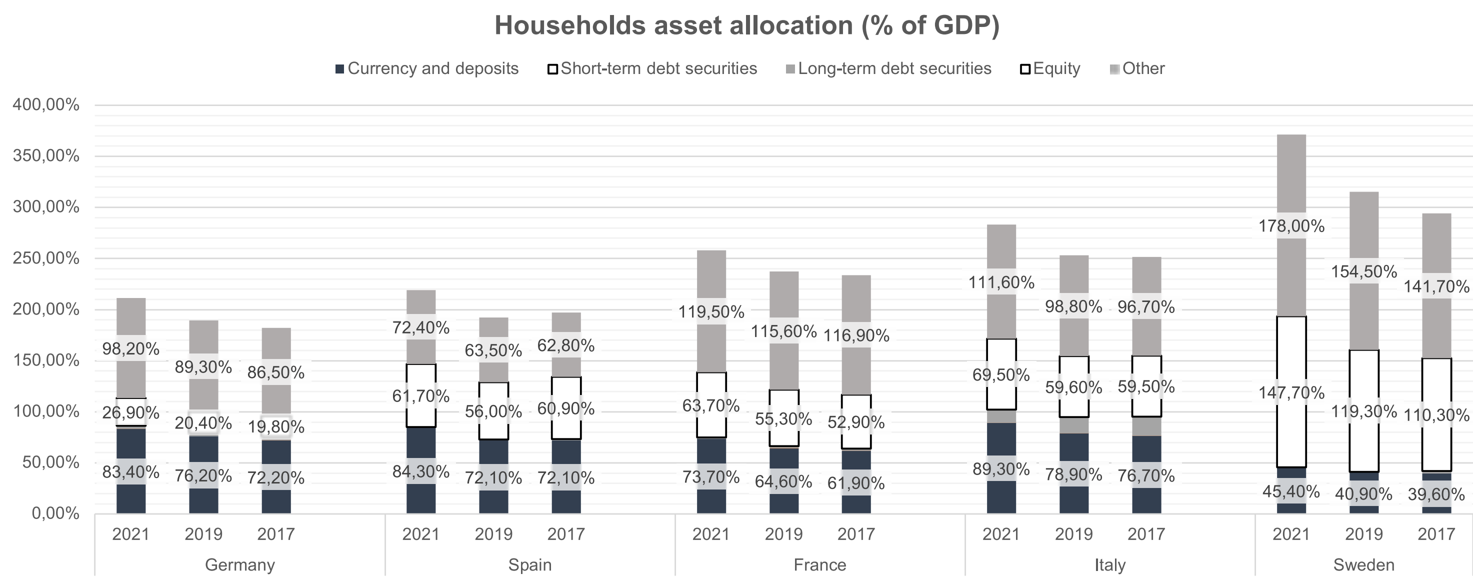
We now turn our attention to factors related to the supply of capital (savings). To gain insights, we examine the composition of households' portfolios in the U.S. and the EU, as depicted in Figure 7. A significant observation emerges: there exists a stark contrast in portfolio allocation between U.S. and European households. U.S. households allocate over 50 percent of their assets to shares, other equities, and mutual funds, indicating a greater propensity for investment in SMEs listed in growth markets. In contrast, European households exhibit a different pattern, with more than 50 percent of their assets allocated to currency and deposits, as well as insurance and pension schemes. This allocation structure significantly limits or diminishes the potential for investment in SMEs. The distinct portfolio composition between U.S. and European households underscores the greater likelihood of U.S. households having substantial investments in SMEs, while European households have limited exposure to such opportunities.

Figure 7 - Financial Assets of Households in the US and EU



Source: CEPS-ECMI available at: https://www.ceps.eu/wp-content/uploads/2019/07/Rebranding-Capital-Markets-Union.pdf)

Figure 8 - Within EU Differences in Households Asset Allocation



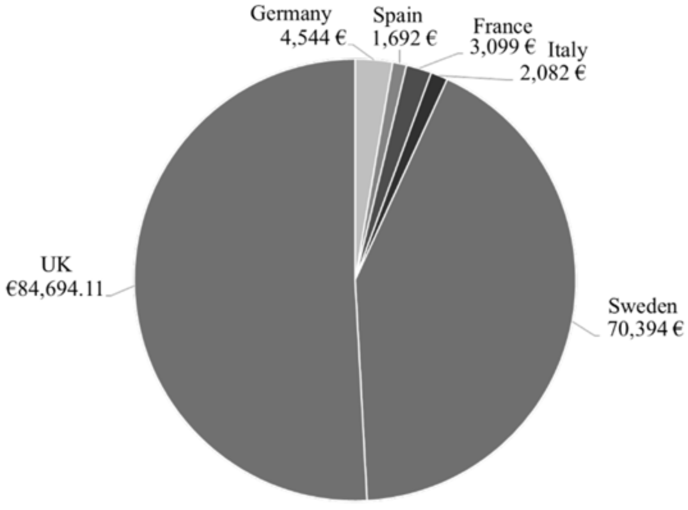
Source: Eurostat NASA_10_F_BS

Next, we turn our attention to the variations in household portfolio allocations within the EU, specifically among the five countries examined in previous sections: Germany, Spain, France, Italy, and Sweden. Figure 8 presents the portfolio allocations in different asset classes, such as currency and deposits, short-term debt securities, long-term debt securities, equity, and a residual category labeled as "other." To enable meaningful comparisons across countries, we scale the allocations by country GDPs. The figure highlights two significant observations. First, Swedish households exhibit a notably higher level of invested wealth, amounting to approximately 3.5 times the country's GDP, surpassing the other countries. For instance, in Germany, invested wealth is approximately twice the country's GDP.

While part of these differences can be attributed to varying country sizes, they also result in substantial disparities in the potential capital supply for SMEs. Second, Sweden stands out with a much larger allocation to equity, accounting for around 40% of the total portfolio and approximately 150% of the country's GDP. In contrast, the other countries exhibit comparatively smaller allocations to equity in terms of both portfolio fraction and GDP percentage.

Figure 9 reinforces the previous findings by presenting per-capita household financial investments in the five EU countries. It provides additional evidence supporting the observations depicted in Figure 8. Furthermore, the figure includes data on the per capita financial investment for households in the UK, which amounts to approximately 85 thousand euros (about one-quarter of their average net wealth), demonstrating its substantial level of investment.

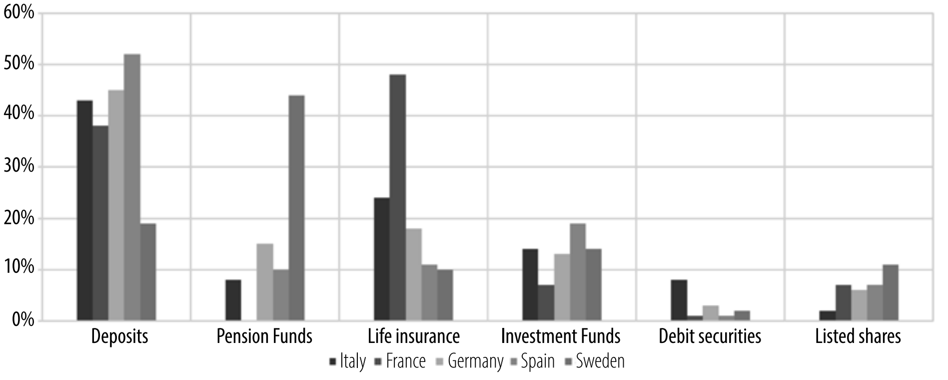
Figure 9 - Households Financial Investment, per capita, by Country



Source: ECB Households Report 2022

There are significant variations in the breakdown of financial assets held by households across the countries in the EU, as reported in Figure 10. Deposits constitute approximately 40 percent of financial assets in Italy, France, Germany, and Spain, but account for less than 20 percent in Sweden. On the other hand, listed shares, representing direct ownership of equities, make up more than 10 percent of financial assets in Sweden, while remaining below 5 percent in the other countries. Swedish households allocate around 40 percent of their financial wealth to pension funds, providing indirect exposure to equities. Similarly, French households also allocate approximately 40 percent of their financial wealth to life insurance investments, which are typically low-risk and predominantly invested in highly-rated fixed income assets. In contrast, households in the other countries have smaller allocations in pension funds and life insurance investments. Italian households also have direct investments in debt securities, likely consisting of holdings in Italian government bonds, influenced by the substantial level of public debt in Italy.

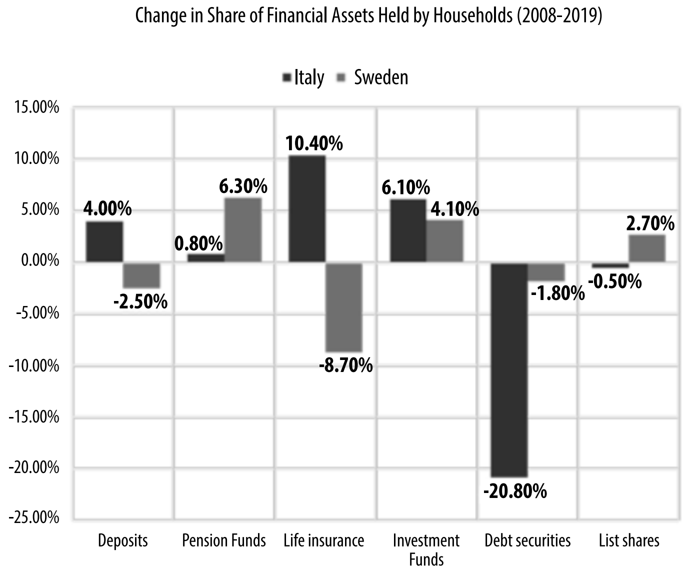
Figure 10 - Share of financial assets held by EU households

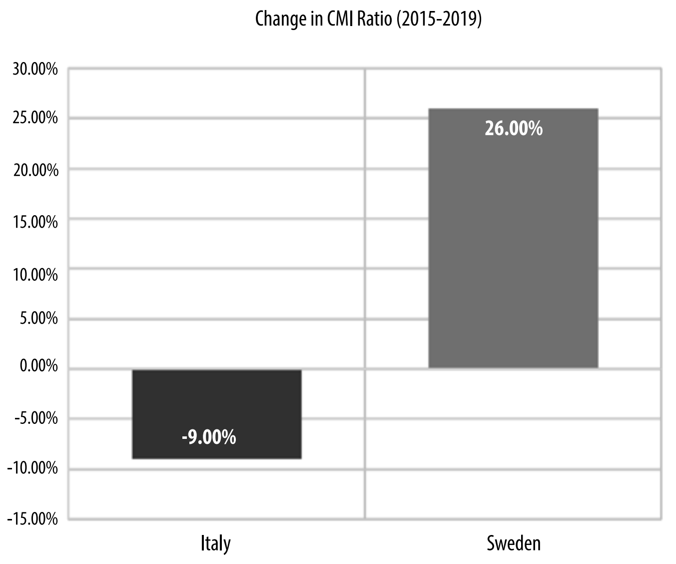


Source: Data is from the European Fund and Asset Management Association and available at: https://www.efama.org/sites/default/files/files/KPI%20Report_FINAL%20version%20%281%29_1.pdf

The preceding discussion has analyzed the latest data, but it is also insightful to examine the evolution of portfolio allocations among European households. Figure 11 presents this information by focusing on two countries, Italy and Sweden. In the left panel, we illustrate the changes in allocation across categories from 2008 to 2019. It is worth noting that Italian households increased their allocation to deposits (+4%), life insurance deposits (+10.4%), and investment funds (+6.1%), while reducing their allocation to debt securities (-20.8%). On the other hand, Swedish households exhibited more stable allocations, with modest increases in pension funds (+6.3%), investment funds (+4.1%), and listed shares (+2.7%), and a decrease in life insurance investments (-8.7%). These shifts in allocations correspond to a risk profile reduction for Italian households (-9%) and an augmented risk profile for Swedish households (+26%). To measure the changes in risk profiles, we provide the CMI ratio in the right panel, which represents the ratio between savings invested in capital market instruments and those held in deposits.

Figure 11 - Evolution of Portfolio Allocations and Risk Profiles of Italian and Swedish households





Source: Data is from the European Fund and Asset Management Association and available at: https://www.efama.org/sites/default/files/files/KPI%20Report_FINAL%20version%20%281%29_1.pdf

We also examine the impact of financial education on the supply side. It is widely supported by empirical academic research that financial education is linked to more sophisticated portfolios, which often have a higher risk profile and a greater exposure to equities. In Figure 12, we present the share of financially literate adults in the countries included in our analysis, with darker colors indicating a larger share. It is noteworthy that households in Sweden, as well as Germany, exhibit the highest levels of financial literacy, while Italy has the lowest. These proportions align with the risk profiles associated with the portfolio allocations discussed earlier.

Figure 12 - Financial Literate Adults

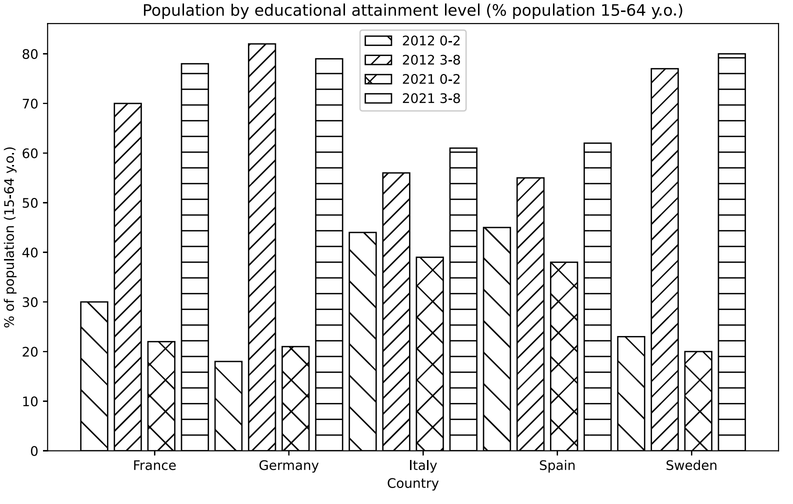
Source: Data is from Eurostat

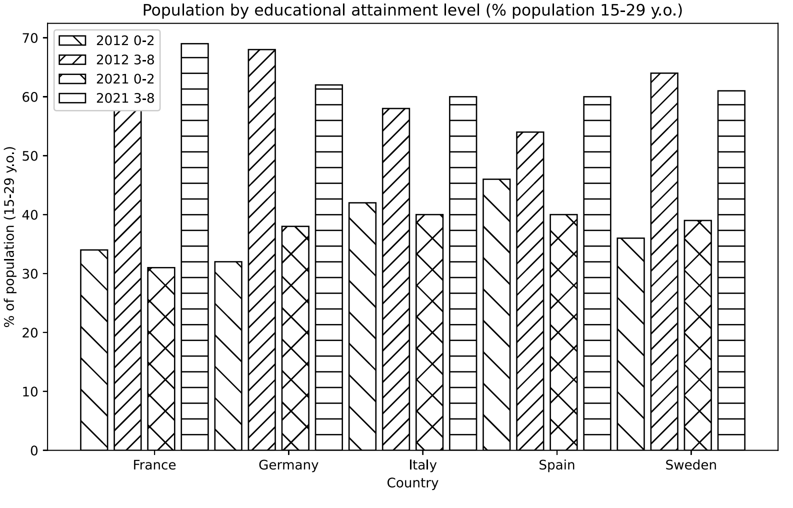
By examining Figure 13, we can draw a similar conclusion regarding the influence of educational attainment. These figures illustrate the population categorized by educational attainment level as a share of the total population. The empirical academic literature highlights that disparities in education are associated with variations in labor income and the propensity to participate in financial markets. Education levels 0 to 2 represent less than primary, primary, and secondary education, while levels 3 to 8 represent upper secondary, post-secondary, and non-tertiary education. The left panel of Figure 13 demonstrates that among the working-age population (aged 15-64), Italy and Spain have the lowest average education level, while Germany and Sweden have the highest. Although the gap between countries has narrowed between 2012 and 2021, it has not completely disappeared. The right panel of Figure 13 reaffirms the trend of closing the gap among countries by presenting the same shares for individuals aged 15 to 29.

We analyze the investment component as a crucial aspect of supply factors. Specifically, we examine the investment share of GDP across three institutional sectors: business, government, and households. A higher investment share is typically indicative of higher economic growth, with business investment considered more productive than government and household investment. Figure 13 reveals an intriguing pattern in this regard.

Sweden exhibits the highest total investment share of GDP, approximately 25 percent, closely followed by France. Italy and Spain lag behind by 5 percentage points. When considering investment composition, business investment holds the greatest significance in Sweden. The country also features interesting figures regarding government investments, in a virtuous public-private interaction. In contrast, France, Germany, and Italy show relatively larger shares of household investment, while business investment remains the dominant component in these countries as well. The role of government investments is lower in Italy, Spain and Germany.

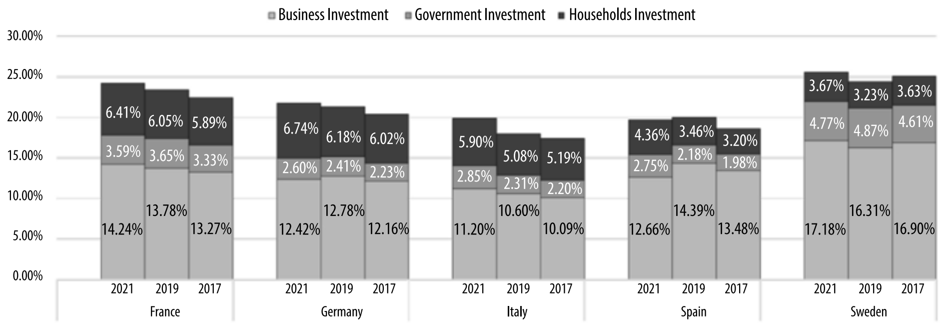
Figure 13 - Population by educational attainment in selected countries in the EU





Source: Data is from Eurostat

Figure 14 - Investment share of GDP by Institutional Sectors

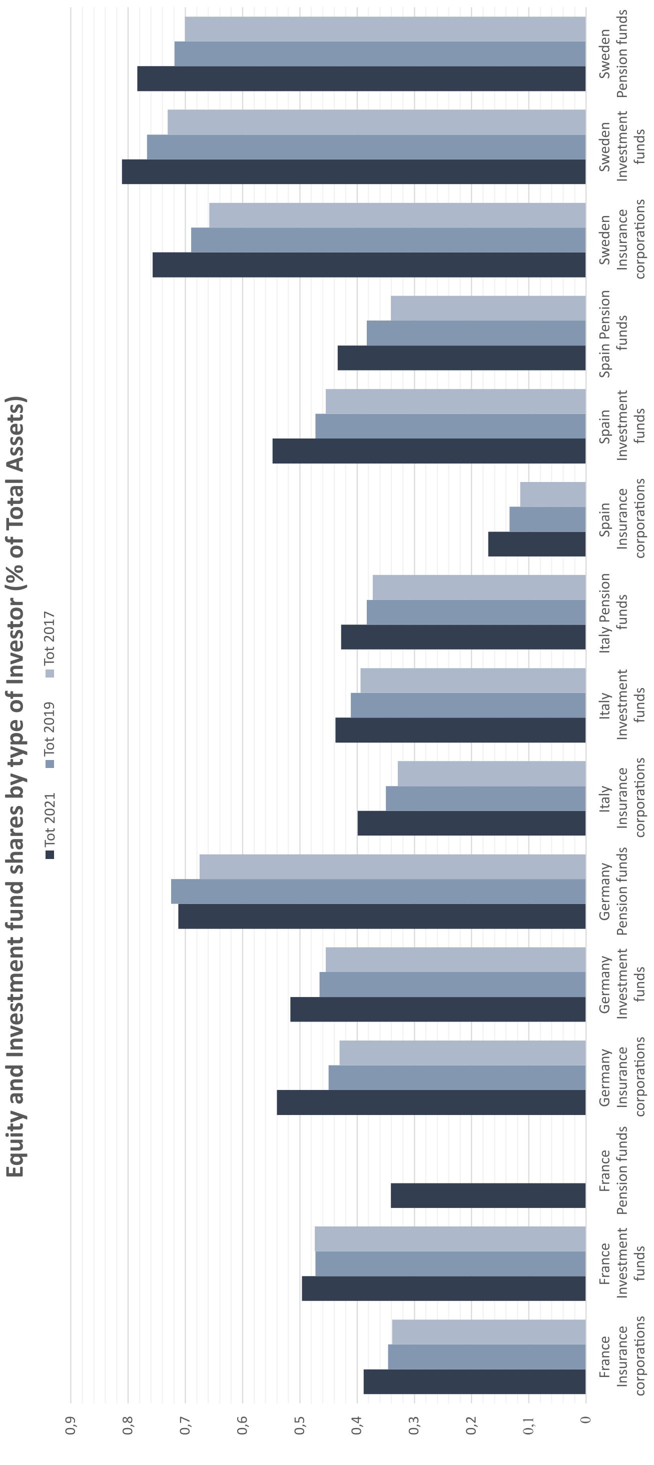


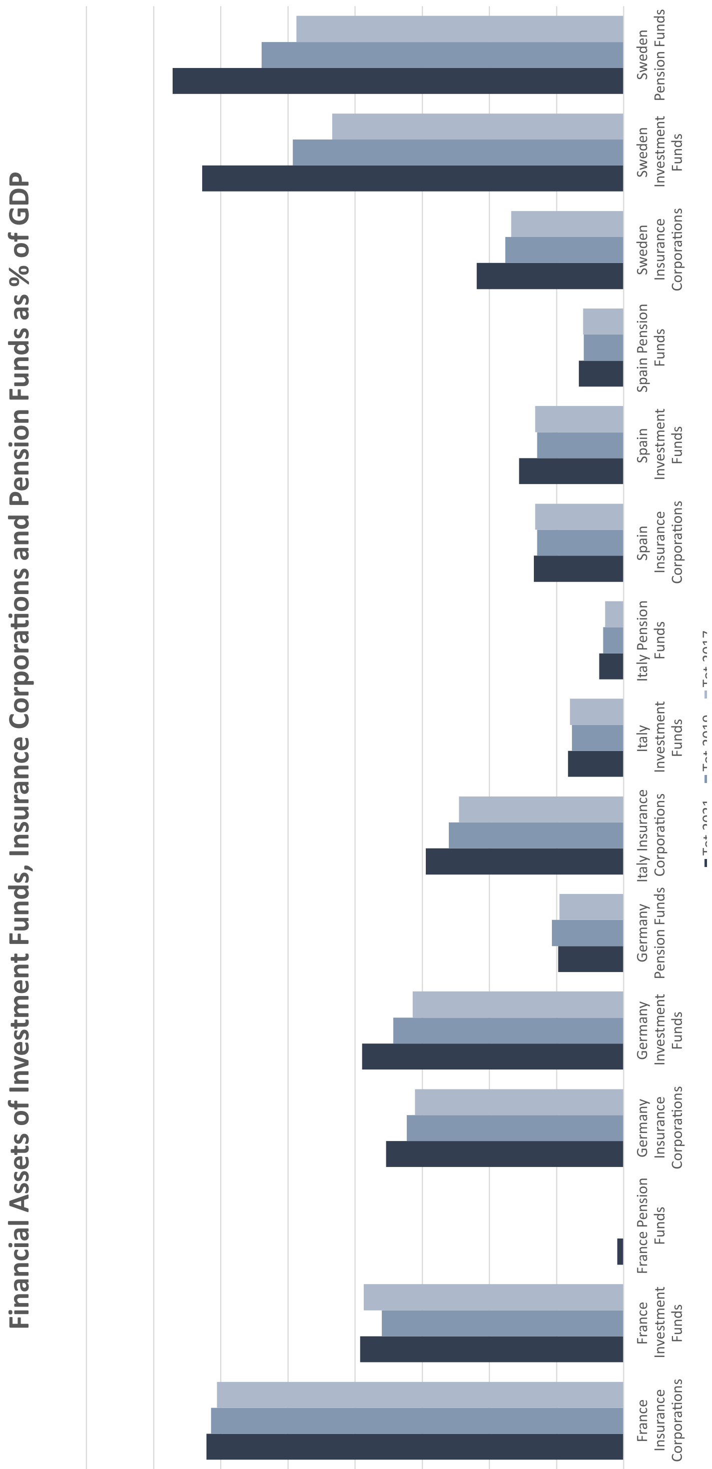
Source: OECD Institutional Investor Statistics 2020

Institutional investor portfolios play a crucial role in the investment landscape, particularly regarding investments in SMEs. Institutional investors possess desirable characteristics such as long-term investment horizons, lower liquidity requirements, and expert management, making them well-suited for such investments. Figure 15 provides valuable insights into these institutional investors' portfolios across the analyzed countries. The left panel considers shares with respect to total assets, and the right panel shares by GDP.

A clear observation emerges from the data. In Sweden, insurance corporations, investment funds, and pension funds allocate a substantial share of their total assets to equities, amounting to approximately 80 percent. In contrast, the shares allocated to equities by these types of investors in the other countries are significantly smaller. For instance, in Italy, the shares consistently remain below 40 percent. Consequently, the figure highlights notable differences in the risk profiles of institutional investors across the analyzed countries. These differences translate into varying levels of capital supply to equities, including SMEs. Countries like Italy and Spain exhibit relatively smaller supplies of capital, underscoring one of the reasons behind the significant disparities observed in their respective growth markets. This evidence underscores the importance of supply factors in understanding the divergent performance of growth markets across countries.

Figure 15 - Equity and Investment Shares by Type of Investor





Source: OECD Institutional Investor Statistics 2020

4. Capital markets union and public policies for the growth of SMEs

Institutional features of the EU can be central for the growth of SMEs. In particular, the European Directive on the Capital markets union (CMU) has the potential to significantly contribute to fostering the growth of SMEs. The CMU aims at creating a single, integrated capital market across EU member states, removing barriers and facilitating access to financing for businesses, particularly SMEs. Here are several ways in which the CMU can be helpful in fostering SME growth:

1. Improved Access to Financing: One of the key objectives of the CMU is to enhance access to diverse sources of financing for SMEs. By harmonizing regulations and facilitating cross-border investment, the CMU can enable SMEs to access a wider pool of capital from investors across the EU. This can include venture capital, private equity, and crowdfunding, providing SMEs with the necessary funding to expand their operations, invest in innovation, and create jobs. Note that that a further benefit is related to the increased diversification opportunities for the suppliers of capital, which could contribute to reduce the cost of capital.
2. Simplified Regulatory Framework: The CMU aims to streamline and simplify the regulatory framework for capital markets within the EU. This can significantly reduce compliance costs and administrative burdens for SMEs, making it easier for them to raise funds and access capital markets. By harmonizing disclosure requirements, prospectus rules, and listing procedures, the CMU can create a more efficient and cost-effective environment for SMEs to navigate the capital markets.
3. Development of Growth Markets: The CMU encourages the development of specialized growth markets tailored to the needs of SMEs. These markets, often referred to as SME growth markets or scale-up platforms, provide a platform for SMEs to list and raise capital from

investors who are specifically interested in supporting the growth of smaller companies. By establishing supportive frameworks and lighter listing requirements, SME growth markets can attract both domestic and international investors, providing SMEs with an avenue to access capital in a more favorable environment.

4. Investor Protection and Confidence: The CMU places a strong emphasis on investor protection and fostering investor confidence. By enhancing transparency, disclosure standards, and investor rights, the CMU aims to create a safer and more trustworthy investment environment. This can be particularly beneficial for SMEs seeking capital, as it can attract a broader range of investors who may have been hesitant to invest in smaller businesses due to perceived risks. Increased investor confidence can lead to more capital flowing into SMEs, supporting their growth and expansion.

Overall, the European Directive on the Capital markets union holds great potential for fostering the growth of SMEs in Europe. By improving access to financing, simplifying regulations, developing growth markets, and boosting investor protection, the CMU aims to create a more supportive and conducive environment for SMEs to thrive. By unlocking the potential of capital markets and facilitating investment in SMEs, the CMU can drive innovation, create jobs, and contribute to the overall economic growth of the European Union.

Furthermore, ESMA (European Securities and Markets Authority) plays a crucial role in promoting the growth and development of SMEs in the European Union. As the EU's independent authority responsible for providing guidelines and technical standards to the European Commission, ESMA plays a vital role in promoting a favorable regulatory environment for SMEs to access capital markets. By supporting harmonized regulations and guidelines, ESMA should ensure that SMEs have equal opportunities to raise funds and access financing through capital markets.

One of the key challenges faced by SMEs in accessing capital markets is the complexity and cost of regulatory compliance. SMEs often struggle with meeting the stringent requirements imposed by capital market regulations, as they may lack the resources and expertise necessary for compliance. ESMA's role in developing guidelines aimed at streamlining regulations specific to SMEs is crucial in addressing these challenges. By tailoring regulations to the unique characteristics and needs of SMEs, ESMA can promote the diffusion of lower barriers to entry and a reduction of the administrative burden for these businesses, making it easier for them to access capital markets.

ESMA also plays a vital role in ensuring investor protection and maintaining market integrity when it comes to SME listings. Given the typically higher risks associated with investing in SMEs, it is important to have robust investor protection measures in place. ESMA's supervision and oversight help safeguard the interests of investors, ensuring transparency, fairness, and adequate disclosure of information related to SME listings. This fosters investor confidence and trust in the market, which is essential for attracting investment into SMEs.

Moreover, ESMA's efforts in promoting market integration across the EU are crucial for SMEs. By harmonizing regulations and standards across member states, ESMA facilitates cross-border investments and listings, enabling SMEs to access a larger pool of investors and capital. This enhances the growth prospects of SMEs and contributes to the development of a more unified and efficient capital market in the EU.

Unfortunately, while we write this study, we have to underline that the project of CMU somehow lost part of its momentum and needs renovated effort to be effectively empowered and brought to conclusion. Similarly, ESMA did not succeed yet in promoting clear and homogeneous standards widely and uniformly adopted in European exchanges, leaving excessive space and bureaucratic powers to national and local authorities. Given the role of economies of scale (and of scope) in attracting investors, services and liquidity in financial markets, the degree of integration among exchanges in the

EU needs to be considerably reinforced if Europe does not want to entirely delegate most of the activities in regulated financial markets to Anglo-Saxon countries.[5]

Ambitious targets at the European level need to be associated with strong intervention powers at the same European level. This requires further delegation from the single member countries to the center, which proved to be crucial for the resilience of the European banking system during the COVID pandemic (see, e.g., Borri and Di Giorgio (2022)). However, it is not clear that this is the common political vision today.

4.1 Public policies for the growth of SMEs

Public investment funds, such as sovereign wealth funds and state-sponsored funds, and incentives for pension funds and other institutional investors, play a crucial role in financing the growth of SMEs and can contribute to their listing on growth markets. These types of institutional investors have significant financial resources and long-term investment horizons, making them well-suited to support the growth and development of SMEs, acting as anchor investors.

State-sponsored funds, typically established by governments to manage their surplus funds and/or manage strategic assets (e.g., military contractors, natural monopolists, etc.), have the capacity to provide patient capital and strategic investments to SMEs. By deploying capital from state-sponsored funds into SMEs, these funds can facilitate their expansion, innovation, and internationalization efforts. This injection of capital can support SMEs in scaling up their operations, developing new products or services, and accessing new markets. Additionally, the involvement of state-sponsored funds can

5 In a recent speech, ECB President Christine Lagarde said "a truly European capital market needs consolidated market infrastructures". She further added that Europe tried to create a "capital market union" for more than a decade but "we have so far failed to advance" and that ESMA should have "a broad mandate, including direct supervision" (see "Europe needs its own SEC, says Christine Lagarde, *Financial Times*, November 17 2023).

enhance the credibility and reputation of SMEs, attracting other investors and stakeholders. In many successful listing stories, it has been crucial the role of a cornerstone investor. State-sponsored funds might play such a role, but in the case of SMEs the same role could as well be played by other subjects, such as arms of state development agencies or even local public financial entities. Note that the investment by state-sponsored funds, or public investment funds more in general, into SMEs can be rationalized by the objective of an efficient diversification and risk-adjusted performance, which should complement the positive externality that the growth of SMEs can offer to the overall economy, for example in term of R&D expenditure and innovation.

Incentives for pension funds can also play a crucial role in financing SME growth. Pension funds are long-term investors with a focus on generating stable returns to support retirees. Encouraging pension funds to allocate a portion of their portfolios to SME investments, implementing specialized tailored asset allocation strategies, can provide a sustainable and stable source of financing for these businesses. By diversifying their investments to include SMEs, pension funds can potentially achieve higher returns while contributing to economic growth and job creation. Governments can provide incentives, such as tax breaks or regulatory adjustments, to encourage pension funds to invest in SMEs, ensuring a favorable investment environment for these institutional investors. Further, government, and government agencies, can offer guarantees to investors, for example by implementing caps to the maximum losses.

Some dedicated incentives or risk reduction guarantees might be also extended, if allowed by the public finance conditions, to dedicated ETFs or active funds for European SMEs, knowing that reaching a desirable size of the market might ask for alliances or consolidation between different exchanges in order to augment both supply and demand for capital. The diffusion of European-wide liquid benchmark indices for the aggregate growth market could facilitate the indirect investment into SMEs, by both retail and smaller institutional investors, through ETFs and passive funds. Further, many institutional investors, such as pension funds and insurance companies, are typically passive investors which track benchmarks. For these investors, the availability of a Euro-wide representative index for growth markets could facilitate investment and interest in otherwise fragmented growth markets. Market infrastructures may be differentiated along size or sector dimensions with the idea of progressively moving towards one European capital market. If governed appropriately, this might also induce cost reductions in listing requirements linked with the associated economies of scale.[6]

The financing provided by public investment funds and the set of incentives for pension funds as well as for retail investors who chose to enter the segment of equity growth markets via dedicated mutual funds can help SMEs overcome the challenges they often face in accessing capital. By leveraging the financial resources and expertise of these institutional investors, SMEs can receive the necessary funding and support to expand their operations, invest in research and development, and enhance their competitiveness. This can boost their credibility and increase their chances on the global markets. Moreover, being listed may provide SMEs with further opportunities for accessing capital, in what could somehow become a virtuous and circular substitution between public and private capital.

At this regard, we believe that the InvestEU IPO initiative, implemented by EIF under the InvestEU Fund, is of great importance as "*it is aimed to support EU enterprises access to public equity markets. [.] The ultimate general policy goal of the Invest EU IPO Initiative is to support companies considering a public listing and listings of companies on EU trading venues".*[7] The recipients of the resources made available by EIF will be financial intermediaries and special-

6 A recent OECD publication ("Institutional Shareholding, Common Ownership and Productivity: A Cross-Country Analysis", August 2023) reveals the growing importance of institutional investors, with a share of market capitalization that increased from 35 in 2010 to 45 in 2019, and reached levels close to 70% in the US. The study also reveals the rising importance of passive investing, which accounts for 30% of the investment funds assets in Europe and 40% in the US (see Figure 4 in the OECD publication available at: https://one.oecd.org/document/ECO/WKP(2023)23/en/pdf). Further, since 2007, equity flows into active funds have progressively declined while they increased for passive funds.

7 For details, see the Annex to the InvestEU Initiative https://www.eif.org/InvestEU/equity_products_calls/annex-iv-ipo-addendum-termsheet.pdf

ized funds, which have an investment strategy focused on pre-IPO, IPO and post-IPO. These institutions, acting as anchor investors and investing in pre-IPO, can provide patient capital and stability in the shareholding structure.

Finally, it is important to stress that providing SMEs with the necessary capital to fuel their growth contributes to the overall growth of the economy, the development of countries, fostering innovation, job creation, and ultimately economic prosperity.

5. Conclusions

This paper discusses the difficulties that SMEs face in order to finance their activity and growth. We move from the scarce dimension of most equity growth markets in Europe and highlight some factors contributing to the anemic state of both the demand and supply of capital in the market.

We are aware that such factors ask for gradual progress in order to be overcome and create a financial ecosystem more open to equity markets and culture. Some steps in the right direction have been undertaken. However, it is important to recognize that once again Europe does not necessarily share one view. The ambitious targets of the CMU need to be accompanied by strong intervention powers and the role of domestic agencies and market infrastructures revisited and properly discussed and eventually modified. A European approach would avoid aggressive tax competition at the single member state as well as competition in laxity to attract more companies, while allowing to reach the benefits of proper dimensions and market efficiency. The alternative is to keep following the US from much behind.

On the demand side, a significant challenge lies in the current severe fragmentation of public markets. The fragmentation results in a very small number of enterprises approaching the public markets, in higher costs, lower valuations, reduced liquidity, and limited market capitalization, all of which can hinder the growth and development of businesses. To effectively address this issue, efforts should be directed towards reducing fragmentation and promoting consolidation in the public equity markets. By doing so, costs can be lowered, liquidity can be increased, and the market capitalization can expand. Moreover, this would also boost the trading activity on the secondary market providing a more favorable environment for businesses to thrive.

On the supply side, there are several measures that can be taken to stimulate investment and increase demand for equity instruments. One approach is to provide incentives to individuals to invest in equity through tax-advantaged retirement accounts and other similar mechanisms. By providing tax benefits for private pension investments in equity instruments, individuals are encouraged to allocate their savings towards long-term investments in the market, contributing to increased demand.

Financial education also plays a crucial role in boosting demand. By improving financial literacy and educating individuals on the benefits and risks of investing, more people can make informed decisions and become confident investors. This can lead to increased participation in the equity market, driving demand and contributing to a more vibrant investment ecosystem.

Additionally, government-sponsored institutional investments, such as the establishment of sovereign wealth funds, or local financial entities, or arms of state development agencies, can have a positive impact on the demand side, supporting an increasing number of financial intermediaries and investment funds with strategies, professional skills and track-records in European SMEs either in the pre-IPO, IPO stage or in the post listing development. These investments can inject significant capital into the market, creating a favorable investment climate, and attracting further participation from other kind of investors. By leveraging government resources, these investments can provide stability and support to the market, driving demand for equity instruments.

Within this framework, Italian and EU SMEs mirror the countries industrial system, characterized by a multitude of small firms, and face challenges in the markets where competitive strategies and appropriate sizes are essential. The capital markets offer fundamental opportunities to SMEs as far as capital raising, business diversification, resilience and flexibility.

In summary, while the proposed changes are welcome and have the potential to address some aspects of the anemic demand and supply in the market, it is crucial to recognize that a comprehensive solution requires tackling the fragmentation of public markets on the demand side. Additionally, measures such as tax-advantaged retirement accounts, more financial education, and government-sponsored institutional investments can help stimulate the supply of capital and create a more robust investment environment. By addressing both sides of the equation, a more sustainable solution can be achieved to improve market dynamics and foster economic growth.

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