EURONEXT

MEMO

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Subject **Position Paper on the EU SME Growth Markets Consultation**

In December 2017, the European Commission published a public consultation[1] on potential measures to strengthen the attractiveness of MIFID II's **'SME Growth Markets'**, with a view to introducing targeted amendments to relevant pieces of EU legislation as part of the Capital Markets Union Action Plan.

The consultation focused on **four main areas**: (i) *challenges faced by public markets for SMEs*; (ii) *specific regulatory barriers (MIFID II related)*; (iii) *alleviation of administrative burden on SME Growth Market issuers (MAR[2] related)*; and, (iv) *fostering local ecosystems for SME Growth Markets and enhancing liquidity*.

This position paper summarises the Euronext view on points (ii), (iii) and (iv) in detail in the following sections, while providing an initial overview below of the challenges faced by public markets for SMEs across the Euronext jurisdictions.

(i) An overview of the challenges faced by public markets for SMEs in the Euronext jurisdictions

Euronext shares the Commission's assessment on the three main drivers behind the weakness of EU public markets for SMEs, **ranked in this order of priority from our experience**:

(i) Local ecosystems that are able to support companies at the Initial Public Offering (IPO) stage are under pressure in many Member States;
(ii) Lack of institutional and retail investors for SME financial instruments; and,
(iii) Weak pipelines of companies seeking a listing.

However, it is important to note that an analysis of each **local Euronext market reveals important differences** which need to be taken into account in terms of the overall assessment. Moreover, the factors are interlinked and cannot be easily distinguished in terms of causes or consequences on each individual local ecosystem. For example, the impact of low levels of liquidity on brokers' business models and investors' appetite for SME instruments are, in our view, the consequences of the decline of ecosystems surrounding the local exchanges, rather than the cause of the decline. In addition, while many themes are shared across countries, the exact way the factors interlink is shaped by each local ecosystem. A more detailed assessment per Euronext jurisdiction is included in the **Annex**.

An important conclusion for policymakers is that these differences – even within a group such as Euronext – underpins the need for exchanges to retain flexibility in their operations to implement tailored solutions for the specific needs of their SME public capital markets.

- **Decline of local ecosystems**

Euronext shares the Commission's assessment that the **network of SME specialists surrounding the local exchanges are under pressure** in many Member States.

[1] European Commission Consultation on building a proportionate regulatory environment to support SME listing
[2] MAR – Market Abuse Regulation

While regulatory and technological changes over the last decade and a half have led to trading becoming more automated, efficient, and inexpensive, there has also been a weakening of the local ecosystems, notably the smaller brokers, market makers, liquidity providers and boutiques specialised in SMEs.

Traditionally, these actors have been incentivised to invest time and resources into building the demand for smaller IPOs. However, these ecosystems have generally been impacted negatively by a range of factors, not least the MiFID framework on the regulatory side, although in different ways across countries. This underpins the need for tailored responses to this challenge.

- **Lack of institutional and retail investment in SME financial instruments**

Euronext agrees with the Commission that there is a lack of institutional and retail investor appetite for SME financial instruments. In our view, this is notably due to a **visibility deficit** on SMEs (arising, for instance, from insufficient research coverage) and challenges in respect of **liquidity** (currently concentrated around blue chips).

The lack of institutional and retail investment can also be explained by **regulatory barriers to investment in SMEs**. These barriers include factors such as the **restrictions in UCITS** limiting institutional investment in SME shares and bonds. Under the framework, mutual funds can only invest in a given company up to a low percentage – 5% or 10% of outstanding equity – often implying a very small ticket which does not necessarily justify the allocation of resources and focus by market participants.

We believe this is an area where changes to the EU framework could be considered to allow for specific funds and/or products and larger investments in SMEs, which would greatly benefit this segment. In addition strong fiscal incentives such as tax breaks are required at national level to encourage investors to invest in smaller growth companies. Conversely, it is not our experience that differences in local accounting standards are hindering cross-border investment in any meaningful manner.

- **Weak company pipeline**

Euronext agrees with the Commission's assessment that SMEs face high compliance costs to be listed on a market, making **other financing avenues** – primarily bank and private equity based – a strong alternative across Euronext locations.

For smaller companies in particular, the transition to being publicly quoted and complying with the relevant exchange requirements and EU / national securities law is demanding. These obligations can have a significant impact on companies' resources in terms of management time, complexity and resulting cost burden. This can be all the more challenging where key individuals within smaller companies can carry multiple roles and where there may be no designated company secretary or compliance function.

In supporting initiatives at EU and national level to identify and remove unjustified regulatory obstacles to small companies accessing public capital requirements, Euronext has created programmes - **IPOready** and **TechShare** - to raise awareness of public capital markets' financing among smaller companies. In parallel, the Exchange has also launched a **FamilyShare** programme specifically designed to inform family businesses on the financing solutions offered by the exchange and public capital markets.

The rest of this paper provides Euronext's assessment and recommendations on potential regulatory amendments to MiFID II and MAR to support strengthened public capital markets for smaller companies, within the context of the preparation of the EU Growth Market initiatives.

(ii) Making a Success of the SME Growth Market Concept

i. <u>Definition of an SME Growth Market and Growth Market issuers</u>

An SME Growth Market under MiFID II is defined as an MTF where at least 50% of the issues are SMEs. In terms of **equity issuers**, SMEs are defined as companies with a market capitalisation of less than €200m over the three previous years, while **debt-only issuers** are subject to a narrower definition originating from the Prospectus Regulation and included within the MiFID II Level 2 framework[3].

While Euronext does not believe that any changes are required to the 50% requirement for SME issuers on SME Growth Markets, we are of the view that the current SME definitions for both debt and equity issuers should be revised.

Debt-only issuers on SME Growth Markets

Euronext believes that the application of the SME definition from the Prospectus Regulation limits the scope for SMEs to issue debt-only instruments on SME Growth Markets and would therefore support proposals to amend the current criteria for non-equity SME issuers in the MiFID II Level 2 Delegated Regulation. In so doing, we believe the application of **a single issuance criterion** would be better suited to covering the specificities of bond issuance, rather than applying a total balance sheet or an annual net turnover threshold.

In contrast, Euronext does not support maintaining **a 'number of employees' criterion** as it would not reflect the fact that SMEs from certain industry sectors employ considerably more employees than others as part of their business models, e.g. the food industry, transport and logistics sectors.

Euronext Recommendation:

In revising the definition for issuers of debt-only instruments on SME Growth Markets, Euronext would support an amendment of the MiFID II Level 2 Delegated Regulation to replace the existing criteria with a single criterion focused on issuance. We suggest the limit could be set on the basis of a cumulative issuance amount of €50m in a given year (over the past 12 months).

Equity issuers on SME Growth Markets

Euronext has consistently **advocated in favour of an increase to the current MiFID II SME definition for equity issuers** as companies with a market capitalisation up to €200m. This position is driven by both listing statistics from the Euronext markets which show that midcaps would benefit from such an increase, as well as from a recognition, in line with the Commission's assessment in the consultation, that there is a misalignment between the MIFID II SME definition and the approach applied to asset managers of equity funds and indices. Moreover, the MIFID II SME definition is not aligned with the approach under the ELTIF Regulation where SMEs are defined as companies with a market capitalisation up to €500m.

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[3] The issuer shall be deemed an SME if it meets at least two of the three following criteria in line with the definitions in the Prospectus Regulation ((Art 2 (f)(i)) and MIFID II Level 2 framework (Art 77(2) of Delegated Regulated 2017/565) where SMEs are defined as having : an average number of employees during the financial year of less than 250; a total balance sheet not exceeding EUR 43 million; and an annual net turnover not exceeding EUR 50 million.

Euronext Recommendation:

Euronext would welcome an adjustment to the MIFID II SME definition for equity issuers in order to increase it to €500m. In our view, this represents a pragmatic approach in terms of both recognizing the current nature – and future growth prospects – of European SME markets, as well as aligning the definition with other relevant provisions in EU legislation. This would contribute to a strengthening of SME Growth Markets' ability to attract more and larger companies, with the consequent potential to increase liquidity on these markets.

In addition, Euronext would also welcome a legislative amendment of the MiFID II regime to introduce the concept of a **tentative market capitalisation.**

In the case of public offers by SMEs which are immediately followed by an admission to trading on an MTF for SME Growth Market **for the first time**, Euronext believes a tentative market capitalization criterion for these prospective new issuers should be added in line with the SME market capitalization threshold established under the Prospectus Regulation and included within the MIFID II Level 2 Delegated Regulation. This is needed to ensure that such firms can benefit from the alleviated prospectus requirements in advance of having a formal market capitalization.

Euronext Recommendation:

Euronext would support the addition of a tentative market capitalisation clause in order to allow companies listing on SME Growth Markets for the first time to be eligible for the alleviated requirements under the Prospectus Regulation in respect of public offers they undertake at this first stage.

ii. Key Adviser Requirements

Euronext wholeheartedly agrees with the Commission's view that Key Advisors play a central role in assisting issuers, particularly in the initial phase of a listing and the period immediately beyond. It is clear that the presence of such advisors plays an important role in supporting investor confidence in the securities listed on SME Growth Markets.

Already today, Euronext requires **equity issuers** to have a Listing Sponsor (the equivalent of a Key Adviser) for admissions on Euronext Growth, our SME dedicated market. The role played by our Listing Sponsors is similar to that described by the Commission for Key Advisers, that is to say assessing the company's suitability for the market, bridging the information gap between quoted SMEs and investors and upholding the reputation and integrity of the market.

In its consultation, the Commission sought feedback on the desirability of EU level intervention on Key Advisers. In our view, the assessment of EU level intervention should take account of the fact that equivalent Key Adviser roles have already been introduced on most of Europe's SME dedicated markets and **reflect the specific nature of each local market and its ecosystem**.

Accordingly, Euronext would support an amendment of the MIFID II legislation to introduce the requirement for **Key Advisers for Equity Issuers** on SME Growth Markets, but **leave** the elaboration of minimum requirements regarding their mission and obligations to the i**ndividual market operators as opposed to outlining them in MiFID II.**

In contrast, Euronext believes the case for an EU level requirement for **Key Advisers for Debt Issuers on SME Growth Markets** has yet to be made. Euronext does not require a Listing Sponsor for SME Debt Issuers, upon neither admission nor on an ongoing basis. It is our view that the introduction of an EU requirement in respect of Debt Issuers should be conditional on a deeper market assessment as to the potential benefits as well as to evidence that such Key Advisers are being introduced systematically by market operators. In any case, nothing in the current framework prevents local markets from introducing Key Advisers for Debt Issuers in their local systems in the meantime.

Finally, the Commission sought feedback on whether the **requirement on issuers on SME Growth Markets to have Key Advisors should be time limited**, following the initial listing.

Euronext believes that, subject to the determination of these requirements being left to local market operators, it does make sense to allow flexibility for said operators to determine cases where the requirement for Key Advisors can be lifted for issuers after a period of three to four years. While this potential flexibility could be enshrined at the EU level, it is important that decisions regarding its deployment are left to market operators to determine.

Euronext Recommendations:

Euronext supports the introduction of an EU-wide requirement for equity issuers on SME Growth Markets to have key advisers. However, the elaboration of minimum requirements regarding their admission and obligations should be left at the discretion of individual market operators as it is important that the requirements can be tailored appropriately to their markets.

iii. Delisting rules on SME Growth Markets

Euronext agrees with the Commission's assessment that **there could be merit in looking at the introduction of minimum requirements for delisting by SME Growth Market issuers**. Such an initiative would reflect the fact that delisting rules do, as the Commission underlines, vary from one country to another with the potential to deter investor engagement, particularly in a cross-border context.

However, any EU initiative should be carefully designed in order to ensure that the **requirements can be calibrated at the local level**, under the responsibility of market operators and their regulators. This is essential given the fact that market depth and the size of listed companies varies from one country to the next, thereby calling into question the merits of any one-size fits all regulatory harmonisation at European level in this area.

In practice, Euronext would support the establishment of minimum EU level common standards on what delisting rules should cover, potentially in the form of a **list of selected criteria and voluntary best practices** that all trading venues could follow. At the same time, however, calibration of each criterion should remain at **local level** under the responsibility of market operators together with their regulators.

Euronext Recommendation:

Euronext would support the establishment of minimum EU level common standards on the range of delisting rules, but with significant flexibility left to the local level in terms of the specific calibration of the rules.

iv. <u>Transfer of listings</u>

Regulated Market to an SME Growth Market

Euronext generally agrees with the Commission's view that there would be merit in introducing harmonised rules at EU level on the **voluntary** transfer of listings from a Regulated Market to an SME Growth Market. We concur with the Commission's view that such an initiative would address some of the issues such transfers can raise.

In a similar vein to the approach we suggest in respect of potential EU harmonisation of delisting rules, Euronext believes that an EU framework in this context could **harmonise specific criteria and best practices** that all market operators could incorporate into their processes with it being clear that the **ultimate responsibility for the calibration of specific rules lies with the local market operators and their regulators**.

Euronext Recommendation:

Euronext would support the establishment of harmonised specific criteria and best practices at EU level on voluntary transfer of listings from Regulated Markets to SME Growth Markets, but with flexibility left to market operators and their regulators in terms of local calibration and implementation.

Transition from SME Growth Markets to Regulated Markets

Euronext understands the logic behind the Commission's position in the consultation in underlining that SME Growth Markets should only be seen as one step on the growth path of SMEs.

However, we do not believe that this 'growth path' should be enforced via the introduction of any regulatory incentives to transition to Regulated Markets. Instead, decisions on transferring to Regulated Markets should be left completely at the discretion of issuers based on their own circumstances, market requirements and state of readiness for a Regulated Market listing. Companies 'outgrowing' SME Growth Markets will be naturally incentivized to switch to Regulated Markets in order to reach a broader and more international pool of investors.

At the same time, while such transfers should not be mandatory, we believe the introduction of **an alleviated prospectus schedule** to facilitate the upgrade to the Regulated Market for issuers choosing to do so would be a helpful regulatory initiative.

Euronext Recommendation:

While issuer transitions from SME Growth Markets to Regulated Markets should not be 'enforced' by regulatory incentives, Euronext believes it would be helpful to introduce an alleviated prospectus schedule to facilitate such transitions.

(iii) Alleviating the Administrative burden on SME Growth Market issuers

Euronext shares the Commission's assessment on the **careful balance** to be struck between reducing obligations on SME Growth Market issuers on the one hand and maintaining a high level of investor protection and market integrity on these markets on the other. For this reason, Euronext would not support any broad weakening of the regulatory framework, notably in respect of the **Market Abuse Regulation (MAR)**.

However, **anecdotal feedback** we have received on the practical application of some of the MAR requirements for smaller companies suggest that they are procedurally burdensome, particularly given how prescriptive they are, and in many instances necessitate legal advice which increases compliance costs for issuers. Therefore, we agree with the Commission that tweaks can be made to lessen the burden in certain instances and summarise these points in the following sections.

In so doing, we believe that particular focus should be afforded to a consideration of whether some of the MAR requirements are **appropriate for all issuers**, particularly issuers of debt securities. In supporting the balance noted above, we believe it is important to address the fact that the application of some MAR requirements to debt-only issuers is making EU capital markets unattractive to certain types of non-EU issuers, which are increasingly choosing to list their securities outside the EU altogether.

i. Half-yearly reports for SME Growth Market Issuers

We agree with the Commission's starting point that, as a general principle, half-yearly financial reporting by issuers is welcomed by investors and contributes to attracting interest in companies. The Commission notes that some market participants have raised concerns with the half-yearly financial reporting obligation, enshrined in the MiFID II Level 2 implementing regulation, citing it as a time-consuming and costly obligation for SMEs.

As one of the market participants to have raised the issue directly with the Commission, it is important to clarify that Euronext's concern relates to the obligation for half-yearly financial reporting applying to **debt-only issuers**.

Euronext has already made it mandatory for its Euronext Growth Markets equities issuers to publish a half-yearly report although the Transparency Directive (Directive 2013/50/EU) does not apply to MTFs[4]. However, **we have lifted this requirement for bond-only issuers[5]** in line with the exemptions available under the Transparency Directive on Regulated Markets.

Unfortunately this approach is not possible within the construct of an SME Growth Market as the MIFID II Level 2 implementing measures are clear that half yearly reports are required for both equity and debt-only issuers. As such, there is **an obvious mismatch** with the approach applied to debt-only issuers on Regulated Markets – **exempted** from the half-yearly reporting obligation under the Transparency Directive – and the prospective situation on SME Growth Markets. In our view, this requires an amendment to MiFID II Level 2 to remove the requirement for debt-only issuers on SME Growth Markets.

[4] This being ahead of the Euronext Growth Markets applying for the SME Growth Market label
[5] Only yearly reports for bond issuers and no report at all for private placements of bonds with a denomination of at least €100k

Euronext Recommendation:

Euronext would support amending the relevant provisions within MiFID II Level 2 implementing rules to remove the obligation for debt-only issuers to publish half-yearly reports on SME Growth Markets, aligning the rules with those applicable on Regulated Markets via the Transparency Directive.

ii. Management's Transactions

The Commission's consultation sought feedback as to whether the management's transactions regime under MAR Article 19 represents a significant administrative burden for SME Growth Markets issuers and their managers. Moreover, the Commission asked for feedback on specific alleviations that could be made to the regime. Euronext believes that the current regime and processes do indeed represent an undue administrative burden which could benefit from alleviation in the following specific ways.

Firstly, we believe the **time limit** in which managers have to notify transactions to the issuer should be kept to 3 days. However, the timelines for notification should be revised so that the issuer has one business day to notify the market following receipt of the notification of the transactions by the PDMR[6]. Currently the issuer must also notify within the 3 days period, which is problematic if the PDMR notifies late on the 3rd day.

Secondly, we would support **an increase of the €5000 threshold** above which managers should declare their transactions. In so doing, we note that Article 19 in MAR allows NCAs to raise the threshold to **€20,000** and are aware of this already being the case for issuers in France[7]. Euronext believes there is merit in assessing whether this level could be harmonised across the EU.

Thirdly, we also believe it would be helpful if the PDMR transaction could be disclosed by way of an announcement of the main information in free text, without having to complete a prescriptive form. Lastly, the issuer should be permitted to notify the NCA of the transaction on the PDMR's behalf, rather than the PDMR having to notify the NCA directly.

While Euronext supports these changes, as highlighted by the Commission in its consultation, we are not supportive of some of the other suggestions, notably proposals to give trading venues responsibility for making managers' transactions public. In our view, the current system whereby the NCAs act as a reference source for all regulatory data works well and should not be modified.

Euronext Recommendation:

Euronext would support amendments to MAR Article 19 to give the issuer one further business day to notify the market following receipt of the notification of the transactions by the PDMR as well as harmonisation of the current flexibility of a €20,000 threshold. We would also support requiring a less prescriptive form for the PDMR notification and allowing the issuer to notify the NCA on behalf of the PDMR.

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[6] PDMR - Person discharging managerial responsibilities
[7] Article 621-18-2 in the AMF rules

iii. Insiders Lists

The Commission's consultation sought feedback from market participants on the impact of the MAR alleviation[8] for SME Growth Market issuers as regards to insider lists and whether further alleviations are required. As noted in earlier comments on the general approach to regulatory alleviations, it is important to strike the **right balance** between reducing obligations on SME Growth Market issuers and maintaining a high level of investor protection and market integrity on these markets.

Taking this as a starting point in the assessment of the options put forward by the Commission in the consultation and having consulted with part of its issuers, Euronext believes insider lists are important for each specific transaction, but agrees with the objective to make the requirements less prescriptive and onerous for issuers.

iv. Justification of the delay in disclosing inside information

The Commission's consultation sought feedback on whether SME Growth Market issuers should be exempted from the obligation of keeping a 'disclosure record' in cases where the issuer has delayed the disclosure of inside information.

Euronext believes this is an area where administrative and cost savings could be achieved for SMEs by removing the requirement to maintain a disclosure record, particularly as it may lead to reducing the frequency with which issuers seek legal advice on disclosure related matters. In addition, we are of the view that the written explanation required from the SME Growth Market issuer justifying the delay to communicate the inside information should be submitted only upon request from the NCA.

Euronext Recommendation:

Euronext would support amendments to MAR Article 17 to limit the requirements on SME Growth Market issuers in relation to delaying the disclosure of inside information.

v. Disclosure of inside information for SME Growth Market Issuers of bonds only

In responding to the Commission's consultation on the disclosure of inside information for SME Growth Market Issuers of bonds only, Euronext strongly believes that the current obligation under MAR is less appropriate for issuers that only list debt securities. The requirements give rise to unnecessary administration and legal costs and are perceived, particularly by non-EU issuers, as being an obstacle to the listing of debt securities on EU markets.

Euronext Recommendation:

Euronext would support amendments to MAR Article 17 to tailor the inside information disclosure requirements for SME Growth Market issuers of bonds only so as to make them more appropriate to such issuances. Specifically, we believe that, for debt securities, it is appropriate to only require disclosure of material information relating specifically to an issuer's capacity to meet its payment obligations under the bond. Such a change would not compromise investor protection.

[8] Article 18(6)

(iv) Fostering the local ecosystems for SME Growth Markets and enhancing liquidity

Euronext strongly shares the Commission's assessment that SME public capital markets need to be supported by **healthy ecosystems**. Policy action at EU and Member State level is required to arrest the decline of local ecosystems to the detriment of well-functioning public capital markets.

While there is a range of issues that need to be addressed in this context, we agree with the Commission that it is important to address **low levels of liquidity on SME public capital markets** since this can deter institutional investors from participating in such markets and undermine brokers' business models.

i. ‘Tick size’ regime of SME Growth Markets

The consultation sought feedback on the introduction of a **mandatory minimum tick size regime** for all markets, including SME Growth Markets, under MiFID II.

Following the first month of implementation of MiFID II, Euronext conducted a **liquidity study on shares** traded on Euronext markets[9] in order to evaluate the impact of the minimum tick size regime introduced by the new legislation. This study concluded that the impact of MiFID II's tick size regime on SME markets is **ambivalen**t: while available volumes at the best bid and offer have increased, wider spreads mean higher costs of trading for investors and create incentives to trade OTC.

However, **Euronext is of the view that it is too early to draw definitive conclusions from such studies** on whether the introduction of more flexibility on tick sizes might be beneficial to SME Growth Markets.

Euronext Recommendation:

We would recommend conducting further analysis in the future on the basis of a wider time horizon and including an assessment of the impact of tick sizes on trading patterns (average number of transactions, average trade size) as was done by the SEC in the US.

ii. Ensuring all SME Growth Market Issuers across the EU can use liquidity contracts

The Commission requested feedback from market participants as whether there would be merits in creating an **EU framework for liquidity contracts** that would be available for all SME Growth Market issuers across the EU. Currently, the MAR framework allows NCAs to adopt Accepted Market Practices (AMPs) covering the operation of liquidity contracts and ensuring that they are not qualified as market abuse under the regime.

Across the Euronext markets, the operation of liquidity contracts is **particularly prevalent in France**, with over 400 liquidity contracts between brokers and issuers on Euronext Paris. These are enabled by the AMF's use of the AMP provisions under MAR. Euronext appreciates the Commission's assessment that such AMPs have only been triggered in 5 Member States meaning that the operation of similar liquidity contracts would still be qualified as a manipulative practice by NCAs in the other countries. Moreover, Euronext shares the Commission's assessment that such a mechanism could improve the liquidity of SME

[9] This study did not take Euronext Dublin into account as it was undertaken prior to the acquisition of the Irish Stock Exchange. An updated study covering the entire Euronext group will be completed in due course.

shares and attract the interest of new investors, whilst creating more business opportunities for midcaps brokers.

Euronext Recommendation:

Euronext would support the creation of an EU framework for liquidity contracts, however, we believe that it should focus on general principles and criteria and **leave flexibility to the local level** in terms of the determination of the precise elements in the liquidity contracts.

iii. Barriers to institutional investors' participation in SME shares and bonds

In noting a range of regulatory initiatives that have been undertaken to improve the ability of institutional investors to invest in SME shares, the Commission consultation sought input from market participants on additional relevant regulatory barriers to institutional investments in SME shares or bonds listed on SME Growth Markets or MTFs.

In welcoming the Commission's focus on these issues, Euronext expressed its ongoing **support for a review of equity capital charges under Solvency II**. Currently, insurers are subjected to a 39% capital charge in respect of equities they hold in listed companies in developed markets[10]. While there is flexibility for regulators to adjust this figure, it is systematically higher than the 15% capital charge applied to debt-related instruments. We believe that further work on this issue is required with a view to assessing whether amendments to the regime are required to reduce the potential disincentives on institutional investment in shares.

In addition, Euronext believes that the MIFID II provision that **all shares on MTFs be considered complex** represents a further burden. Moreover, appropriateness tests under MiFID are not calibrated for equities and may push fund managers to focus on factors such as volatility risk rather than long-term value. There may also be national restrictions which could be reviewed to diversify and grow the investor base for SME shares. Given the above concerns, we welcome the fact that the Commission has confirmed the launch of an external study on the drivers of equity investment by insurance and pension funds.

Euronext Recommendation:

We support a reconsideration of: (a) capital charges for equities under Solvency II Review; and, (b) the status of all MTF shares as complex. Above all, we would support a prioritisation of follow-up to the external study on the driver of equity investment by insurance and pension funds.

iv. Introducing free float requirements on SME Growth Markets

The Commission consultation requested feedback from market participants on whether a rule on minimum free float should be introduced in EU legislation with criteria and thresholds either: (a) determined at EU level; or, (b) left to the discretion of the SME Growth Market operator.

We share the Commission's view that limited free float may contribute to low levels of liquidity as it may limit the opportunities of day to day trading. However **Euronext does not support the introduction of a**

[10] And 49% for other categories of shares.

rule on minimum free float in EU legislation since the definition of free float differs from one market to the next depending on local index characteristics.

Euronext Recommendation:

We recommend maintaining the status quo, with local free float rules defined at local level by market operators

Annex: Challenges Faced By SME Public Capital Markets Across The Euronext Jurisdictions

Current situation of SME-dedicated markets in the Euronext jurisdictions	
France	In France, the low number of SMEs coming to public markets is a consequence of other factors rather than a cause of a perceived weakness in EU SME dedicated markets. SMEs and midcaps are discouraged from listing on public markets due to other determining factors, such as increasing administrative burdens and higher costs of compliance with regulation. At the same time, the local ecosystem dedicated to SMEs has remained relatively robust in spite of the increased regulatory burden and structural changes, triggered notably by the MiFID framework. Such structural changes include a decline in the diversity of local market participants with the rollback of the French operations of smaller German or UK brokers to focus on their own home markets. In contrast, there is a vibrant community of retail and institutional investors in France, with around 200 asset managers dedicated to SMEs. However, while this number is significant, the total amounts that are invested in SMEs and midcaps by these asset managers remain limited.
Belgium	Similarly, in Belgium, our experience is that the low number of SMEs listing on Euronext Brussels can be explained by factors linked to structural issues within the local ecosystem. In particular, there are insufficient incentives for both SMEs to come to public markets and intermediaries, such as banks, to promote investment in these companies via public capital markets. These factors combine to erode the local SME ecosystem.
Ireland	In Ireland, the low number of companies joining public markets is related to a number of factors - the smaller size of the Irish market; the dominance of bank finance as a funding mechanism; the tendency for smaller companies to seek alternatives such as venture capital and private equity prior to even considering IPO as an option; the lack of understanding of public markets as a viable funding option; trade sale being a common exit for founders when companies reach a certain size; and the initial and on-going regulatory burdens and costs acting as a disincentive to listing. In addition, revised EU securities legislation, including MAR and MiFID II, is compounding the challenges of making public markets more attractive for smaller companies.
Netherlands	In the Netherlands, it is our experience that regulatory reform over the last decade and a half, notably the introduction of the MiFID framework has eroded the ability of the local ecosystem to support SMEs use of public capital markets. Banks have increasingly withdrawn from advising and supporting companies with a market capitalisation below €250m. For example, the recent listing of Avantium in March 2016, evaluated at €267m was referred to by Dutch banks as an example of the lowest possible market capitalisation that they were willing to support. This is however above the market capitalisation threshold for a company to be considered an SME under MiFID II. In addition, domestic investors - which were traditionally very active in investing in local SME companies - have structurally lowered their investments in the local market. This has resulted in a structural shift of investments in the domestic equity markets allowing foreign investors (primarily from the United States and the United Kingdom) to represent more than 90% of the funds invested in Dutch equities.
Portugal	Finally, in respect of Portugal the local SME market ecosystem and investors were significantly impacted by the country's 2011-2015 bailout which led to: (i) a fundamental reorganisation of the financial sector, leading to significant cost-cutting, restructuring, and industry consolidation (either as a result of bankruptcies or acquisitions by foreign players), (ii) a reduction by international investors of their exposure to Portugal and (iii) a general decrease of growth perspectives for the Portuguese economy and companies. The challenges under points (ii) and (iii) - which inter alia limited the number of companies seeking a listing and thus hindered market dynamics - have largely been addressed by the

	return of GDP growth, an increased internationalisation of the local economy and an improvement of Portugal's credit rating. However, issues remain in respect of the challenges under the first point notably in respect of the potential negative impact on SMEs resulting from MIFID II implementation. Turning to investors, traditionally there is a strong retail investor community in Portugal and historically medium and large-size operations in Portugal commonly show oversubscription ratios in both equities and bonds. However, local institutional investors are of an insufficient size to assure a steady base for a mid-sized IPO. As noted above, foreign institutional investors are re-discovering Portugal but at a slow rate.
Main factors to explain the low number of SMEs seeking an admission to public markets in the Euronext jurisdictions	
France	In France, the diversity of financing options, from bank loans to private equity provides SMEs with a range of alternatives to finance their growth. Combined with a lack of awareness on the benefits of public markets, the factors mentioned in the previous question are quite significant in explaining the relatively low number of SMEs using them to finance their growth. Moreover, SME owners – particularly in the case of family businesses – can be reluctant to relinquish a stake in the capital of their company. This contrasts with other types of companies, notably in the tech sector, where the opening up of the company to a larger pool of shareholders is not perceived as an issue at all. In contrast, the lack of preparation by companies' management is not seen as cause of the relatively low number of SMEs seeking admission on public markets.
Belgium	In Belgium, there is a similar experience with the reluctance of SMEs' owners to relinquish a stake in the capital of their company (for equity) and the distinction between family businesses and others, notably in the tech space.
Ireland	The dominance of bank finance as a funding mechanism; the tendency for smaller companies to seek alternatives such as venture capital and private equity prior to even considering IPO as an option; the lack of understanding of public markets as a viable funding option; trade sale being a common exit for founders when companies reach a certain size; and the initial and on-going regulatory burdens and costs acting as a disincentive to listing. In addition, revised EU securities legislation, including MAR and MiFID II, is compounding the challenges of making public markets more attractive for smaller companies due to onerous regulatory requirements, negative impacts on liquidity and research coverage of smaller companies.
Netherlands	In the Netherlands bank financing is available for compelling, solid, stable and well-managed SME companies: attractive prospects for listing have plenty of financing alternatives. Moreover, the cost of equity (including all costs related to regulation, compliance and documentation) is relatively high in contrast to bank financing which is still relatively cheap, depending on the structure of a company's balance sheet. Moreover, companies looking for equity finance are also able to attract private equity funding, with this source of financing representing the biggest competitor to public capital markets, together with strategic buyers looking to acquire companies to add to their current portfolio. These factors are an obstacle to the growth of SMEs listing on the local public markets. The issuance of bonds is an alternative for companies with a solid track record and consistent cash flow development. However SME companies are not always able to comply with the conditions that investors in bonds require.
Portugal	In Portugal, the main hurdle to equity listings - from a company's perspective - remains cultural: traditional - mostly family owned - SMEs are very prudent on sharing control. This factor is compounded by a lack of financial knowledge which creates a lot of misconceptions regarding listings. Turning to bonds, the current low-interest-rate environment makes bank

	loans very competitive and even cheaper than an SME bond, decreasing bonds' value proposition. This may change if and when quantitative easing conditions change and rates increase. Tax incentives in favour of equity could lead companies to a more balanced capital structure, which would also benefit capital market alternatives to bank financing.
Main factors that inhibit institutional and retail investments in SME shares and bonds in the Euronext jurisdictions	
France	In France, the key missing ingredient is visibility on companies, but not necessarily the instruments being offered to the public and/or admitted to trading. This visibility deficit is linked to insufficient research coverage of SMEs, leaving investors with little information and visibility on investment opportunities in this area since SMEs are not (yet) identified as an asset class in the French savings and investment ecosystem and are therefore not within the scope of retail investors' financial decisions. In contrast, it is not in our experience that differences in local accounting standards hinder cross-border investment. In practice, companies on Euronext Growth have a choice between local GAAP and IFRS depending on whether they are seeking international exposure and wish to attract cross-border investors. Regulatory constraints on investors are, however, a determining factor, notably as a result of capital charges imposed under Solvency II on investments in equities. Liquidity, in turn, is an important factor for institutional investors – especially for fund managers - but not for retail investors. Finally, tax incentives have been put in place in France (PEA, PEA-PME) to foster investment in SMEs by redirecting savings and investment to public markets. This demonstrates how tax incentives play a central role in determining the strength and attractiveness of SME dedicated markets.
Belgium	In Belgium, our experience is that more could be done in respect of tax incentives. For example, locally listed companies are not under the Belgian Shelter Tax Regime with the effect that the tax incentives in place today only promote non-listed start-ups, not larger SMEs nor scale-ups which could be eligible for public market financing. In addition, the MiFID framework restrains institutional and retail investments since intermediaries are no longer able to promote SME shares to investors (as a result of product governance and suitability requirements). Intermediaries no longer pro-actively propose SME shares or bonds as investment opportunities but only relay the obligatory information linked to shares or IPOs upon client demand and do not encourage further investments. The framework also concentrated liquidity around blue chip companies instead of SMEs. Finally, it is not our experience that a lack of investor confidence in listed SMEs is an inhibiting factor to institutional and retail investments or a result of market failure, but is rather linked to individual company performance.
Ireland	In Ireland, there is not a sufficient equity investment / capital markets culture, particularly among retail investors, to stimulate an active capital markets environment for SMEs. The lack of fiscal incentives for investing in smaller, riskier companies is also a contributing factor. More recently, legislative changes under MiFID II such as research unbundling are adding further to the challenges of creating a vibrant SME market.
Netherlands	In the Netherlands, all the factors outlined by the Commission apply to the local investor community: lack of visibility, liquidity and support by the local ecosystem, combined with a relatively higher risk profile of SME companies, make domestic and international institutional investors very wary to invest in Dutch SME companies. Moreover, the quality of companies, their visibility and liquidity are very much interconnected issues.
Portugal	Similarly in Portugal there is a feedback loop between institutional investors' involvement and liquidity. In recent years liquidity was considerably reduced as a result of disengagement by institutional investors linked to: (i) Portugal's 2011-2015 bailout; (ii) the 2011- 2017 downgrade of Portugal's credit rating below investment grade; and (iii) an unfavourable tax

	context. In respect of taxation, the domestic regime is seen by stakeholders as unpredictable. Moreover, it is compared unfavourably to other jurisdictions which have taken steps to introduce tax incentives to favour the growth of investments in SMEs on public capital markets. Tax incentives may be decisive on the increase of savings rates (hence investments) and would benefit IPOs' attractiveness in regards to other financing alternatives. Finally, the implementation of MIFID II, and its potential impact on SME research and coverage, may also negatively impact trading of SME shares.
Which participants of the ecosystems surrounding the Euronext markets for SMEs are declining the most?	
France	In France, brokers, market-makers, liquidity suppliers, financial research providers and investment boutiques specialised in SMEs are declining the most while the rest of the ecosystem remains strong. At the same time, larger institutions working on all asset classes have not filled the gap left by the shrinking SME dedicated sector. In order to weather the increasingly complex regulatory environment, SME specialists have been pushed to consolidate (e.g. Natixis-Oddo, Kepler-Cheuvreux). In parallel, we have seen a decline in diversity of participants: as noted in the earlier questions this can be seen in the rollback of the French operations of smaller German or UK brokers to focus on their own home markets. In practical terms, where previously an SME might have been followed by several analysts generating research coverage from several firms, it will now only be followed by one analyst or none at all.
Belgium	in Belgium the experience is very similar to that of Portugal. Moreover, Solvency II has been an additional factor in the Declining investor base in local market as insurance companies left the equity scene.
Ireland	In a smaller market such as Ireland, the impacts of legislation changes, such as research unbundling and the tick-size regime under MiFID II, dilute the incentives for brokers to support certain SMEs. In addition, our market has evolved in such a way that companies need to scale to a certain size before it becomes feasible for advisory firms to even take them on as potential IPO clients.
Netherlands	In the Netherlands, the main commercial banks do not undertake any advice or support for companies with a market cap below €250m (see previous answers). In certain cases where the prospective issuer is a longterm client, exceptions can be made to this rule; however they are usually accompanied by higher management fees or are on a "success fee" basis. While a few smaller local players have shown some appetite in the segment, there are no dedicated SME boutiques to support the local market. Furthermore, non-domestic banks mostly lack the distribution power for Dutch SME companies. Regarding investors, retail and semi-professional/semi-institutional (including private wealth, family office, etc.) investors have more potential than domestic/international institutional investors. However, new distribution channels need to be developed to attract these potential new buyers.
Portugal	In Portugal in recent years, the main local banks in Portugal have reduced their investment banking activities as a result of the banking industry restructuring which led to companies' bankruptcies, acquisitions by foreign players or significant cost-cutting. Moreover, banks reconsidered the cost and benefit of their SMEs' advisory services leading them away from opportunities in this segment as smaller SME IPOs are not seen as very profitable. Stand-alone broker activity – market making and similar – have always been small in Portugal and with a low impact on SMEs. Such activities are mainly conducted by banks, which have been reducing this type of activity as well. Other stakeholders – such as law firms, auditors and boutiques – have maintained their overall activity in recent years. Finally, local stakeholders believe that financial research coverage on SMEs is likely to reduce as a result of regulatory constraints following MiFID II. In turn, this may translate into a reduced investor base

	targeting SMEs as less coverage will be provided on these companies, thereby negatively impacting liquidity and making it harder to attract and list other SMEs on the local markets.
Main reasons behind the decline of ecosystems surrounding the Euronext markets for SMEs	
France	In France, while the impact of regulation is the most striking - in particular the MiFID framework – other factors are interlinked and cannot be easily distinguished in terms of causes or consequences on the local ecosystem. For instance, had brokers been able to focus more resources on SME segments and dedicate higher levels of commercial intensity to promote them, investor interest and appetite in the asset class would have certainly grown. However, low investor appetite, low liquidity, and in turn low profitability fuel a self-reinforcing downward trend where brokers are further less incentivized to focus on SMEs.
Belgium	In Belgium, low levels of liquidity on brokers' business models is due to local market models: as brokers earn less on trading, there are fewer incentives to promote liquidity in the segment. The market model and execution fees also render the activity of liquidity provision for SMEs non-profitable for intermediaries. The main reasons behind the decline of the local market ecosystem in the last 15 years is due to regulatory constraints on investment services providers (e.g. MiFID), not to a decline of appetite on either the part of issuers nor investors.
Ireland	In Ireland, a combination of the following factors has contributed to a reduction in the incentive for brokers to support smaller, less liquid stocks: (1) lower liquidity in smaller companies' shares; (2) reduction in the level of research being provided on smaller companies; and (3) increased in regulatory obligations and costs of business.
Netherlands	In the Netherlands, all of the reasons behind the decline of the ecosystems surrounding Euronext Amsterdam referred by the Commission are highly relevant, notably the impact of low level of liquidity on brokers' business models (including their appetite for SME instrument), the regulatory constraints on investment services providers and the lack of profitability of the SME segment.
Portugal	In Portugal, a lack of profitability explains in large part brokers reduced interest in supporting SME IPOs and listings, since SMEs have been generating less liquidity and business. In contrast, on bonds, this does not seem to be an issue: bond listings are usually traded less and mostly OTC.