15 October 2019
ESMA71-99-1235

Quality of Corporate Governance

Corporate Governance Conference – Zagreb

Steven Maijoor,
Chair
European Securities and Markets Authority

Dear Minister of Finance,

Ladies and Gentlemen,

It is a great pleasure for me to be here in Zagreb with you today for the signing of the new Corporate Governance Code later today by Ante Žigman from HANFA and Ivana Gažić from the Zagreb stock exchange. It is actually my second time in Croatia in just a few months which not only allowed me to discover your beautiful country and seaside but also the country's economic potential. I then also believe that a strong corporate governance code will further contribute to Croatia's development within the European capital markets.

Let me first say a few words about ESMA before going into the importance of corporate governance especially in light of EU's Capital Markets Union initiative. ESMA is the EU's financial market regulator. Together with the national authorities like HANFA we contribute to enhancing investor protection and promoting stable and orderly financial markets.

ESMA achieves this through four activities:

1. Assessing risks to investors, markets and financial stability not only through market analysis but increasing data collection at EU level and information sharing between the different national authorities. Understanding market developments and risk patterns is a valuable input for our work, especially to achieve our investor protection mandate. This has allowed us, among others, to warn investors for certain products, such as for example so

called contracts-for-differences (on which we have put strict restrictions by now with our product intervention powers and) which were also largely mis-sold to Croatian investors.

2. The development of a Single Rulebook, that is to say that we contribute to the development of the Internal Market by ensuring that we have common rules across the Union. That allows firms to operate in other Member States and SMEs to tap capital from other jurisdictions. Usually the key principles are set by the Commission, Council and Parliament in Brussels which we then complement by practical rules workable in day to day practice. At the start of ESMA in 2011 this was really our main priority to ensure the implementation of pieces of legislation like MIFID 2 and EMIR.

3. To promote supervisory convergence: having a common rule is one thing. Having it consistently applied in practice another. This is really becoming the most important priority for ESMA. As you may know, actually there has recently been a review of ESMA's founding regulation and the EU institutions confirmed that for investors and firms to benefit from and maintain their trust in the Single Market we need to make sure that our rules are applied in a similar way across the Union. That means that we do not only bring together the different regulators across the EU to ensure that they have similar practices, we also follow-up on the implementation of those rules for example through peer reviews of national supervisory practices.

4. Finally, ESMA is also a direct supervisors of certain pan-European market participants such as credit rating agencies and trade repositories. During the recent review to which I just referred to, the co-legislators also entrusted us with new direct supervision powers in relation to critical benchmarks (think about Euribor), data service providers and central counterparties (which is really important when the United Kingdom leaves the Union as important market infrastructures are currently located there).

In doing all of this, national authorities play an important role. Indeed, the Board I am chairing consists of the 28 heads of national authorities from across the Union. This has the big advantage that we can build on their knowledge and experience and that ESMA's work is supported across Europe. So if we publish something it means it has the support from the national regulators with whom you work more closely. In that respect I would like to use the opportunity to thank Ante for playing an active role in the Board of Supervisors.

Capital Markets Union

Let me now move to the Capital Markets Union – a Commission initiative which ESMA supports very much – a project on which the Union and the Member States in essence started working already more than fifty years ago by harmonising their legal and regulatory frameworks with the objective of supporting cross-border service provision in financial markets. It was European Commission President Jean-Claude Juncker who made the Capital Markets Union a priority in the economic agenda of the now outgoing European Commission, alongside the Banking Union.

It is widely known that capital in the EU remains primarily channelled through traditional banking. And, whilst we, of course, as regulators, must always remind households of the higher risks of investing in securities markets compared to saving via deposits, we must also act upon the fact that our economy is not suitably served by a primarily bank-based financial system. It is not through savings deposits that we achieve economic growth or financial prosperity. When they do not participate in the capital market, retail investors and households are missing returns that they badly need for future expenses related to education, housing and pensions. This issue is linked to trust in financial markets or the lack thereof. Retail investors do not always feel that they can invest their hard-earned savings in securities markets, and they even more rarely feel comfortable investing them in securities traded beyond their national borders. One reason for this is the fact that there are differing rules and market practices, so even those households that do invest in financial markets may not dare invest in securities traded elsewhere than on their national stock exchange.

There is a need to protect investors and to give them the reassurance needed to encourage them to trust financial markets and to become financial actors themselves. That way they will start investing in our start-ups, in our SMEs which need financing and hold the technologies and business of the future. the CMU, harmonized legislation, supervisory convergence, and strong and aligned principles of corporate governance across the European Union are crucial to achieving this.

Corporate governance

The role of corporate governance to attract retail investors to the financial markets can then also not be underestimated. Corporate governance is like democracy: it should not only be applied it should also be *seen* to be applied. If we want our markets, if we want retail investors – or by large: the citizens – to trust our financial markets we need to lead by example. People will only trust their money to someone if they trust the person taking care of it. It is impossible to develop a long-term financial centre without trustworthy operators.

I can then also only underline what Ante and Ivana wrote in the opening words of the corporate governance code which they will sign later today: Good corporate governance rests upon people. A strong code is then also helpful to understand what is expected, to align the interests of the different parties and to overcome the often-existing information asymmetry. But a code or a charter that is not lived up to, that is not implemented in practice remains a promise and empty words.

For supervisors respecting corporate governance arrangements is then also key. Does the entity have the right company culture with a focus on the right people doing the right things? This goes far beyond listed companies and whether management is working in the interest of the company and its shareholders. This is also relevant in the area of MIFID when we talk about selling products or more particularly in relation to checking whether directors are capable of taking decisions that ensure the sound and prudent management of their investment firm by being *fit and proper.* Also for ESMA as a direct supervisor strong governance with the high-quality people and clearly set processes is extremely important. For example, in the credit rating agencies business after what we learned through the financial crisis eliminating conflicts of interests remains crucial for ESMA. In that respect we have issues a fine of more than 5 million euro earlier this year against the Fitch group for breaching the conflict of interest provisions.

But corporate governance today is about much more than only respecting the long-term interest of the company and its shareholders. Business has an impact on wider society and the environment we are working in. Sustainable finance has then also become an important building block of the Capital Markets Union. This is an excellent example of how well-developed financial markets can help to achieve fundamental shifts to the benefit of everyone's life. I do not need to convince you that the negative impact of climate change is real, and that capital markets can play a key role to address this negative impact.

While we, regulators with a mandate regarding financial markets, are not able to address the main drivers of climate change directly, we do need to ensure that all risks of assets are taken into account and that financial markets respond to the (changing) preferences of investors. Supervisors will then also focus more and more on the relevant disclosure, transparency, conduct and governance frameworks to consider the sustainability risks of assets. This will allow an increasing number of investors assess the sustainability impact of assets when making an investment decision.

Ladies and gentlemen, let me conclude by indeed highlighting that only a long-term perspective and maintaining our efforts will help us in developing Europe's capital markets. And we will not be able to do so if we cannot convince retail investors to engage in financial markets to improve their financial position. And whether we can convince investors within Croatia, within the Union, and at global level to invest here or elsewhere will depend on our acts, on behaviour. I am sure that you will lead by example and that Croatia has everything to become a bigger financial market centre in the Balkan region and Europe. I am sure the new corporate governance code will contribute to that.

Thank you!