Swedish Securities Markets Association
Svensk Värdepappersmarknad

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Swedish Securities Markets Association response to ESMA Consultation on SME Growth Markets

Introduction

As apparent from the data presented by ESMA in the consultation paper Sweden has a comparatively vital and is the largest equity environment for SMEs in the Union. Swedish households have a long tradition of saving in equities as well as in mutual funds which in their turn invest in equities and bonds. The strong development of the Swedish SME-market stems from this investor demand. One out of five Swedes hold direct investments in equity. Eight out of ten Swedes save in funds and if you include the fund-based premium pension savings that figure is ten out of ten Swedes. Much of this is in equity or mixed funds.

An important reason behind the development of the Swedish savings pattern is that savings in securities have been subject to different kinds of tax subsidies. The subsidies have sometimes been related to the saved amount and sometimes to the return. Also, the Swedish pension system is based on market-based savings and in the public pension system part of the capital is reserved for risk capital investment. There are also specialized pension funds that focus on SME IPOs. A wide group of business angels and family offices are also part of this development. This strong tradition together with the low level of interest rates as well as the inexistent return on bank account savings have led to a search for yield behaviour that has to a large extent benefited investment in SMEs in recent years and thereby also created strong demand for new listings.

About the ecosystem, it has developed almost automatically as the conditions for the related markets have improved. It is not the result of rules or frameworks created by Swedish authorities. The tradition has rather been voluntary regulation and parts of the framework surrounding our growth markets result from work done by semi-legal bodies such as the Swedish Securities Dealers Association, the Swedish Securities Council, the Swedish Corporate Governance Board, and the Swedish Financial Reporting Board. It is also worth mentioning the work done by the Swedish regulated markets to improve the SME eco-system. Selfregulation combined with a strict and sensible legal framework adapted to growth companies provides both investor protection and the conditions necessary for the development of a healthy growth market surrounded by an efficient local ecosystem.

We would also like to underline that successful growth markets are local by nature not the least in the initial stages of the development. The ecosystem and the investors are to a very large extent local. Hence, it is our strong belief that cross border regulation should, as much as possible, be limited to outcome-based regulation where the areas to be regulated are decided at the EU level, but the actual rules are set in each jurisdiction or marketplace.

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Summary of questions

Q1: Do you have any views on why the SME activity in bonds is limited? If so, do you see any potential improvements in the regime which could create an incentive to develop those markets?

There are probably several reasons why SMEs do not use issuing of bonds as a source for funding. The bond market is dominated by Institutional Investors and for them issues from SMEs probably are too small and too illiquid. There is also a lack of infrastructure when it comes to less costly credit ratings, especially prompted by the EU regulation of Credit Research. Financial market participants are no longer allowed to have internal credit rating of issuers, or "shadow rating". The prospectus rules could also be a hindrance, though recently alleviated. All these problems make it difficult and costly for SMEs to use bonds for financing. The way forward is probably to make these bonds more attractive for retail investors and create a functioning and transparent market for bonds in smaller trade lots.

Q2: In your view, how could the visibility of SME GMs be further developed, e.g. to attract the issuers from other members states than the country of the trading venue?

Harmonisation of rules and regulation across Europe is needed. When that is in place common information material, which is easy to access on how to list on different exchanges could be centralised via ESMA. It goes without saying that investors also need to get information about what they are buying. Therefore, financial research and credit information are vital aspects for attracting investors. For that purpose, changes to the rules on credit research for SMEs could be considered. It could also be a marketing issue for the exchanges. Different currencies might also have an effect in this development since it is local. Issuers may want to list in a country which have the same base currency. More information made available by ESMA about the different SME growth markets could be beneficial–especially in terms of information about what growth markets are, how they work and where they are existing. But it could also be statistics regarding listings, issuance, market capitalisation, turnover etc. All with the purpose to make people aware of these markets.

Q3: In your view does the 50% threshold set in Article 33(3)(a) of MIFID II remain appropriate for the time being as a criterion for an MTF to qualify as an SME GM? Do you think that a medium-term increase of the threshold and the creation of a more specialised SME GMs regime would be appropriate?

SSMA believes that 50% threshold is appropriate right now. Especially with the uncertainty created by Covid-19. Since most SME GMs seems to be well above this threshold an increase could probably be evaluated in the medium term. It must however be analysed carefully before it is increased since GMs are a quite new creation and the percentage could change quickly depending on the development of the market. It could also be difficult to find a "one size fits all" solution since local markets are different depending on the size of the economy and therefore too high a threshold could be problematic. Therefor the threshold should remain a minimum and it should be possible for the respective MTFs to set the threshold higher if desired.

Q4: Do you consider that a further alignment of the definitions of an SME in different pieces of regulation with the MiFID II definition of SME would be helpful? Can you provide specifics of where alignment would be needed?

SSMA is of the opinion that harmonisation is good. It must however be done in a way so that changes to the definition do not lead to stricter rules in certain aspects. It is also important that local market

practices are taken into account and analysed before further harmonisations are introduced. Again, it could be difficult to find a "one size fits all" solution since local markets are different. We would therefore advocate an outcome-based regulation where the need for a SME-definition is defined and included in the different EU-based frameworks but the limits to be drawn to define an SME are set locally as they need to be adapted to local conditions and sizes of corporates.

Q5: Which are your views on the regime applicable to SME GMs regarding the initial and ongoing admission to trading of financial instruments? Are there requirements which should be specified?

Today these rules are to a large extent dictated by the issuing rules of the respective exchanges, which are developed from the existing rules and regulations. There are also different rules in different jurisdictions. Harmonised and potentially stricter criteria for listing must be developed taking the local differences into account. Free float is probably the most interesting criteria to analyse. A higher level of free float usually means higher liquidity in the share and better price discovery. This must however be put against the fact that small companies many times have concentrated ownership, which they might not want to lower too much.

Q6: Do you think it could be beneficial to harmonise accounting standards used by issuers listed on SME GMs with the aim of increasing cross-border investment?

SSMA is of the view that accounting standards already exists, at least locally. Non listed companies can use different methods and when they choose to become a listed company, they need to follow the accounting standards. If there are different standards in different jurisdictions it could be beneficial to harmonise minimum accounting requirements. It must however be done in a way so it does not increase the burden for the companies or harm existing local SME markets. We would like to underline that successful growth markets are local by nature not the least in the initial stages of the development. The ecosystem and the investors are to a very large extent local. Hence, it is our strong belief that cross border regulation should, as much as possible, be limited to outcome-based regulation where the areas to be regulated are decided at the EU level, but the actual rules are set in each jurisdiction or marketplace.

Q7: Should ESMA propose to create homogeneous admission requirements for issuers admitted to trading on SME GMs? Should such requirements be tailored depending on the size of the issuer (e.g. providing less burdensome requirements for Micro-SMEs)?

If harmonised admission requirements are developed for issuers, they need to be in a delegated act so there is no room for different interpretations in different countries. Again, successful growth markets are local by nature and both the ecosystem and the investors are to a very large extent local. Hence, it is our strong belief that cross border regulation should, as much as possible, be limited to outcome-based regulation where the areas to be regulated are decided at the EU level, but the actual rules are set in each jurisdiction or marketplace.

SSMA is not in favour of introducing micro-SMEs, see Q10.

Q8: Should ESMA suggest an amendment requiring an MTF registering as SME GM to make publicly available financial reports concerning the issuers admitted to trading on the SME GM up to one year before registration?

In most cases the information exists and is already made publicly available in the listing process. However, SSMA is of the opinion that there are cases where corporates do not have financial reports

for the year before a listing. Introducing a formal requirement could therefore lead to such corporates being unable to list and as a result in fewer listings.

Q9: Is there any other aspect of the SME GMs regime as envisaged under MiFID II that you think should be revisited? Would you consider it useful to make the periodic financial information under Article 33(3)(d) available in a more standardised format?

There are local standards on how periodic information should be published, which from a Swedish perspective works very well. Standards are often a good way to improve, but it must not make it worse for existing processes that are well established locally. One suggestion could be to select some relevant key performance indicators and collect and publish these numbers in a standardised format in order not to harm local markets that already function well. Inducements rules could be revisited, see Q14.

Q10: Do you think that in the medium term a two-tier SME regime with additional alleviations for micro-SMEs could incentivise such issuers to seek funding from capital markets? If so, which type of alleviations could be envisaged for micro-SMEs?

SSMA believes that it is an interesting idea, but we see many problems with a two-tier SME regime. It would be difficult in practice to make rules and regulations for micro-SMEs less strict than for other SMEs. It would create conflicts with several regulations and would also be difficult to handle from an investor protection perspective. The liquidity in these shares would also be very limited with an elevated risk of easily manipulated share price. A two-tier approach would probably also result in increased costs for different counterparts such as issuers, investment firms and exchanges.

Q11: Do you think that requiring SME GMs to have in place mandatory liquidity provision schemes, designed in the spirit of what is envisaged in Article 48(2) and (3) of MiFID II, could alleviate costs for SMEs issuers and provide them an incentive to go public? Do you think that on balance such provision would increase costs for MTFs in a way which encompasses potential benefits, resulting in reducing the incentive to register as an SME GM?

SSMA recognises the benefits for the market liquidity where liquidity provision schemes are in place. Today those provision schemes are governed through exchange rules in Sweden. If a company listing does not get the number of needed investors it can compensate for this by engaging a liquidity provider. SSDA believes this system works fine and can see problems with making it mandatory.

Q12: Do you think the requirement in Article 33(7) of MiFID II regarding the issuer non objection in case of instruments already admitted to trading on SME Growth Markets to be admitted to trading on another SME growth market should be extended to any trading venue? Should a specific time frame for non-objection be specified? If so which one?

The main problem for many listed SMEs is poor liquidity in shares. To divide that liquidity over several trading venues would probably increase this problem further. The reason why dual listings work for more liquid shares is that market makers and HFTs are often in place to ensures that prices are non-arbitrary between the different venues. Their trading strategies does not work that well for illiquid shares and they would therefore probably be less inclined to engage in dual listed SMEs. Since SSMA sees a problem with dual listings of SMEs, our view is that any extension of this possibility should be done carefully so that it does not hurt the existing local market structure.

Q13: Do you think that it should be specified that obligations relating to corporate governance or initial, ongoing or ad hoc disclosure should still hold in case of admission to trading in multiple jurisdiction?

It is important that trading on multiple venues and possibly in different jurisdictions does not make corporate governance, disclosures and information requirements more burdensome for the issuers or market participants. If shares are admitted to trading in other jurisdictions by non-objection it should not impose additional requirements on the primary market.

Q14: How do you think the availability of research on SMEs could be increased?

This has recently been consulted on by the EU Commission. In short SSMA favours solutions that are based on a commercial basis and through different sponsored arrangements. SSMA highlights two options for further analyses and those are bundling of SME research and improved issuer sponsored research. The current rules on credit research might also be revisited to promote information and research to investors. To improve availability maybe a central EU database could be investigated, which would make access to cross border research easier.

Q15: Do you agree with the proposed limits on resources or would you propose different ones? If so, please provide a justification.

SSMA want to point out that Sweden does not have the system with liquidity accounts and therefore has no strong views on amendments to that system. Sweden on the other hand has a system with liquidity providers who trade on their own account under Nasdaq member rules and issuers pays the liquidity provider for this service. SSMA is of the opinion that this system works well and does not want to adopt a new structure for providing liquidity, which would add complexity to the existing market structure.

Q16: Do you agree with the proposed limits on volumes or would you propose different ones? If so, please provide a justification of the alternative proposed parameters.

See Q15 – no strong view

Q17: Do you think that specific conditions should be added as regards trading during periodic auctions? For SME GMs following different trading protocols, are there criteria or safeguards which should be considered in order to make sure that the liquidity contract does not result in a manipulative impact on the shares' price?

SSMA believes that activities in periodic auctions already has the necessary rules and monitoring systems in place to identify and prevent market abuse. SSDA sees no need at this point for introduction of further safeguards for the Swedish market.

Q18: Do you agree with ESMA's view that the liquidity contract may cover large orders only in limited circumstances as described in paragraph 118?

See Q15, but SSMA understands the problem of large orders in a liquidity contract set up. In that system large orders should probably have separate rules. In the Swedish structure for liquidity providers this is not a problem since large orders would end up on the own account and the risk will only be market risk for the liquidity provider not the issuer. It will therefore be a risk/reward decision whether to take on larger trades or not.

Q19: Do you agree with the proposal described above regarding the template for the insider list to be submitted by issuers on SME GMs? If not, please elaborate.

SSMA agrees that today too much unnecessary information is included in the insider list and the requirement of information have resulted in a heavy administrative burden and costs for issuers and others. In our opinion only adequate, relevant data should be included, and information should not be excessive in relations to the purpose of the insider list. SSMA believes this simplified template is an improvement. The proposed changes and simplifications of the SME insider lists would also be welcomed on a broader scale for all issuers, since there is an abundance of information. For countries where the national ID number leads to all necessary information, which is the case for Sweden, certain information is not necessary but would be easily accessible upon request by a competent authority from e.g. the tax office and authorities.

CBA Q1: Can you identify any other costs and benefits? Please elaborate.

SSMA has no view on costs or benefits for the system with liquidity contracts since Sweden do not have that system – see Q15.

For the simplified insider list the SSMAs overall view is that it is important to make sure that the proposed changes do not result in increased costs as this could have an opposite effect than the one intended, leading to less SME listings and investments. ESMA should also consider that currently there are many on-going regulatory implementations carried through that demand a lot of resources, both human and financial. It is therefore very important to stress that any regulatory changes do not lead to new IT-intensive implementation projects. Any changes must not force new IT infrastructure. If the simplification can be implemented with limited investments it would be a of benefit for the market, especially if the requirements will be the same for all different insider lists. That would take away unnecessary mistakes and minimize errors.

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