Corporate financing in Austria in the run-up to capital markets union

Helmut Elsinger,
Robert Köck,
Marcel Kropp,
Walter Waschiczek[1]

In this study, we examine the financing of Austrian companies through the lens of the measures proposed in the European Commission's action plan on building a capital markets union. The Austrian corporate sector has not been faced with major financing problems in recent years. Nevertheless, there is clearly room for improvement in the area of equity financing, in particular with regard to funding start-ups and innovations. It is safe to assume, however, that banks will continue to play a key role in corporate funding in Austria. This is especially true for smaller and medium-sized companies, whose borrowing needs are low in absolute terms, tend to be highly volatile over time or require tailor-made collateralization. Here, banks will continue to have a comparative advantage over standardized funding options available on the capital market. Still, a diversification of funding options proposed by the capital markets union project would enable the Austrian corporate sector to tap into complementary financing sources. The measures envisaged in the action plan to minimize the information gap between potential investors and companies in need of financing may help reduce the cost of funding and, more importantly, enable the completion of transactions in the first place. This way, capital markets will play a more active role in spreading the risks and opportunities inherent in investment projects among a wider circle of investors.

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Since the outbreak of the financial crisis, bank lending to the corporate sector has clearly flattened both in Europe as a whole and in Austria. At the same time, corporate financial investment and public infrastructure investment have slowed down as well. The European Commission responded to this development by proposing to build a capital markets union with a view to complementing bank financing with stronger capital markets and thus mobilizing capital and channeling more capital from savers to companies.

The capital markets union project is not a closed system; instead, it comprises most diverse aspects and measures, which the European Commission (2015c) encapsulated in an action plan. More integrated capital markets are expected to improve the long-term funding of Europe's corporate sector. The idea is to enable companies to choose from a more diverse range of funding options and to gradually bring down barriers to cross-border investment. Some of the proposals go beyond Europe-wide harmonization and include farther-reaching positions, such as same tax treatment of debt and equity capital or restructuring insolvency procedures to give entrepreneurs a "second chance."

The cornerstone of the capital markets union project – developing an EU-wide capital market by bringing down

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Thomas Saghi,
Federal Ministry for
Science, Research
and Economy

[1] *Oesterreichische Nationalbank, Economic Studies Division, helmut.elsinger@oenb.at; European Affairs and International Financial Organizations Division, robert.koeck@oenb.at; Economic Analysis Division, walter.waschiczek@oenb.at; European Central Bank, Monetary and Financial Statistics Division, marcel.kropp@ecb.europe.eu. At the time of writing, Marcel Kropp was employed by the OeNB. Opinions expressed by the authors of this study do not necessarily reflect the official viewpoint of the OeNB or of the Eurosystem. The authors would like to thank Ernest Gnan, Vanessa Redak, Doris Ritzberger-Grünwald, Stefan Schmitz, Martin Schürz, Katharina Steiner and Martin Summer for valuable comments and Philipp Reisinger (all OeNB) for the provision of data.*

national barriers – is not a new idea. As a matter of fact, the free flow of capital was one of the fundamental principles on which the EU was built, and this idea has fed into many EU initiatives and projects. These undertakings ranged from the 1988 deregulation of capital movements in the EU (European Commission, 1989) to the 1999 Financial Services Action Plan, to the proposals set forth by the Giovannini Group (from 2001) for removing obstacles to the cross-border clearing and settlement of securities transactions. Also, creating more efficient capital markets was named as an explicit goal of monetary union. Capital markets union is a further step toward the completion of a single European capital market.

In addition to the banking union project, the European Commission will assign top priority to the capital markets union project in the years to come. While both are being called "unions," capital markets union differs substantially from banking union. In contrast to banking union, which harmonizes supervision and resolution and restricts the scope of banks' activities further (through enhanced capital and liquidity requirements and refinancing rules), the capital markets union project encompasses a program for actively developing and strengthening capital markets. Furthermore, capital markets union does not entail a consolidation of the supervision of the respective instruments and institutions at the EU level, whereas banking union rests on a centralized supervisory framework. The measures outlined in the action plan on building a capital markets union are rather diverse and, hence, not as closely intertwined as the building blocs of banking union. Also, capital markets union is – in contrast to banking union – an EU-wide project.

This study provides an analysis of the Austrian corporate sector specifically with regard to the domestic take-up of the instruments[2] listed in the action plan. It also examines in what way the measures proposed in this plan might help Austrian companies catch up where they may be lagging behind. After highlighting the main characteristics of these financing instruments, we will, depending on data availability, compare the relative importance of these instruments for corporate finance in Austria with peer countries in Europe. This study focuses on economic aspects and does not touch on any legal issues.

In this study, Austria is compared with countries that display similar economic structures. As the countries whose economic structures and financial systems are most similar to those of Austria are the other "western European" countries, the countries in transition in Central, Eastern and Southeastern Europe (CESEE) are not part of the peer group. While CESEE is of crucial importance for the Austrian economy, the region's economic structure – and especially financial market structures – still differ substantially from western European countries in general and Austria in particular. This is why a comparison vis-à-vis the CESEE region did not seem opportune in this case. Nor did we account for those smaller EU Member States in which the financial sector makes a disproportion-

[2] *For this reason, important types of corporate financing, such as trade credits, factoring or leasing are not covered. For more information on the financing of small and medium-sized enterprises (SMEs), see, for instance, Nassr and Wehinger (2014) and OECD (2014 and 2015).*

ately high contribution to GDP. This left us with the larger western EU Member States to include in our sample.

This paper is organized as follows: It starts with a brief overview of the corporate structure in Austria and analyzes whether there are any pointers to specific requirements with regard to the measures proposed in the action plan on building a capital markets union. Sections 2 and 3 examine the effects capital markets union is likely to have on individual debt and equity financing instruments that are defined in the action plan as the main funding sources and which are meant to complement corporate finance in the medium and long term. Section 4 presents the main conclusions.

Box 1

Key aspects of the capital markets union initiative

The European Commission has bundled its activities aimed at unlocking long-term finance under the ***capital markets union*** *initiative, which is aimed above all at reinforcing measures in two areas: mobilizing funding for* ***infrastructure projects*** *and funding for small and* ***medium-sized enterprises*** *(SMEs).*

In implementing its strategy, the Commission is taking the following action:

- *Prospectus requirements: The Prospectus Directive is to be modernized with a view to reducing the fixed costs associated with the issuance of bonds.*
- *Assessment of creditworthiness: Standardized quantitative methods are to be developed that enable nonexperts and nonbank lenders, such as insurers and asset managers, to assess the creditworthiness of SMEs to facilitate loans to SMEs.*
- *Review of securitizations: The European Commission is drafting regulatory requirements and quality criteria to allow for a simple and transparent classification of securitizations for nonexperts.*
- *Promotion of the development of European long-term investment funds: This initiative aims to encourage insurance companies and pension funds to make longer-term investments in private infrastructure projects and undertakings.*
- *Development of a European market for private placements: Such placements take place outside of a stock exchange, i.e. a public trading venue. In other words, securities are directly placed with a small group of investors (individuals or institutions). The European Commission is currently harmonizing the legal framework to align national insolvency and disclosure laws.*

1 State of play of the Austrian corporate sector

This section examines how the measures envisaged by capital markets union may affect the Austrian corporate sector in a positive or negative manner. First, as to the structure of the corporate sector: Do key indicators on company demographics point to strengths and weaknesses that might entail specific effects from capital markets union? Second, given that capital markets union is meant to improve corporates' funding situation, how do Austrian companies rate financing problems? Third, we compare Austrian companies' financing structure with international peers, in particular with regard to the two aspects tackled by capital markets union: equity levels and the role of bank loans in corporate finance.

1.1 Company demographics in Austria

In Austria, the share of SMEs[3] in the number of employees (68%) and value added (60.4%) broadly corresponds to the figures recorded by other smaller western European countries (see table 1). A more granular SME breakdown by size shows that, above all, very small companies (with up to 9 employees) contribute relatively little to employment and value added, while medium-sized companies (with 20 to 49 and 50 to 249 employees) make above-average contributions compared with the EU-14 peer group examined here. Given that alternatives to bank funding tend to be a more viable option for larger companies, one might assume that Austrian businesses could derive disproportionately high benefits from capital markets union.

The relatively minor share of very small companies could result from the low start-up ratio. At 5.9 start-ups per 1,000 existing businesses, the number of business births in Austria trails behind the "birth rate" of most other countries examined in this study. The small share of private equity might indicate that the low start-up ratio is attributable to financing deficits, even if a more thorough analysis of the private equity volume shows a mixed picture (see section 3.1). Should financing bottlenecks put a brake on business start-ups in Austria, then the fact that large countries record higher start-up ratios could imply that capital markets union would have a positive impact on Austria's number of business births.

Another aspect that might explain the comparatively little share of very small businesses is the substantial portion of foreign-controlled companies in Austria. In 2012, one-third of Austria's value added was delivered by foreign-controlled companies, which accounted for one-fifth of overall employment. Both relative to the number of employees and to value added, this share exceeds the average of the peer group of countries examined in table 1.[4] Not surprisingly, foreign-controlled companies play a more important role in smaller countries than in larger countries. With regard to capital markets union, this could, on the one hand, imply rather minor direct effects in Austria, because in foreign-owned businesses, strategic financing decisions tend to be taken abroad. Yet, on the other hand, integrating individual national capital markets toward a single European financial market could promote cross-border investments in businesses.

And finally, table 1 shows that the legal form of corporation is notably less widespread in Austria than in many other countries. Only one in five Austrian companies adopted the legal form of limited liability company or stock corporation, while this is, on balance, the case with one in three companies in the country peer group used in this study. In countries with more market-based financial systems, over two-

[3] *The definition generally used for SMEs in Europe comes from the EU, which has laid down three size-related criteria for classifying companies. Hence, SMEs are businesses with fewer than 250 employees and whose sales do not exceed EUR 50 million per year or whose balance sheet amounts to no more than EUR 43 million. The international Eurostat and OECD tables on which table 1 is based use employee figures for breaking down the results.*

[4] *In part, the differences in the shares in the number of employees and value added posted by foreign-controlled companies might relate to the fact that some countries offer considerable profit-based tax incentives. Hence, the profit and value added of many multinational corporations are recorded in those countries.*

Table 1

Company demographics

2012 or last year available, %

	Share of SMEs in		Business births per	Share of foreign-controlled companies in		Share of corporations in
	number of employees	*value added*	*1,000 companies*	*number of employees*	*value added*	*number of companies*
AT	68.0	60.4	5.9	19.3	25.0	20.6
DE	62.5	54.0	7.9	11.6	24.0	17.9
UK	53.0	50.9	11.5	19.5	30.1	68.7
FR	63.5	58.0	10.4	10.5	15.8	39.0
IT	79.9	67.3	7.1	7.5	14.1	17.9
ES	73.8	62.9	8.2	11.5	19.8	38.0
NL	66.9	63.8	7.3	16.0	26.8	20.4
SE	65.5	59.1	7.7	21.8	27.8	42.6
BE	70.4	62.4	5.1	17.1	28.0	59.9
DK	64.9	60.5	. .	20.3	23.9	. .
FI	62.5	57.9	9.3	15.5	20.7	41.5
IE	72.4	51.8	. .	23.3	57.1	. .
GR	87.3	75.7	. .	5.0	10.9	. .
PT	78.9	66.1	11.8	11.2	20.2	32.9
EU-14	65.5	58.3	8.4	14.1	23.2	36.1
AT/EU-14, %	104	104	70	136	108	57

Source: OECD, Eurostat, authors' calculations.

thirds (United Kingdom) or some 60% (Belgium) of companies opted for these legal forms. The legal form of corporation makes a difference when it comes to issuing equity securities, because access to organized capital markets is usually limited to corporations. Even in cases where companies do not necessarily have to be incorporated, agency problems and reduced fungibility of shares present obstacles that are more pronounced than with corporations, especially in the case of third-party investments in partnerships.

Overall, company demographics suggest that Austria might, indeed, benefit from the measures introduced by capital markets union, provided the weakness in investment of recent years reflects restrictions on the funding side.

1.2 Sizing up companies' funding problems

Apart from the structure of the corporate environment, the extent to which the measures envisaged in the action plan may boost the funding volume (and hence investment activity) of Austria's corporate sector also depends on whether if and to what extent funding issues dampen entrepreneurship in Austria.

To answer this question, we draw on the responses to the Survey on the Access to Finance of Enterprises (SAFE) that is carried out in a harmonized manner throughout the EU.[5] This survey comprises questions on funding options as well as on business performance and development. Respondents are asked, among other things, to rate various problems they are faced with

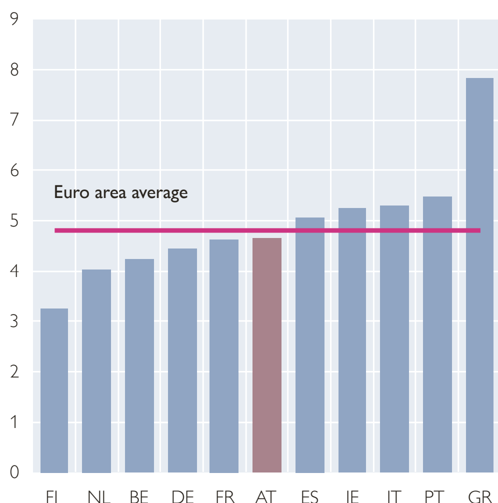
[5] *SAFE is a joint project of the European Commission and the European Central Bank, which targets mainly small and medium-sized enterprises; yet, the survey also includes several large companies. However, in light of the small number of surveyed large companies, only SME results are published for Austria.*

Chart 1

Assessment of SME financing

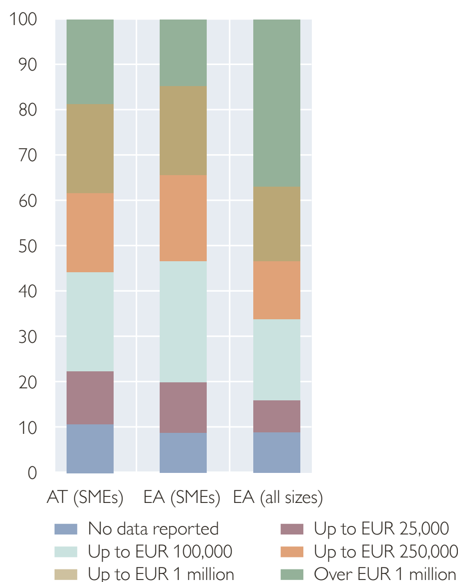
Access to finance for SMEs

1 (easy) to 10 (difficult), self-assessment of the surveyed companies, Q2–Q3 2015



Financing needs by amount

Share in responses in %, Q2–Q3 2014



Source: ECB (Survey on the Access to Finance of Enterprises – SAFE).

as entrepreneurs on a scale from 1 to 10. With the exception of the first SAFE survey in 2009 carried out at the height of the crisis, the factor "access to finance" has always been rated as the least pressing problem, with the score invariably remaining below the euro area average (see chart 1, left panel). Given that, according to this survey, access to finance is considered to be a relatively small impediment by SMEs in Austria – and lately also in the euro area in general –, this would imply that capital markets union measures will entail below-average benefits for Austrian businesses. The authors of a recent OeNB study examining the causes of declining investment activity in Austria (Fenz et al., 2015) arrived at a similar conclusion, arguing that funding restrictions did not seem to have dampened moderate investment activity.

The survey is also indicative of the amount of funding needed by companies. At greater intervals (most recently in 2014), companies are asked to quantify their funding needs for expanding their business. Close to two-thirds of the Austrian SMEs surveyed (no figures are published for the Austrian corporate sector as a whole, as mentioned above) stated that they needed less than EUR 250,000 to this end, while almost 20% had funding needs exceeding EUR 1 million (slightly more than in the euro area as a whole). When we include large companies, more than one-third of the respondents in the euro area indicated funding needs of more than EUR 1 million (see chart 1, right panel). As to the financing needs of SMEs, they tend to be smaller than the amounts necessary to gain access to financing instruments in the action plan that are geared toward institutional investors.

1.3 Financing structure of Austrian companies

To assess the relevance of capital markets union for funding behavior in Austria's corporate sector, we must also take a look at the structure of corporate finance, apart from the corporate environment and businesses' financing needs. By international standards, equity funding plays a relatively minor role for Austrian companies.[6] At 44.9% of total liabilities at end-2014, the share of equity in Austria stood at the lower end of the range compared with the country peer group under survey here (see table 2).[7] This relatively low equity ratio contrasts with a disproportionately high share of bank loans, even though the latter have become less important in past years (Beer and Waschiczek, 2012).[8] Yet, although the share of bank funding nearly halved from almost 40% in the mid-1990s to slightly more than 20% recently, it was

Table 2

Company funding structure in Austria and in selected European countries

Outstanding volume, 2014 (or last year available), %

	Equity	Bank loans		Bonds		Other debt[1]	
	% of total assets	*% of total assets*	*% of debt capital*	*% of total assets*	*% of debt capital*	*% of total assets*	*% of debt capital*
AT	44.9	20.4	37.0	6.4	11.6	28.3	51.4
DE	46.6	14.4	27.0	2.8	5.2	36.2	67.8
UK	51.7	8.2	17.1	8.6	17.7	31.5	65.2
FR	58.4	9.9	23.9	6.9	16.6	24.7	59.5
IT	43.9	23.3	41.5	4.5	8.0	28.3	50.5
ES	52.3	16.2	33.9	0.7	1.4	30.9	64.8
NL	47.1	18.3	34.7	5.1	9.6	29.4	55.7
SE	69.7	8.9	29.5	3.7	12.1	17.7	58.4
BE	54.5	5.5	12.1	2.5	5.5	37.4	82.3
DK	65.0	14.6	41.8	2.6	7.5	17.8	50.7
FI	51.4	12.1	24.8	5.8	12.0	30.7	63.1
IE	54.4	5.4	11.9	1.2	2.6	38.9	85.4
GR	41.0	42.1	71.2	0.0	0.0	17.0	28.7
PT	38.3	15.6	25.3	6.3	10.2	39.8	64.4
EU-14	51.9	12.5	26.0	5.4	11.2	30.2	62.7
AT/EU-14, %	86	163	142	118	103	94	82

Source: OeNB, ECB, Eurostat, authors' calculations.

[1] *Loans from nonbanks, trade credit, pension fund reserves, other liabilities.*

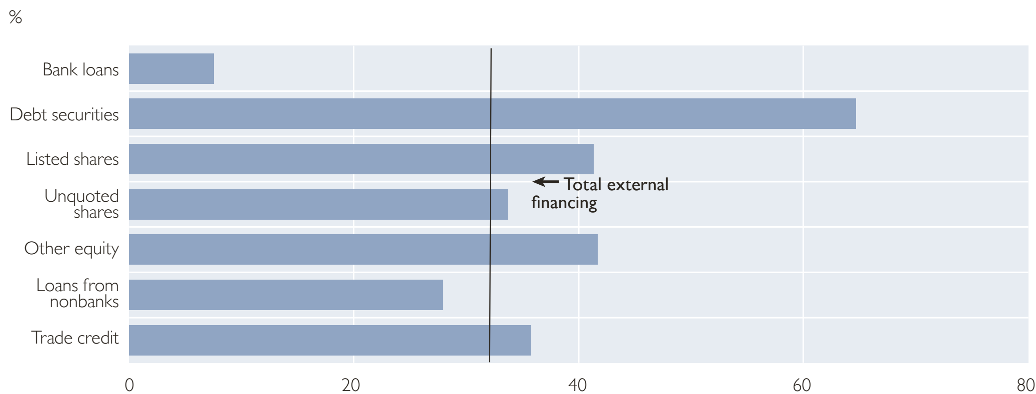
[6] *On the issue of Austrian companies' capitalization, see also ECB (2002), Dirschmid and Waschiczek (2005) and Raidl (2013).*

[7] *Table 2 refers to financial accounts data, which contain a financial balance sheet of the corporate sector (and of the other economic sectors). These data, which are part of the national accounts, are comparable with other economic measures and become available for all EU countries after a relatively short time lag. At the same time, the financial accounts data do not allow for a breakdown by economic sector or size. Such information may be gleaned from the BACH database, which is based on corporate balance sheets. Yet due to considerable methodological and conceptual differences, the BACH data diverge markedly in absolute terms from the national financial accounts data. Moreover, BACH data are not available for all EU countries and are released with a larger time lag since they are based on audited balance sheets. For an analysis of Austrian companies' equity ratios based on BACH data, see e.g. Dirschmid and Waschiczek (2005).*

[8] *In addition to extending loans to companies, banks hold corporate bonds and stocks. At end-2014, the entire volume of fixed-income securities and stocks (both listed and unlisted) ran to EUR 7.8 billion or 1.1% of companies' total liabilities.*

Chart 2

Foreign share in external financing in the corporate sector



Source: OeNB.

still the third largest in the group of countries under review.[9]

One key objective of capital markets union is to expand cross-border financing options for the corporate sector – both within and beyond the EU. Because international databases do not contain comparable data on the share of cross-border funding of the corporate sector in other countries, we only portray the situation in Austria. The cross-border share is lowest for bank loans, while almost two-thirds of Austrian corporate bonds are placed abroad, which may be ascribable to the relatively small domestic bond market. The sizable foreign share in equity instruments and in other loans reflects the relatively high share of inward direct investment in the Austrian corporate sector.

2 Debt instruments

This section discusses the funding options that the European Commission's action plan addressed as debt funding alternatives to bank loans, taking the different degrees of disintermediation as a starting point: In the case of loan securitization, credit intermediation occurs in the banking system; it is only after the process of intermediation has been completed that the loans are transferred from the bank balance sheet to another intermediary (which may be yet another bank). In the case of loans extended by institutional investors, borrowers and lenders are still matched by intermediaries, but intermediaries other than banks. In the case of funds that companies raise directly in capital markets by issuing bonds, banks (above all banks operating in universal banking systems) may often act as a go-between in the issuance process. Yet, the funds as such are raised from the markets, on which banks may likewise invest in corporate bonds.

2.1 Securitization of corporate loans

Securitization serves to provide long-term funding for the real economy, such as SMEs, from institutional and private investors.

[9] *For a detailed analysis of the development of financing structures in the corporate sector over the past 20 years based on financial accounts data, see Andreasch et al. (2015).*

Table 3

Outstanding SME securitization

As at 2014

	EUR million	% of company liabilities	% of debt capital	% of bank loans	Annual change from 2010 to 2014, %
AT	0	0	0	0	
DE	1,889	0.03	0.06	0.24	–37.3
UK	8,724	0.14	0.30	1.74	24.6
FR	1,016	0.01	0.03	0.12	–14.1
IT	23,946	0.69	1.23	2.96	51.6
ES	29,934	0.89	1.86	5.50	–23.1
NL	9,563	0.51	0.97	2.81	–10.8
SE	0	0	0	0	
BE	18,479	1.07	2.35	19.33	6.1
DK	0	0	0	0	
FI	0	0	0	0	
IE	0	0	0	0	
GR	6,731	2.97	5.04	7.07	–14.7
PT	5,588	1.02	1.65	6.50	–3.7
EU-14	106,819	0.32	0.67	2.42	–10.1

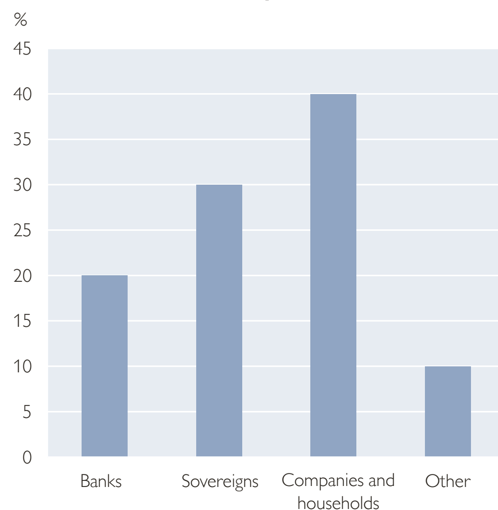
Source: Association for Financial Markets in Europe (AFME), ECB, Eurostat.

Europe is characterized by a heterogeneous securitization market (see table 3). The peripheral EU countries Italy, Spain, Greece and Portugal account for the highest stocks of securitized loans to SMEs. While in Italy the stock of outstanding SME securitization jumped by somewhat more than

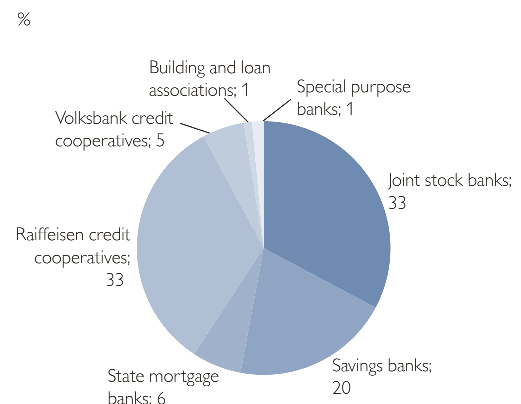
Chart 3

Austrian banks' claims

Austrian banks' claims by debtor



Austrian banking groups' claims on nonbanks



Source: OeNB.

Note: Based on June 2015 data.

50% in the period from 2010 to 2014, in other peripheral countries major securitization projects had already been implemented before 2010. Among the core countries, Belgium stands out with a relatively large securitization market: In Belgium, almost 20% of all bank loans to SMEs have been securitized.

The European securitization market cannot be compared with the U.S. subprime market. While the default rate for U.S. papers has been close to 20% since 2007, it has been markedly below ½% for European papers according to data compiled by the Association of German Banks (Bundesverband deutscher Banken, 2014).

By European standards, the volume of securitized products issued by Austrian intermediaries was rather small before the onset of the crisis and has remained rather small ever since. Yet the potential for larger-scale securitization exists (see chart 3, left panel): by the end of June 2015, companies (including SMEs) and households accounted for some 40% of the aggregate claims of Austrian banks (EUR 651 billion).

Joint stock banks and Raiffeisen credit cooperatives had a share of about one-third each in the claims of Austrian banking groups on nonbanks (see chart 3, right panel). The loan receivables of those two groups are characterized by a high share of individual loans with comparatively small amounts on average. The loan receivables of savings banks (share of around 20% in Austrian banking groups' claims on nonbanks), state mortgage banks (share of 6%) and Volksbank credit cooperatives (5%) are high enough in absolute terms to generate additional momentum for the Austrian securitization market.

2.2 Corporate finance provided by institutional investors: loan-originating funds

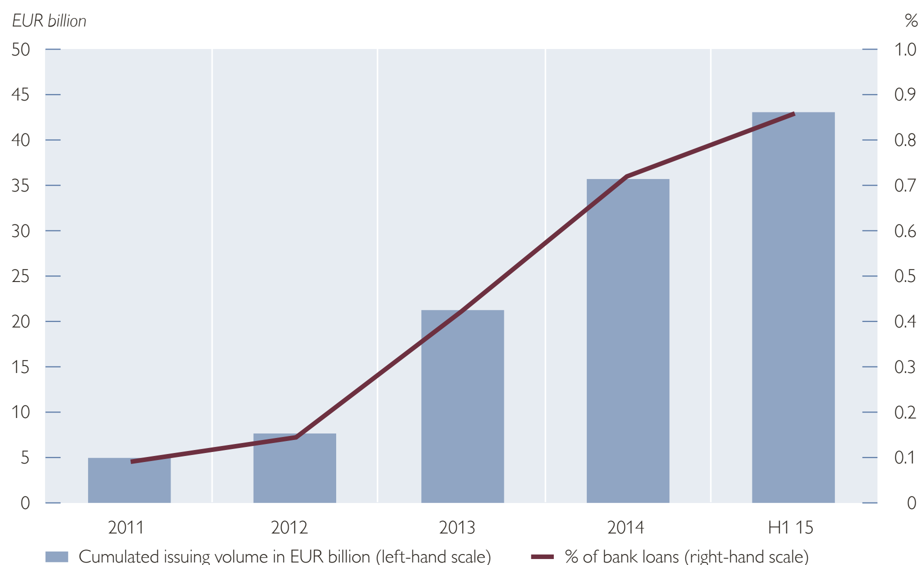
As an alternative to and in addition to securitization, where credit intermediation occurs in the banking system, the European Commission's action plan also envisages an enhanced role of funds for the provision of credit, i.e. loan-originating funds. European funds specializing in corporate lending already reported very high growth rates in recent years, as is evident from data compiled by Creditreform (2015), notwithstanding the rather small volumes in relation to loans originated by banks (see chart 4).[10] Among other things, the high growth rates may reflect the current low level of interest rates, which has increased the incentive for institutional investors to expand into higher-yield, higher-risk assets. Furthermore, uncertainty about the regulatory framework for securitization may have contributed to the heightened relevance of loan-originating funds. The volumes indicated in chart 4 may include direct lending by funds – often through participation in syndicated loans – as well as the acquisition of loans originally extended by banks. To the extent that loans are bought by funds, the patterns and the issues are very much the same as those with securitization (see also Kraemer-Eis et al., 2014). In the event of direct lending, the funds perform the whole range of intermediation services otherwise provided by banks.

Analyses of data for the U.S.A., where loan-originating funds emerged earlier and have been used more widely, show that, at least before the onset of the crisis, institutional investors were providing higher-risk loans than banks,

[10] *Creditreform (2015) provides only data for Europe as a whole (without an exact definition); there is no country-by-country breakdown. Kraemer-Eis et al. (2014) report a strong expansion of such funds above all in the countries hardest hit by the crisis.*

Chart 4

Direct lending funds in Europe



Source: Creditreform Rating, ECB.

such as leveraged financing, in the context of mergers and acquisitions (Nandy and Shao, 2007; Nini, 2013; Ivashina and Sun, 2011). Furthermore, these studies indicate that the stepped-up involvement of institutional investors also increased the overall supply of credit for the corporate sector – primarily in the form of securitized loans but also in the form of direct lending.[11] At the same time, the data highlight that loan-originating funds above all replaced bonds, whereas they are no substitute for revolving credit lines as provided by banks (Nini, 2013). With regard to the improved availability of corporate information targeted by capital markets union, the findings of Sufi (2009) may be of relevance, namely the fact that institutional investors began to embrace syndicated loans in the mid-1990s when Moody's and Standard & Poor's started to publish ratings of bank loans.[12] In the context of capital markets union, this would imply that a higher degree of harmonization and standardization of borrower information would facilitate the risk monitoring for institutional investors, such as loan-originating funds. Notwithstanding easier access to information and a more straightforward assessment given data harmonization, another issue remains, namely the pronounced economies of scale involved in monitoring and risk analysis. Building adequate capacities may pay off only if funds intend to diversify into new markets permanently and on a large scale. It remains to be seen whether and to what extent this is true for loans to Austrian companies.

[11] *It should be noted, though, that this evidence primarily relates to wholesale funding, and to syndicated loans in particular, and that it is based on a much broader definition of institutional investors.*

[12] *However, the enhanced availability of information came at a price. Nandy and Shao (2007) show that (before the onset of the crisis) syndicated loans granted by institutional investors generated a higher yield than comparable bank loans. They interpret the higher yield as compensation for the higher efforts needed to gather information.*

Table 4

Bonds issued by nonfinancial companies

Outstanding volume, 2014 (or last year available), %

	% of company liabilities	% of other debt	% of bank loans	Annual change from 2010 to 2014
AT	6.4	11.6	31.2	8.9
DE	2.8	5.2	19.2	2.8
UK	8.6	17.7	103.6	7.8
FR	6.9	16.6	69.6	10.8
IT	4.5	8.0	19.3	12.1
ES	0.7	1.4	4.0	13.3
NL	5.1	9.6	27.7	1.1
SE	3.7	12.1	40.9	9.9
BE	2.5	5.5	45.7	17.4
DK	2.6	7.5	17.9	–0.5
FI	5.8	12.0	48.4	4.7
IE	1.2	2.6	22.0	–2.8
GR	0.0	0.0	0.1	–56.8
PT	6.3	10.2	40.5	0.5
EU-14	5.4	11.2	43.2	2.9
AT/EU-14, %	118	103	72	

Source: ECB, Eurostat, authors' calculations.

2.3 Corporate bonds

Two of the measures presented in the action plan specifically address steps to facilitate corporate bond financing: On the one hand, there is a proposal to modernize the Prospectus Directive with a view to reducing the prospectus requirements for the placement of bonds, by streamlining the prospectus disclosure and update requirements as well as the approval process. On the other hand, the European Commission intends to review possibilities for improving the liquidity of corporate bond markets and the voluntary standardization of offer documentation.

In recent years, the volume of corporate bond financing has already increased markedly in most European countries, including Austria. In 2014, capital raised through bond issuance accounted for more than 6% of Austrian' companies total external finance, which by European standards, was an above-average result (see table 4). The issuance volume proved also high in relation to the volume of debt capital, whereas it was below average compared with the stock of bank loans, given the high relevance of loan-based financing. In this respect, it should be noted that agencies account for a comparatively high share of bond issuance in Austria, even following the transition of data compilation to the ESA 2010.

Raising capital through the issuance of bonds, above all in organized bond markets, differs from taking out a bank loan in a number of areas (see also Waschiczek, 2004). While the cost of taking out a bank loan increases in proportion to the loan volume, the cost of issuing bonds decreases progressively in line with the issuance volume. Such economies of scale reflect the fact that the issuance of bonds comes with a series of one-off costs, which are mostly unrelated to the credit volume.[13] When

[13] *These costs include the syndication commission for syndicate banks, which underwrite the issuance and guarantee the placement of bonds; marketing costs, such as the cost of producing the issuance prospectus and conducting roadshows to inform institutional investors; and the cost of the stock market listing, consisting of the commission for initial public offering and the stock exchange listing fee.*

we compare the minimum volume required for cost reasons with the corporate funding needs reported by companies under the SAFE survey (see section 1.2), we see that bond issuance will seldom be an option for smaller companies. SMEs which nonetheless fund themselves through bonds will have to establish liquidity management tools. While there is more to bonds than standard coupon bonds, tailor-made solutions are costly and tend to be illiquid (Demary et al., 2015).

A number of other factors may also put a limit to the share of loans that may be replaced by bonds. Bank loans are better suited to overcome the information gaps that exist between lenders and borrowers. Long-standing relationships give banks enhanced insights into the finances of their corporate customers, thus enabling them to arrive at a more informed assessment of their debtor's credit quality. The implicit relations that emerge over time between banks and their borrowers also facilitate negotiating services that cannot be agreed upon up front. However, such a close relationship between banks and their borrowers need not necessarily be an advantage. Haselmann et al. (2014) show that close personal ties between bank managers and corporate executives may also lead to lending inefficiencies. Improving and standardizing the public availability of SME-related credit data, which is one of the goals of capital markets union, may facilitate bond investment, but such measures address neither the higher flexibility of bank loans nor the smaller amounts in which loans may be taken out.

Subsidized loans will also be difficult to replace with bond financing solutions, at least for the time being. According to data reported to the OeNB[14] subsidized loans (excluding housing loans) to nonbanks totaled some EUR 42 billion in mid-2015, thus accounting for some 13% of total direct lending to nonbanks. Since the data do not allow for a sectoral breakdown of subsidized loans, it is not possible to single out the share of corporate loans. Bonds are poor substitutes also for overdraft facilities. While commercial papers are an option, even if only for large corporations, they are not very common in Austria. When we equate overdraft facilities with short-term loans (with a maturity of up to one year), in mid-2015, MFI loans to nonfinancial corporations would have accounted for a share of approximately 28% of lending.

According to the financial accounts, two-thirds of the bonds issued by Austrian companies (66% based on end-2014 data) are held by nonresident investors (see chart 5).[15] International investors buy above all large liquid bonds externally rated by rating agencies. In Austria, this bond segment is dominated by public entities or by agencies. The share of bonds held by nonresident investors has increased by more than 10 percentage points since the onset of the crisis in 2008. At the same time, the share held by Austrian banks has halved, to close to 13%. Since 2011, the corporate bond portfolio of Austrian banks has even been decreasing slightly in nominal terms. Smaller bonds that are not externally rated and not included in any of the common indexes are unattractive for international institutional investors. Moreover, SMEs tend to be lesser known, which is one

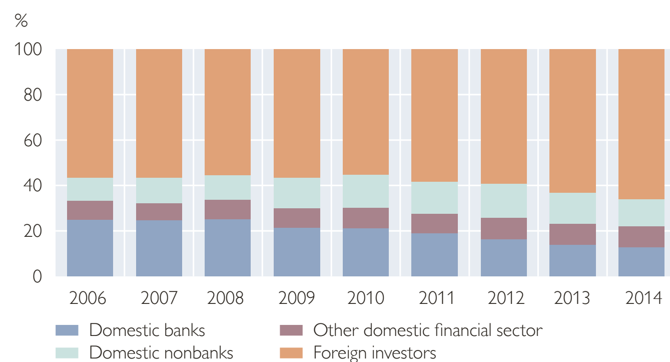
[14] *Based on asset, income and risk statements.*

[15] *International databases do not contain comparable data for other countries.*

more obstacle to raising capital in bond markets, above all from international investors. The extent to which the proposals of the action plan on building a capital markets union can effectively improve the risk assessment of smaller, lesser known companies depends on the design of the information requirements (Prospectus Directive, public access to company information). The same contingency applies to smaller bond issues that are meant to improve liquidity in bond markets.

Chart 5

Investor structure of Austrian corporate bonds



Source: OeNB.

2.3.1 Private placements

In addition to encouraging the placement of bonds in regulated markets, the action plan is also aimed at promoting the development of private placement markets across Europe. As a result, businesses whose financing needs are not big enough to allow them to tap regulated markets will have more funding choices. In this respect, the action plan is therefore supportive of private sector initiatives rather than having launched specific initiatives at the EU level. In some European countries, dedicated market segments have been developed for smaller businesses, with those segments essentially targeting the largest SMEs (Nassr and Wehinger, 2014). In those segments, the issuance requirements are less stringent, and ratings are not required. However, these initiatives have, in essence, remained national in their scope and have neither been able to overcome market fragmentation, which remains severe, nor able to attract much cross-border investment, which remains low (Nassr and Wehinger, 2014). A stronger harmonization of regulatory frameworks as proposed in the action plan on building a capital markets union, including investor protection rules, might push up cross-border financing volumes.

According to data published by the rating agency Scope (2015), in Germany a total of 149 issuers placed 194 mid-cap bonds ("Mittelstandsanleihen") with a volume of EUR 7 billion from 2010 to the first quarter of 2015. Rating requirements differ heavily across stock exchanges, ranging from exchanges which do not require ratings at all to exchanges which demand some kind of rating, to exchanges which have minimum rating requirements (Feiler and Kirstein, 2014). In the case of mid-cap bonds, the ratings are more likely to be provided by smaller rating companies, such as Euler Hermes, Creditreform or Scope rather than S&P, Moody's or Fitch (Steinbach, 2013). The absence of major-agency ratings makes such instruments less attractive for many institutional investors, though.[16] Therefore private investors tend to dominate. Despite the (good) ratings, the default rate was high for the mid-cap bonds. Out of the 149 issuers in Germany, a total of 30 companies with a cumulated issuing volume of EUR 1 billion had defaulted by the end of the first quar-

[16] *Another aspect that makes SME bond issuance less attractive is the fact that SMEs are not represented in indexes.*

ter 2015, which translates into a default rate of 15% (Scope, 2015).[17] Following the large defaults, the issuing volume declined in 2014, by 53% compared with 2013. Given the short maturities, this decline of investor interest implies a substantial refinancing risk for the companies involved (Scope, 2014).

In contrast, the German "Schuldscheine" market, to which the action plan specifically refers, is dominated by institutional investors. German Schuldscheine are financial instruments governed by German law that are used above all by German companies. The past few years have also seen an increase in nonresident issuers (Koller, 2014). The Schuldschein is legally not a security but a bilateral loan. As a rule, companies seeking to take out a Schuldschein will approach institutional investors directly.[18] Therefore such instruments are not subject to disclosure requirements and come with fewer reporting obligations. The relevant documentation is typically lean and standardized; borrowers are not required to submit an issuance prospectus or an external rating. A small number of lenders notably increases flexibility, discretion and confidentiality (if a company wishes to keep the transaction confidential; many companies, above all larger ones, will make their Schuldschein issues public). As Schuldscheine qualify as receivables and not as securities, they do not lead to market-driven write-downs that will be charged against profit (if they are part of the investment portfolio). For this reason, insurance companies are heavily invested in Schuldscheine, and they will typically hold them until maturity.[19,20]

3 Risk-capital financing instruments

3.1 Private equity

Apart from seeking to foster financing flows outside the banking system, the action plan on building a capital markets union also aims to strengthen risk capital financing. In this context, private equity plays a prominent role in the action plan. The regulatory framework for private equity was reformed at the European level a few years ago with the implementation of AIFMD (Alternative Investment Fund Manager Directive) and EuVECA (Regulation on European Venture Capital Funds). Based on those rules, the European Commission's action plan foresees a set of measures to support risk capital financing in the EU. The list of actions includes measures to revise the EuVECA and EuSEF[21] regulations and a proposal for pan-European venture capital funds-of-funds as well as financial support from the EU budget for multi-country funds.

Private equity funds are intermediaries that collect capital from investors which they invest in the form of (minority) interests in companies seeking capital. Private equity funds invest in

[17] *Almost one half of the defaults were related to sector-specific developments in the renewable energy sector. There were also some incidences of suspected fraud.*

[18] *In the case of smaller transactions, the conditions may also be tailored to the investment requirements of investors, in particular when structured bonded loans are involved.*

[19] *See Koller, 2014; Institutional Money, 2012.*

[20] *The other side of the coin is the limited liquidity of Schuldscheine. When a Schuldschein is transferred to an investor, the promissory note is handed over and notice is given to the paying agent and the issuer. Schuldscheine are not exchange-traded, and no electronic settlement takes place through clearing systems. This makes such instruments particularly adequate for buy-and-hold investors.*

[21] *Regulation on European Social Entrepreneurship Fund.*

private companies for a given period and also monitor and provide expertise and support for the management of the companies in which they invest. Especially in the early stages of funding, e.g. in the start-up and expansion stage of companies, such expertise and support is a key aspect of private equity financing (known as venture capital financing in this stage). Since third parties tend to know little about the conditions and outlook of such companies, private equity funds serve as "delegated monitors" for their investors (Diamond and Dybvig, 1983).

Furthermore, private equity also plays a role in the restructuring of and during ownership changes at mature companies. In this respect, the motivation to invest for financial rather than for strategic business reasons is also seen critically.[22] One point of criticism is that private equity funds are investors who look for short-term profits, dissolve reserves and dismantle the firms in which they invest, only to resell their stakes and leave the firms weaker off. Another point of criticism is that many of the acquisitions made by private equity funds are highly leveraged. The additional leverage placed on the companies taken over would put a high burden on them, or abundant dividends would weaken the company in its substance.

An annual survey on private equity activity in Europe (transactions but not stocks) is undertaken on behalf of Invest Europe, formerly known as EVCA (European Private Equity & Venture Capital Association). According to this survey, which has been undertaken since 2007,[23] private equity volumes have declined considerably since the onset of the crisis. While SMEs accounted for close to 85% of all transactions across Europe in the period from 2007 to 2014, they only had a share of 26% in private equity financing. The average volume of SME financing was EUR 2.6 million, which pales beside the average figure for a large company: EUR 39.5 million, or 15 times as much.[24]

In Austria, the volume of private equity financing is very low (see table 5). In the period from 2007 to 2014, Austrian companies raised EUR 3.6 billion in terms of gross private equity and venture capital financing. This sum corresponds to 0.13% of GDP, which is the lowest score for all countries under review here but Greece. The net equivalent, i.e. adjusted for disinvestment, was 0.07%. When we compare this amount with the overall volume of external finance or with the amount of equity capital raised from external sources according to the financial accounts, in order to take national patterns in corporate financing into account, Austria moves up somewhat in the ranking. However, the amount of private equity invested in Austrian companies is only about half the EU average. When we disregard the volume and look only at the number of

[22] For a comprehensive review of the problems that arise with this financing instrument, with a strong focus on the U.S.A., see Applebaum and Batt (2014).

[23] The data after 2007 are not comparable with those before 2007 because of a substantial change in the survey method. Given the small financing volumes, the annual data are driven by large individual transactions especially in smaller countries and are thus highly volatile. Therefore, this section looks at the average for the period from 2007 to 2014 instead.

[24] The data provided by Invest Europe do not allow for breakdowns by stage of financing or country.

Table 5

Private equity[1]

Funding volumes (total, 2007–2014)

	Funding volumes				Foreign share	Financing by foreign funds		Financing by domestic funds		Average trans-action volume	Num-ber of trans-actions	Share of high-tech	Venture capital	Initial funding for the com-pany
	Gross	Net position[2]								Gross (including financial services)				
	% of GDP	*% of GDP*	*% of com-pany liabili-ties*[3]	*% of equity capital*[3]	*% of debt funding*	*% of GDP*	*% of equity capital*[3]	*% of GDP*	*% of equity capital*[3]	*EUR million*	*% of compa-nies*	*% of debt funding*	*% of debt funding*	*% of debt funding*
AT	0.13	0.07	1.3	3.4	86.7	0.06	2.9	0.01	0.4	4.0	0.30	10.0	14.4	57.9
DE	0.25	0.09	2.6	9.5	17.8	0.02	1.7	0.07	7.8	5.2	0.47	9.9	11.2	48.6
UK	0.50	0.22	6.6	17.3	12.7	0.03	2.2	0.19	15.1	15.2	0.35	8.7	8.3	54.3
FR	0.36	0.16	2.0	4.2	16.4	0.03	0.7	0.14	3.5	9.5	0.23	9.3	10.3	41.9
IT	0.14	0.07	2.7	5.7	37.5	0.03	2.1	0.04	3.5	17.8	0.03	5.3	3.2	54.1
ES	0.20	0.07	4.9	2.2	21.5	0.02	0.5	0.06	1.8	12.3	0.06	7.8	9.0	57.8
NL	0.39	0.15	4.2	14.4	45.3	0.07	6.5	0.08	7.9	8.0	0.30	7.1	8.0	54.2
SE	0.56	0.28	3.4	9.8	31.1	0.09	3.0	0.19	6.7	5.4	0.50	9.4	13.0	38.6
BE	0.32	0.15	1.0	2.2	74.6	0.11	1.6	0.04	0.6	7.1	0.24	9.2	9.7	44.0
DK	0.42	0.12	4.4	2.6	35.1	0.04	0.9	0.08	1.7	11.3	0.37	20.6	10.3	44.4
FI	0.38	0.39	6.7	21.4	25.7	0.10	5.3	0.30	16.1	3.2	0.83	11.1	14.4	40.9
IE	0.17	0.10	0.7	–7.0	82.9	0.08	–5.8	0.02	–1.2	5.3	0.44	25.8	19.4	41.9
GR	0.04	0.02	0.7	3.4	41.2	0.01	1.4	0.01	2.0	16.9	0.01	1.4	13.0	82.5
PT	0.17	0.12	1.7	6.4	11.0	0.01	0.7	0.11	5.7	2.8	0.11	6.8	15.2	60.7
EU-14	0.33	0.15	3.4	7.8	27.6	0.04	1.6	0.11	6.2	10.1	0.29	9.4	9.8	48.9
AT/EU-14, %	39	46	39	43	315	157	181	8	7	40	102	107	146	118

Source: EAVC/Invest Europe, Eurostat, authors' calculations.

[1] *Excluding financial services.*
[2] *Gross position minus disinvestment.*
[3] *According to financial accounts data.*

transactions,[25] Austria moves up to a position that is even slightly above average. In absolute figures, Invest Europe registered 895 transactions in Austria in the period under review, which corresponds to 0.3% of all Austrian companies in 2012 and is in line with the average of the countries surveyed.

The comparatively high figure of companies receiving funding and the low amount of financing provided on balance imply that the underlying transactions are very small in the case of Austria. On average, private equity transactions totaled approximately EUR 4 million, which is slightly less than half the average of the EU countries under review. This outcome may be related to the lack of very large enterprises in Austria; at the same time, the share of large companies in the Austrian corporate landscape – as outlined in section 1.1 – is not that small. To some extent, the outcome may also be related to the relatively high share of early-stage funding we

[25] *Strictly speaking, the figures compiled by Invest Europe only provide evidence on the number of companies that received financing in a given year. If a company received funding from an investor more than once in a given year, these instances were counted only once.*

find in Austria. In 2007–2014, venture capital in the narrow sense of the definition accounted for 14.4% of all equity financing, which is a comparatively large share. What might also play a role is that more than half of the funds raised was made up of initial investments. Finally, the share of funds that went into the high-tech sector[26] was disproportionately high at 10%.

What is striking about the data for Austria is the high share of capital invested by foreign funds. On average, foreign funds accounted for 87% of all private equity financing in the period under review, which was the highest share among all countries under review. In smaller countries, foreign funds will generally have a higher share in financing than in larger countries. At the same time, private equity plays a small role in corporate financing in the first place in the countries where the domestic share is small (apart from Austria: Belgium and Ireland).

In the case of Austrian private equity funds, public agencies accounted for a very large share (33.5%) in the period from 2007 to 2012,[27] the European average being 5.1%. These figures no doubt reflect the fact that the Austrian authorities embrace public-private partnerships with a view to supporting venture capital. The development of innovative companies and the commercialization of new technologies are promoted by a dedicated agency, Austria Wirtschaftsservice (aws). Given the comprehensive support provided by aws, the comparative small volume of venture capital invested in Austria is unlikely to result from too low a degree of support. At the same time, this pattern also reflects the virtual absence of institutional investors among the investors in domestic private equity funds. In the period from 2007 to 2012, only 14.7% of the capital raised stemmed from institutional investors, compared with an average of 51.3% for the 14 EU countries reviewed here. Hence, the main problem of private equity financing in Austria would appear to be the size of domestic funding rather than access to foreign sources of finance.[28] It would, without doubt, be a good thing if international funds were to invest even more money in Austrian firms. However, given the specific functions of private equity/venture capital, chances of a substantial further increase in the share of foreign investors are low, as private equity funds prefer to invest in companies closer to home (Lerner, 1995).

What appears to be even bigger than the need for specific regulation is the indirect impact of other measures identified in the action plan on private equity, above all the measures aimed at strengthening capital markets that are relevant for exits. Typically, private equity investments do not pay any dividends. Investors often commit money for longer periods of time, reaping the benefits when they sell their stake, for instance during a successful initial public offering. As the information relating to private equity financing tends to be highly proprietary, measures to standardize credit information and simplify accounting standards are unlikely to create additional momentum. After all, in contrast to standard credit assess-

[26] *According to Invest Europe, which does not define the term "high-tech" in greater detail, though.*

[27] *Invest Europe has stopped publishing those data for individual countries.*

[28] *However, EVCA/Invest Europe (2015) considers even the European private equity funds too small in general to interest large institutional investors, given the high economies of scale involved in portfolio management and credit quality assessments.*

ments, private equity financing requires substantial management skills and business acumen.

One factor that was not addressed in the action plan is a possibly low demand for risk capital because of structural factors. Recent evidence (such as Jud et al., 2013) shows that the use of risk capital is highly correlated with numerous national indicators of education and innovation intensity, i.e. the number of university graduates, the share of technology-intensive industries, the size of public and private R&D budgets.

3.2 Crowdfunding

With a view to offering European companies, SMEs in particular, more choices of funding, the action plan also specifically mentioned the goal of promoting crowdfunding across Europe. Based on an analysis of crowdfunding markets in Europe, the Commission will decide on the best means to enable the development of this new funding channel across the EU.

"Crowdfunding"[29] is a generic term for a host of (mostly) online-based funding instruments. Crowdfunding builds on crowdsourcing, which is based on the idea of turning to a large and heterogeneous but otherwise unspecified group of people over the Internet for the implementation of certain tasks or projects. The evolution of the crowdfunding market has been largely driven by the Internet. In all forms of crowdfunding discussed here, online market places serve to pool funds committed by many individual investors. Those funds are then paid out to capital seekers, in the form of crowdlending, crowdinvesting or reward-based crowdfunding.

Given the relatively early stages of development, the available evidence on international crowdfunding markets is as yet inconclusive. The biggest data pool is that of Wardrop et al. (2015), who collected data from 255 European platforms for the years 2012 to 2014 in a dedicated European online survey (see table 6). Even if these financing in-

Table 6

Crowdfunding

Funding flows, 2012–2014

	Crowdlending	Reward-based crowdfunding and crowdinvesting	Total		Annual change from 2012 to 2014
	EUR million			*% of liabilities*	*%*
AT[1]	. .	. .	3.6	. .	. .
DE	78.1	6.1	84.2	0.002	115.0
UK	218.0	1,332.0	1,550.0	0.026	174.6
FR	94.1	8.3	102.4	0.001	111.7
ES	80.6	17.1	97.7	0.003	112.3
NL	29.5	57.0	86.5	0.005	102.2
Total (excluding AT)	500.3	1,420.5	1,920.8	0.008	127.7

Source: Wardrop et al. (2015).

[1] *Including other types of crowdfunding.*

[29] *For a comprehensive overview, see e.g. Beck (2014) or Sixt (2014).*

struments have been characterized by very high growth rates, their contribution to corporate financing is as yet very low. In Europe, market volumes have been highest by far in the United Kingdom, both in absolute terms and in relation to total corporate liabilities. Austria, in contrast, reports very low crowdfunding volumes.[30] What is important with regard to capital markets union is that to date crowdfunding markets have been highly fragmented along national lines. Almost 50% of the platforms surveyed by Wardrop et al. (2015) did not report any nonresident investments, 35% reported shares between 1% and 10%, and 10% reported shares between 11% and 30%.

To what extent crowdfunding instruments will provide companies with long-term access to financing depends on the tradeoff between investor protection and the cost burden resulting from disclosure requirements. Moral hazard and adverse selection problems, which are central problems in any financing decision, are particularly relevant for crowdfunding, given the myriad of information asymmetries that exist between investors, platforms and firms. These problems may lead to the creation of a "lemons" market, meaning that there is the risk that only firms unable to raise money in any other market may be left on the crowdfunding market (Dorfleitner et al., 2014; Wilson and Testoni, 2014). The adverse selection problems are often aggravated by the fact that crowd investors/lenders tend to contribute rather small amounts. Hence they will have less of an incentive or often limited means to meticulously analyze the firm in question, which may weaken the hoped-for "wisdom of the crowd" effect considerably. At the same time, crowdfunding investors are found to seldom offset this risk by adequately diversifying their portfolio (Dorfleitner et al., 2014; Wilson and Testoni, 2014). This will have implications not only for the financial assets of households, but may even deprive capital-seeking companies of this financing option in the event of large defaults. A number of platform providers have already begun to react to these problems by taking the initiative to conduct credit quality checks or implementing management systems that represent investor interests vis-à-vis the firms. In addition there are platforms which are open to investors only once they have proven adequate expertise in their field of operations or who are liquid enough to exceed high minimum investment thresholds (Wilson and Testoni, 2014). In other words, those platforms have been taking on more and more intermediary functions.

4 Summary

The action plan on building a capital markets union is aimed at supporting all forms of financing that are not directly linked to banks' balance sheets, by measures to improve market infrastructures and to strengthen the role of nonbank intermediaries. One priority of the capital markets union project are measures to encourage corporate risk capital financing, which is a valuable contribution to reinforcing financial stability also from an Austrian perspective, given the comparatively low capital ratio of Austrian firms. The idea is to facilitate access to equity

[30] An alternative source for recent data is CrowdfundingHub (2016); the data run up to 2015, but the country breakdown is less systematic. With regard to Austria, we find a total of EUR 11.1 million to have been raised for crowdinvesting purposes since 2013, of which EUR 8.1 million were raised in 2015 alone. These figures show that, while the momentum of crowdfunding has been increasing in Austria as well, its contribution to corporate financing has remained very small.

financing above all for highly innovative start-ups, which tend to be turned away from banks for moral hazard and adverse selection reasons. Such firms stand to benefit from simplified, harmonized and transparent capital market rules. Above all in the area of start-up financing and innovation funding, i.e. areas of financing which are typically not compatible with the risk profile of banks, there is definitely room for improvement in Austria, as is evidenced by the low rate of business births and the low volume of (domestic) private equity financing.

Another priority of the capital markets union project are measures to strengthen the role of nonbank intermediaries in the area of debt financing. Yet even if the relevance of loan financing declines further, banks will continue to play a major function in the overall financing process. After all, bank loans will remain the financing tool of choice especially for small and medium-sized enterprises, not least because of the discrepancy between the volumes typically needed by SMEs and the minimum deal sizes required for capital market financing. This barrier will remain in place even once the bar for the latter is lowered in line with the action plan for building a capital markets union. Recourse to the credit market will remain high also because firms' funding needs may fluctuate too much for them to tap the capital market or because collateralization requirements will be too complex. Furthermore, the shift toward capital market financing will help free up capacity on banks' balance sheets and increase their ability to lend to companies (including SMEs) which are not able or willing to raise capital in the capital markets.[31]

In Austria, a number of attempts have been made in the past to revive the capital market, yet any resulting effects have not been long lived. While measures to improve investor protection – such as rules enhancing the disclosure of company information or corporate governance rules for listed companies – have helped reduce information gaps, these measures have of course increased the cost burden from a company view. Above all for companies with smaller financing needs, these measures have not eased access to the capital market. Likewise, the attempt to spread the costs of raising capital more broadly by bundling individual issues failed to deliver in the end. Furthermore, measures to facilitate capital market funding by strengthening demand for Austrian shares – for instance with state-subsidized personal pension plans requiring a minimum share of stock exchange investments – were problematic from the perspective of risk diversification. From this perspective, measures as proposed in the action plan, which support cross-border investments, would appear to be more effective.

One way to combine the advantages of bank credit and capital market financing is the securitization of corporate loans by banks, which has so far played a lesser role in Austria. If or to what extent this may change in the future, depends on the actual design of securitized products, for instance on how securitizations are "tranched." While securitization may increase the willingness and/or capacity of banks to extend credit, as seen from the firms' perspective, it does not reduce their dependency on banks. Vice versa, securitization increases the capital

[31] *Also, banking regulators have been taking action to facilitate equity backing of SME loans (by implementing lower risk weights than for large companies, an SME factor, etc.) in order to support credit financing of SMEs by banks.*

market dependency of bank financing. To complete the picture, it is important to remember that securitized products, like bonds, make it considerably more difficult for banks to renegotiate the underlying contract in the event of payment difficulties.

A stronger involvement of institutional investors, such as loan-originating funds, may open up additional (or even new) financing options for projects with a high potential for growth and risk, given that funds tend to invest in higher-risk lending. At the same time, fluctuations in the risk tolerance of institutional investors may – contrary to the goals of capital markets union – add to the cyclicality of corporate financing facilities.

Even if the financing problems of companies in Austria have been rather limited, introducing greater financing choice, as envisaged by the action plan, may open up complementary financing sources for companies, thus reducing financing risks. Capital markets can contribute to stabilizing economic developments over the business cycle by making it easier or possible to spread the chances and risks of investment projects among a broader range of investors who are able and willing to shoulder the related risks. From a stability perspective, shifting funding responsibilities further away from the banking sector removes a layer of intermediation, even if a diversification of financing forms does not have a stabilizing effect per se. Generally speaking, a stronger capital market orientation will have major consequences for risk allocation within the financial system. While in bank-based financing systems, the financing risks are borne by the – increasingly regulated – banking system, capital markets union would redirect financing flows to other intermediaries or to private individuals. What is crucial in this respect is the ability and capacity of such lenders to adequately evaluate and monitor risk-taking. Cases in point are, first, the risks arising from developments in the German mid-cap bond market, which may go hand in hand with a higher exposure of private individuals to such instruments and, second, the increasing requirements concerning the assessment of risks implied by the choice of financial products issued by other intermediaries or, possibly even more relevant, of risks related to non-intermediated investments. These developments may, among other things, increase the need for financial literacy measures.

Another goal of the action plan is to help companies, SMEs in particular, overcome the information barriers for fundraising. Given the reduced availability of transparent and credible information on the economic condition of smaller firms and start-ups, the action plan includes measures to investigate how to develop or support pan-European information systems. As information gaps between capital providers and capital-seeking companies increase the cost of external financing, a higher degree of transparency may contribute to lowering companies' financing costs, or may even make fundraising possible in the first place. Moreover, a higher degree of transparency may improve risk identification and pricing in the financing process, thus reducing the misallocation of capital. However, the direct contact with investors and the need to keep them thoroughly informed (in particular when raising funds on a regulated market) also have considerable repercussions on the corporate governance structures of a company. Especially owner- or family-run businesses, which play a major role in Austria, may not be very forthcoming about internal corporate information.

Last but not least, the action plan for building a capital markets union left unaddressed a number of obstacles which have hampered cross-border financing in the past. Apart from persistent legal and tax differences, these obstacles include language barriers and political risks.

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