UK Finance

UK capital markets: the regulatory agenda

Four years of reflection have produced a broad package of targeted reforms designed to strengthen the UK as a place where companies and investors come together. Large and small, these reforms add up to a material evolution of the UK's regulatory framework. They now need effective implementation.

UK Finance supports the timely implementation of the regulatory reform package developed over the last four years in the UK, including:

- Delivering proposed listing reforms and ongoing review of disclosure, corporate governance and stewardship requirements for public markets.
- Embracing measures that harness technology and financial innovation, such as digitising share ownership, accelerating settlement times, delivering greater price transparency for investors and incorporating distributed ledger technology into the operation of UK capital markets.
- Enhancing the provision of investment research: a revised regulatory model for research payment that provides investors with flexibility on how they pay for research.
- Ensuring that UK regulators' new secondary objective to facilitate the competitiveness and growth of the UK economy helps deliver long-term strength for UK capital markets.

Global Counsel Research Partner

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What all of the measures in this package have in common is that each seeks in its own way to achieve a market that is more transparent, more efficient and better served by cutting-edge technology.

Regulatory change is not a silver bullet for strengthening the competitiveness of UK capital markets. That competitiveness reflects a wide range of factors that include tax and incentives, skills, and the strengths of the professional services sector that support capital market activity. However, transparency, efficiency and technological innovation in both primary and secondary markets are critical to their competitiveness. It is these dimensions that have been the target of a comprehensive and valuable package of regulatory reforms drawn up over the last four years.

That package has been prompted by UK capital markets starting to show some important weaknesses. The UK is a world leader in financial services. It consistently ranks in the top three financial centres globally and is a major financial centre in areas such as bond issuance. In terms of the total number of companies on its public markets and their total market capitalisation, the UK is one of the largest capital markets in the world. However, the number of domestic and international companies choosing to join public markets in the UK has fallen sharply over the last decade (see Figs 1-3).

The number of domestic companies using public markets in the UK has fallen by a third since 2010. The fall in the number of international companies has been even sharper. In contrast, several of the UK's major global competitors have enhanced their attractiveness as trading venues for international companies, especially the US Nasdaq exchange. For both domestic and international companies, UK capital markets have performed a vital role in helping companies already using the public markets raise additional finance both after the 2008 banking crisis and during the COVID-19 pandemic. However, they have been weaker in attracting new companies (see Fig 4).

The shrinking pool of companies joining UK public markets is a concern in both the domestic and international contexts. The number of domestic companies going public is one of the basic measure of the effectiveness of the capital market in supporting the UK real economy. The number of international companies going public in the UK is a measure of the success of the UK in attracting the best companies in the world to the UK.

Addressing this is the motivation for the set of wide-ranging regulatory changes for UK capital markets drawn up over the last four years. These are set out in the Annex. While many of these proposed reforms in the UK are individually small and can often seem unrelated, they add up to a material

UK capital markets in a global context

Fig 1: Capital markets by companies traded.
Number of companies traded, 2023 and change since 2015; excludes exchanges that do not host foreign companies.

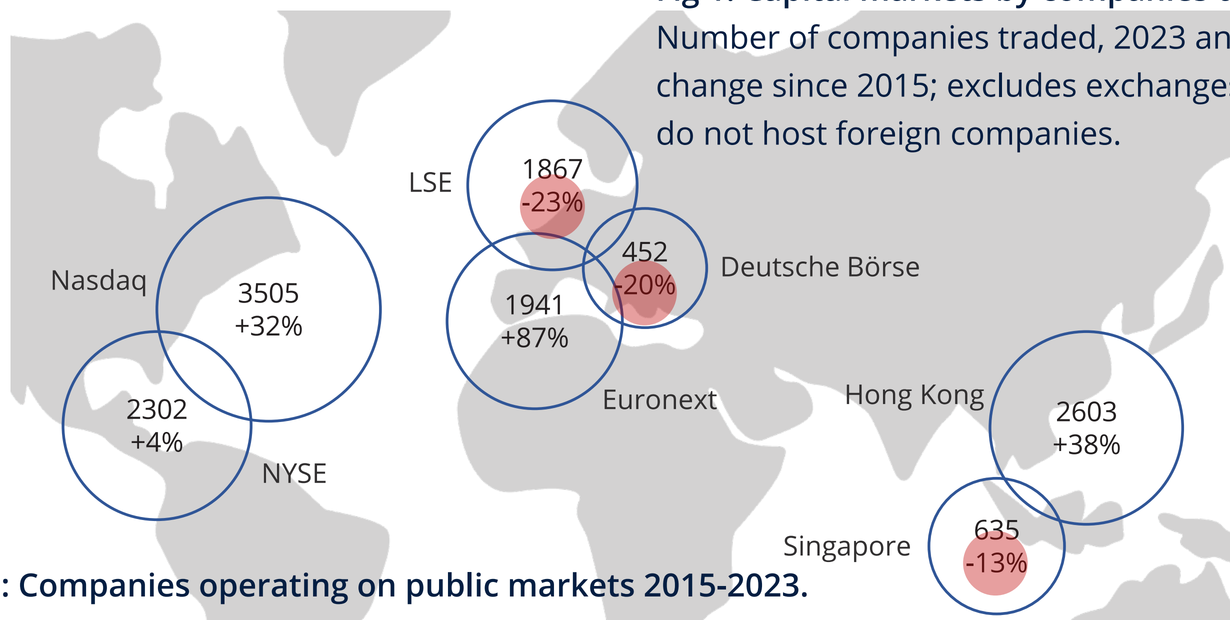


Fig 2: Companies operating on public markets 2015-2023.
Net change in number of companies.

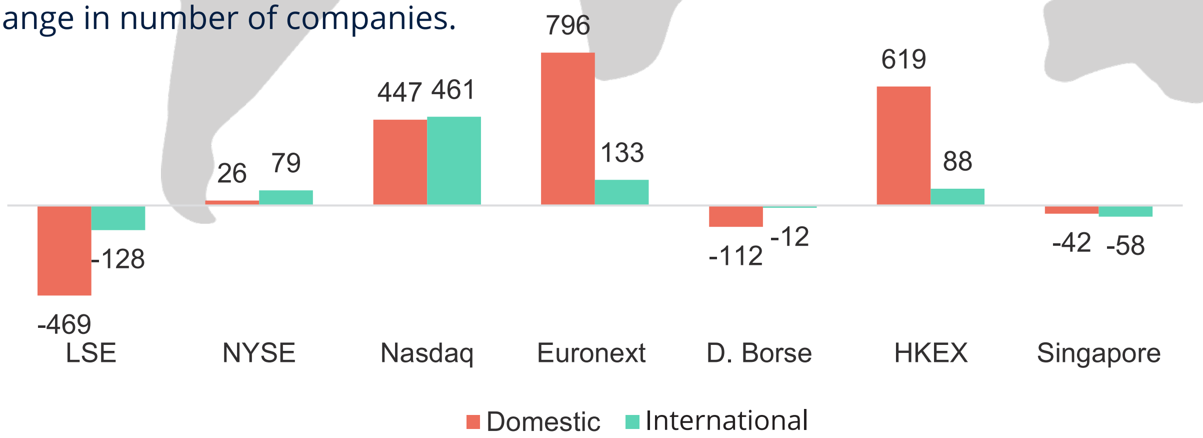
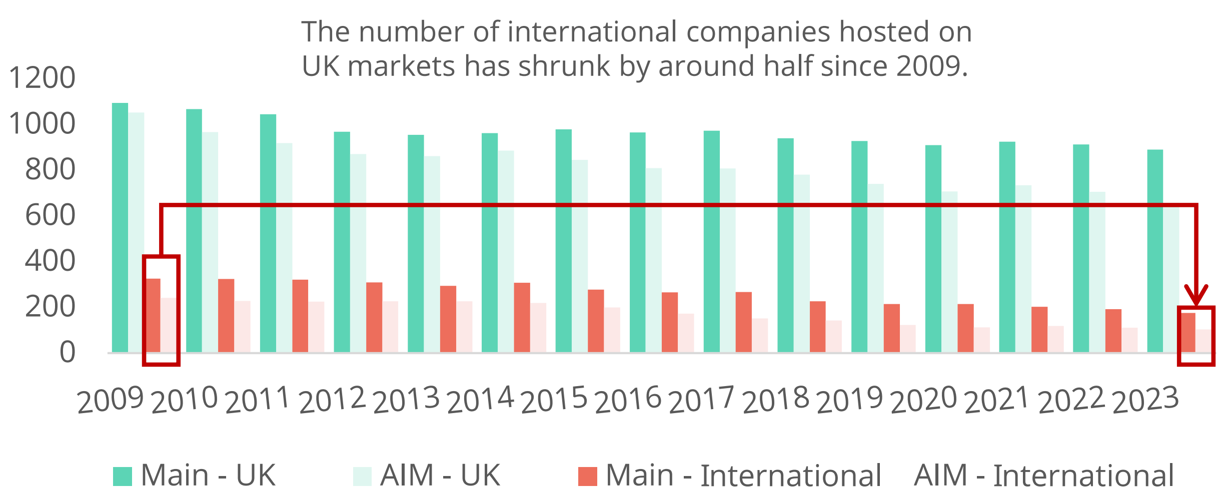


Fig 3: The cohort of companies participating in LSEG public markets in the UK has shrunk by a third over the last fifteen years.
Total companies listed on all LSEG markets, December of each year.



World Federation of Exchanges; London Stock Exchange Group

The most important contributions technology can make are those that make it simpler to participate in UK capital markets, including measures that increase price transparency and efficiency for market users.

evolution in the operation of UK capital markets. Although they can seem complex, what they all have in common is that they seek, in their own way, to achieve a market that is more transparent, more efficient and better served by cutting-edge technology. The UK must now focus on delivery and implementation of these reforms.

Listing and corporate governance reform

In any public market there are a range of rules which set the criteria for companies wishing to participate in the market. These include listing rules, market disclosure rules and corporate governance rules. To ensure that the UK capital markets remain attractive, it is important for these rules to keep pace with the needs of both companies and investors.

At the core of the most recent reform proposals is the concept of merging the current 'standard' and 'premium' listing segments on the London Stock Exchange Main Market into a single category with a proportionate set of obligations and a clear emphasis on disclosure. These reforms will help significantly in attracting more innovative and fast-growing companies to join public markets and grow in the UK.

However, listing rules cannot be viewed in isolation. They need to be considered as part of the wider framework that adds up to the experience of being a traded company in the UK. Alongside listing reform, there is now an opportunity to create an improved disclosure regime for securities offerings via the new Public Offers and Admissions to Trading Regime (POATR).

In parallel, the UK must also reflect on how its corporate governance framework supports companies and their investors. Robust rules can provide assurance and confidence for investors, but proportionate governance requirements are also a key consideration when companies are choosing where to join a public market. The key is to see admission, disclosure and governance rules as a single package and not in isolation. For example, the benefits of improvements to the UK listing regime could be outweighed by overly restrictive corporate governance requirements once the company is traded. It is important that the UK strikes the right balance across these areas. As a priority:

- Proposed reforms to the UK listing framework from December 2023 should be implemented at pace to give companies the confidence to join public markets in the UK now.
- The ongoing changes to the POATR should focus on ways in which prospectus requirements can be simplified and streamlined, including by helping remove

unnecessary duplication between the public offer regime and ongoing disclosure requirements. The UK should also look for ways to ensure that relevant documentation produced in selected peer markets can also be used in the UK to simplify the process of joining public markets or fundraising in the UK. As with listing reform, it is important for the UK to move as quickly as possible in this area.

- The current review of the UK corporate governance framework should take a holistic view of the obligations of public companies to ensure that duties are proportionate, transparent and provide robust controls, which investors value. The UK should ensure that in developing disclosure frameworks, especially in key areas such as ESG, it does so without creating unnecessary burdens on companies seeking to take advantage of equity and debt markets. In setting such frameworks, the UK should play a leading role in aligning global standards across key markets.

Technology leadership in capital markets

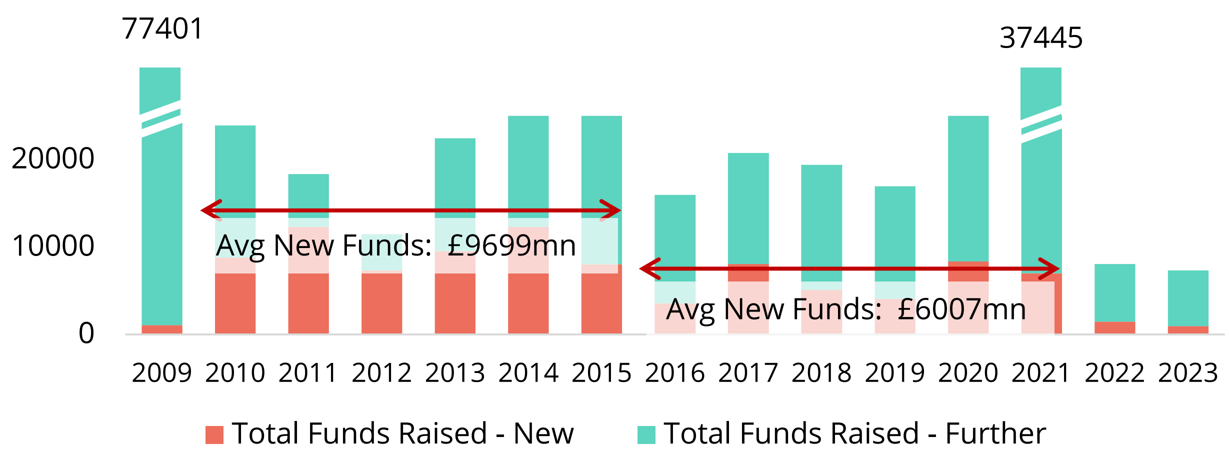
Changes in technology inevitably shape the way capital markets operate and evolve. The most important contributions technology can make are those that make it simpler to participate in UK capital markets, including measures that increase price transparency and efficiency for market users. Against this benchmark, there are several changes that the UK should focus on.

- The UK should implement proposals to improve market transparency by making available real-time pricing information, as far as technically possible, for both bonds and equities. This would be delivered via a UK 'consolidated tape' which will bring together prices and volumes of all the trades in a specific asset class that take

New and follow-on fund-raising

Fig 4: UK capital markets have been a valuable source of further finance for publicly-traded companies after the 2008 and COVID crises, but have had a declining role in new equity issuance.

New and further funds raised on main market (£mn).



LSEG

place in the UK. This will inform investors of prices and volumes in a timely manner, leading to greater market participation. The UK government should follow through on commitments to implement a UK consolidated tape for bonds, and not delay plans for an equities tape.

- The interim conclusions of the Digitisation Taskforce in 2023 have identified a set of changes that aim to enhance the efficiency of UK capital markets and improve the experience of investors in engaging the companies they invest in. Digitisation of the shareholding system, ending the issuance of paper share certificates and requiring the carefully managed conversion of extant paper shares to digital ones is key. Digital Annual General Meetings (AGMs) could also encourage wider participation, which is important in attracting individual investors back to shareholding. The Taskforce's work should now be the basis for reflection on how these aims can be best achieved.
- The UK needs to carefully consider the merits of an accelerated UK settlement regime. The US is moving to a regime that settles transactions the day after trade date (Accelerated Settlement or T+1). European policymakers are therefore considering a similar future move in order to harmonise global settlement cycles. This would be a significant market transformation with cross border implications. There is no competitive advantage for the UK to move ahead of the EU and Switzerland or vice versa. Therefore, the UK's move to T+1 should be contingent on a robust cost/benefit analysis, drawing on lessons learnt from US implementation. The UK should coordinate with the EU and Switzerland to ensure a consistent European regional approach with sufficient preparatory time for market users.
- The UK should signal its ambition to lead the world in securities tokenisation and harness the momentum created by the launch of the Digital Securities Sandbox. Widespread industry participation in the Sandbox, experimentation with securities tokenisation and the corresponding use of distributed ledger technology would accelerate innovation, improve operational efficiencies and help retail investors access capital markets in new ways. To realise this ambition, the UK must now form a joint industry and regulatory group to provide recommendations to drive the UK's leadership in the digital assets transformation.

Supporting informed investors: the role of investment research

High-quality research provides objective, informed analysis of companies joining public markets or trading on a market and is often invaluable for investors. Current UK rules require the separation of research and execution costs when these are provided to market users. These 'unbundling' rules, introduced in 2018, may have impacted the provision of investment research in the UK.

There is little case for sustaining an outright ban on bundling research costs as part of an investor service package. Instead, greater optionality should be introduced to empower clients to choose whether they wish to pay for research on a bundled or unbundled basis. Current rules[1] that require, in certain circumstances, investment research on a company joining a public market to be published seven days after the company publishes its registration document are also unnecessarily restrictive and should be changed.

The convening power of government

In addition to the ongoing regulatory reforms, the UK government should better exercise its convening power and hold an annual capital markets summit in the UK. This should convene UK policymakers, UK companies and investors, both domestic and international. It would help to promote UK capital markets and demonstrate the opportunities available for international companies in the UK. It would also be a vital forum for debate on future regulatory evolution in capital markets.

Conclusion

The international competitiveness of UK capital markets and their success in attracting and supporting a deep pool of growing companies is not simply a question of regulation. The UK needs the right frameworks for tax, skills and digital infrastructure as well as a supportive culture of risk and reward. However, the regulatory regime for primary and secondary markets in the UK is key. A strong primary market needs an efficient and transparent secondary market where prices are clear and trades can be completed quickly and efficiently. A healthy secondary market needs a strong pool of companies seeking to join public markets. Both need informed, empowered investors. The right regulatory reform package can and will strengthen all of these.

The UK has a unique opportunity to refresh its regulatory framework, make up some of the ground it has lost internationally over the last decade and reinforce its global strength. It has never been more important for industry and political leaders to work together to enhance the international competitiveness of UK capital markets and strengthen them as the engine of domestic company growth.

Companies will continue to evolve in terms of their needs and preferences, as will the investors that support them. Technology will continue to define what is possible in many areas of capital markets, including efficiency, transparency and widening participation. Enhancing the UK's capital market strength means having a regulatory framework that is ready to evolve with them.

How can I support this agenda?

- Support rapid and comprehensive implementation of the package of reforms set out in the Annex, alongside timely consideration of the aims of the Flint, Austin and Kent reviews.
- Support ongoing reform to UK listing and public offer rules in 2024, conducted in close coordination with changes to corporate governance and stewardship requirements as part of a single framework for taking a company public in the UK.

1 FCA COBS 11A.

Annex: Measures currently under review or scheduled for implementation

What unites technical changes like accelerated settlement times on UK secondary markets with changes to listing rules for UK primary markets? They are part of a single package of proposed changes that have emerged over the last four years in the UK to improve the transparency, efficiency and technological sophistication of UK capital markets. That package now needs to be completed and implemented.

Policy	Origin and policy vehicle	UK Finance policy recommendation	Why does it matter?
Market Data (a UK consolidated tape)	Wholesale Markets Review and subsequent FCA consultations	Implementation of consolidated tapes for both bonds and equities	The consolidated tape will enhance market transparency for investors of all sizes
Accelerated Settlement (T+1)	Edinburgh Reforms – HMT Accelerated Settlement Taskforce	A move to T+1 once a thorough cost/benefit analysis and detailed assessment has been carried out, following the US's implementation, leveraging lessons learnt there	Enhanced speed and efficiency for market users and maintaining harmonised practice across major jurisdictions
Short Selling Regulation	Edinburgh Reforms – HMT consultations and upcoming FCA consultations	Improvements to the regulation such as: • The market-maker application process can be made more efficient • A positive securities list held by the Financial Conduct Authority (FCA) • Reforming the scope (removing UK Credit Default Swaps (CDS) and UK sovereign debt) • Public disclosures to move to aggregated net positions	Reform will ensure the UK's regulatory regime alleviates disproportionate burdens and improve its effectiveness and efficiency

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Digital Securities Sandbox	Edinburgh Reforms – 2023 Summer consultation	Ensure a smooth transition for entities choosing to enter and subsequently exit the Sandbox	The Sandbox will encourage experimentation and digital innovation
Digitisation/ Dematerialisation of shares	Mansion House 2022 – Digitisation Taskforce launched	Adopt model three as the most viable approach for publicly-traded companies	Technological advancement and simplification will benefit issuers and investors
Investment Research	HMT Investment Research Review	Ensure regulatory change to introduce more optionality on how to pay for investment research	A healthy research market is an enabler of an attractive UK capital market where investors can obtain the information they need to make informed decisions
UK Listing reform	HMT Listings Review	Implement the enhanced single listing regime	Reform will alleviate disproportionate burdens, increase efficiencies and boost UK competitiveness
Reform of the UK public offer (prospectus) regime	HMT Listings review FCA Public Offer Engagement Papers and expected consultations	Design and implement an integrated, coherent continuing obligations and disclosure regime	Reform will alleviate disproportionate burdens, increase efficiencies and boost UK competitiveness
Implementation of the UK Corporate Governance Code	Restoring trust in audit and corporate governance DBT White Paper (2021)	Proportionate implementation and reassessment of the operation of the "comply or explain" model	Reform will foster growth and competitiveness
Reform of the Stewardship Code	Stakeholder and market feedback on 2020 revisions to the Code	Ensure effective and proportionate stewardship both for companies and investors	Reform will foster growth and competitiveness