

Comments from the Norwegian Ministry of Finance to the EU Commission CMU Midterm Review, March 2017

The Norwegian capital markets are well-functioning vehicles for providing capital to small and medium-sized entities. Please find below a description of the markets, and some proposals for the CMU Midterm review.

1 Description of the Norwegian capital markets

Introduction

The Nordic capital markets are primarily SME-markets. Although some of the listed companies are large in a global context, the market capitalisation in the Nordic region is small on an absolute basis compared to other EU countries.

The Nordic bond market, particularly in Norway and Sweden, has developed into an important alternative source of funding for SMEs. The Norwegian bond market is generally acknowledged to be a well-functioning market for such issuers.

A typical feature of the Norwegian market is the importance of, and specialisation in, oil and gas, shipping and seafood. The market places, advisors and regulators have specialized competence in those areas, and the growth in the equity and debt markets is highly dependent on these sectors. Oslo Stock exchange also attracts listings and investments from other parts of the world where the same sectors are present, such as from Canada and Singapore, even though these companies have no other presence in Norway.

Market infrastructure, regulated markets and MTFs

The main part of the trading in Norway in listed equity instruments, i.e. shares and equity certificates, is made through Oslo Børs, which also operates the regulated market Oslo

Axess, as well as the trading venue Merkur Market, authorized as a multilateral trading facility (MTF). Oslo Børs and Oslo Axess offer dark pool functionality through its North Sea Dark Pool.

In Norway, a minor part of the trading volume in equity instruments is made outside the trading venues, i.e. over-the-counter (OTC). Equity instruments listed on a Norwegian regulated market, may also be traded on trading venues outside Norway, which includes the MTFs Turquoise, First North and AQUIS.

The fixed income market consists of the bond market (maturity of one year and more) and the money market (up to one year maturity). Oslo Børs offers listing of bonds and certificates on its regulated market, and operates the unregulated trading venue Nordic ABM which is not subject to regulation and supervision. At Nordic ABM the continuing obligations for issuers are mainly equal to those of Oslo Børs, but there are no prospectus listing requirements or IFRS requirements.

Nordic Trustee, which is owned by institutional investors, takes care of third-party financial entitlements on a contractual basis. Its primary function is to act as trustee for the investors in interest-bearing securities (<http://nordictrustee.com/>). The Group has established dedicated trustee companies in Norway, Sweden, Denmark and Finland, and also has a representative in Iceland.

The only Norwegian Central Securities Depository, VPS ASA (VPS) has its own settlement system, VPO NOK, consisting of settlement of securities entered into VPS and corresponding cash settlement between banks in Norges Bank (the central bank). The settlement is based on the principle of delivery versus payment (DvP).

Oslo Børs has an agreement with two CCP's for clearing of trades in equity instruments, LCH.Clearnet Ltd and SIX x-clear AG. Both the CCP's are participants in the settlement system of VPS.

Equities

Primary market

The Norwegian stock market, represented by Oslo Børs, has developed positively. During the period 2005-2016, Oslo Børs had the highest number of new listings among the

Nordics, totally 240 IPO's compared to 143 in Stockholm, 64 in Copenhagen and 37 in Helsinki.

During the last twenty years, the total number of listed companies has been stable above 200, with lower numbers only in 2003 and 2004. The number of new listings on an annual basis has varied between 3 and 58, averaging 20.6. On average, 18.8 companies have been delisted each year. The latter is mainly due to the market for mergers and acquisitions. From 2005 to 2016, the listed companies at OSE and NOTC (Norwegian over-the-counter venue) issued EUR 63 bn. in new equities, averaging EUR 5.7 bn. annually.

*Please see **Appendix 1** "Number of companies, new listings and delistings".*

Secondary market

Compared to many other markets, Oslo Børs (OBX) has given investors on average a positive return on investment during the last years. For the period 30.12.08-31.01.2017 the OBX Total Return Index has given investors 212.44%.

Liquidity development for the period 2003-2017 in terms of turnover and number of trades is given in **Appendix 2**. This development has been affected by regulatory changes and new trading venues which has given competition among market places. In addition there has been a decline in trading volumes after the financial crisis.

Investors

The shareholder structure of the companies listed on Oslo Børs is split between:

- Foreign investors: 36.7% (including Norwegians who have emigrated and are operating from outside Norway)
- Government and municipalities: 33.2%
- Private companies : 16,4%
- Mutual Funds: 7,7% (increased from 3,6% in 2007)
- Private Investors: 4,1%
- Other: 1,4%

The large part held by the government is mainly explained by the Norwegian government's ownership in some of the largest companies.

Large private investors hold their investments at Oslo Børs in private companies primarily for tax purposes, while retail investors primarily invest through investment funds. The government is currently working on a proposal to create separate investment accounts in order to give all private investors the advantage of deferred tax. This intends to increase the private investors' investments in shares and funds and to remove the lock-in effect of capital gain tax.

For ownership structure and development of size in the Norwegian bond and money market funds and the equity funds please refer to **Appendix 3a and 3b**.

Debt capital

The corporate bond market has developed significantly during the past years. In the period 1997-2004, Norwegian listed corporates raised an average of EUR 3.5 bn annually in risk capital combined, about half of this in corporate bonds and the other in equities. For the last four years, 2013-2016, the annual average risk capital issuance has been EUR 14.2 bn EUR annually, with 70% coming from bonds.

The yearly new issuances and taps on Oslo Stock Exchange and Nordic AMB, excluding government bonds and treasury bills, have grown from EUR 10.8 bn. in 2002 to EUR 38.2 bn. in 2016. This shows the importance of the debt market in order to finance important Norwegian sectors (oil and offshore) and as a supplement to the traditional bank financing.

Several factors have strongly contributed to the development of this bond market, creating an important and alternative funding source for medium sized corporates:

- Efficient documentation processes, facilitated by Nordic Trustee
- Efficient electronic securities depository systems (VPS)
- Methods and models for mark-to-model pricing (Nordic Bond Pricing)
- «Shadow ratings» published and regularly updated by several banks and investment banks for each issuer.

The banks play a dominant role in the market for bond and certificate issuance and trading in Norway, whereas in the corporate bond market, the independent investment firms have an important role as these issues need broad international investor distribution.

The number of issuers in the Norwegian listed bond market has increased significantly. In 1999 there were 158 unique issuers and at year-end 2016 there were 236. Corporate / industry bonds represent the main increase in number of issuers (29 in 1999 and 112 in 2016).

For further details see **Appendix 4** "Number of issuers at year end"

The outstanding volume per 31.01.2017 is dominated by four sectors:

- Covered bonds: 29.3%
- Other financials (Bank and insurance): 24.0%
- Government bonds: 23.2%
- Non-financials: 17.2%

The total outstanding volume has increased from EUR 70.5 bn. in 2006 to EUR 203.7 bn. in 2016, an annual growth of 11.2%. The number of outstanding loans has in the same period increased from 926 to 1,918, and the average size of these loans has thus increased from 76 million Euro to 107 million Euro.

Please refer to **Appendix 5** "Outstanding nominal value and number of issues" for further details.

The total turnover, measured by value, has not shown the same increase. From 2006 to 2016, the total turnover increased on average by 5.2% per year, mostly due to a reduction in trading volumes during 2006-2009. From 2009 to 2016, the total turnover increased on average by 7.8% annually. It is also worth looking closer at how the proportion of the traded volume has developed per issuer sector as displayed in **Appendix 6** "Turnover by value (NOK million) excluding repo"

Investors

The ownership structure of all bonds listed on Oslo Stock Exchange as at year end 2016 shows that most of the bonds are owned by insurance undertakings and private pension funds, foreign investors, banks and mutual funds. Private retail investors primarily hold their investments through Investment funds and insurance products.

Please refer to **Appendix 7** for development and further details of ownership in bonds and certificates.

Credit ratings in the Norwegian bond market

An important condition for a well-functioning bond market is credit ratings. Credit ratings in the Norwegian markets are used as follows:

- **Financials:** Almost all of the outstanding covered bonds have an official rating. Of the 25 covered bond programs in Norway, only four do not have an official rating. However, only 19 of the Norwegian banks have official ratings (of a total of 127 banks).
- **Non-Financial Corporates:** Only a few of the biggest issuers have an official rating. Most of the issuers, even large companies, do not have official ratings
- **Municipalities:** Only two of the biggest municipalities, Oslo kommune and Stavanger kommune, have official ratings, representing EUR 3.4 bn. of approx. EUR 15.6 bn. of bonds and commercial paper outstanding from municipalities.

Investors in corporate bonds, particularly in SMEs, have relied on so-called "shadow ratings". These are informal credit assessments published by Norwegian banks and investment firms as part of their investment recommendations for fixed income securities, and as such not requested or paid for by the issuers.

The experience from the Norwegian market is that «shadow ratings» enhance and contribute to investor protection. The ratings provide important information regarding credit risk and pricing, and they are not influenced or controlled by the issuers. Further, there is a disciplinary market mechanism in place since there are several banks and investment firms issuing such ratings on each issuer. The costs related to official ratings are of a prohibitive nature for use by SMEs. In this context, the use of "shadow ratings" has worked well.

The Norwegian bond market has been effective for SMEs and small savings banks. The normal loan size is typically EUR 15 – 500 million, and an efficient and standardized loan documentation framework has been put in place (30-40 pages).

Measured per capita, the volume of Norwegian high yield issuances has for some years been between 3.5 and 8 times larger than within EU. The Norwegian high yield market is an alternative source of funding for borrowers representing a higher credit risk, other than bank financing.

ESMA is currently investigating the practice of "shadow ratings" in the Nordic market through a process directed towards the major pan-Nordic banks. Due to this investigation, 4 of the 5 banks involved have already stopped issuing "shadow ratings" and are now communicating relative risk in their investment recommendations without applying a grading system.

2 Proposals for the mid-term review

The objective of the Capital Markets Union (CMU) is to enhance the efficiency of capital markets in support of the wider economy, in order to stimulate growth and job creation. The Nordic bond market has become an important source of funding for SMEs and savings banks, creating a significant and alternative funding source for medium sized corporates. Several features of the Nordic and Norwegian bond market could serve as ideas for how to improve the efficiency of corporate bond markets, and corporate finance in general, in which companies and investors may operate in a cost-effective, stable and fair manner.

The regulatory developments in recent years have been ever more demanding for participants in the financial markets. Also for regulators this has been a challenge. The number of new regulations and reporting obligations and the detail of the regulation have been difficult to absorb.

Detailed regulation creates entry barriers to the market which favours the larger, already established players. The amount of regulation prevents smaller organizations from entering the capital markets.

For the Norwegian market, which is mainly a SME market, the detail of regulation is an important factor for the ability of the market to evolve. In Norway both Merkur Market, which is a listing MTF, and Nordic ABM, which is an unregulated bond market, illustrate that the regulatory aspects are important in attracting SME's to the capital markets. For Nordic ABM the ability to use national GAAP and not being required to file a full prospectus have been important features.

An example of regulation which might be positive for smaller markets is the regulation of SME growth markets and especially the SME growth prospectuses. There are signs that this will increase the possibility to have more alternative investment markets, with a more robust regulation. Therefore we would support further such initiatives.

We would welcome further initiatives which promote SME markets and the ability to maintain and develop small markets in Europe. We do, however, recognize that measures to improve the financing of the real economy and SMEs must be designed in a way that does not jeopardize financial stability in the longer term.

We would also like to point out that provision of so-called “shadow ratings” has been one of the features contributing to a well-functioning market for corporate and bank debt. Several Norwegian banks and investment firms have previously published «shadow ratings» as part of their investment recommendations for fixed income securities. The experience from the

Norwegian market is that «shadow ratings» enhance and contribute to investor protection. Such assessments provide important information regarding credit risk and pricing and they are not influenced or controlled by the issuers.

Investment research is subject to the MiFID and MiFIR regulations. Recently, ESMA has however strongly indicated that the publication of «shadow ratings» falls within the scope of the Credit Rating Agency Regulation and that the provision of this type of investment analysis without an authorisation as a credit rating agency would be in conflict with the CRA regulatory framework.

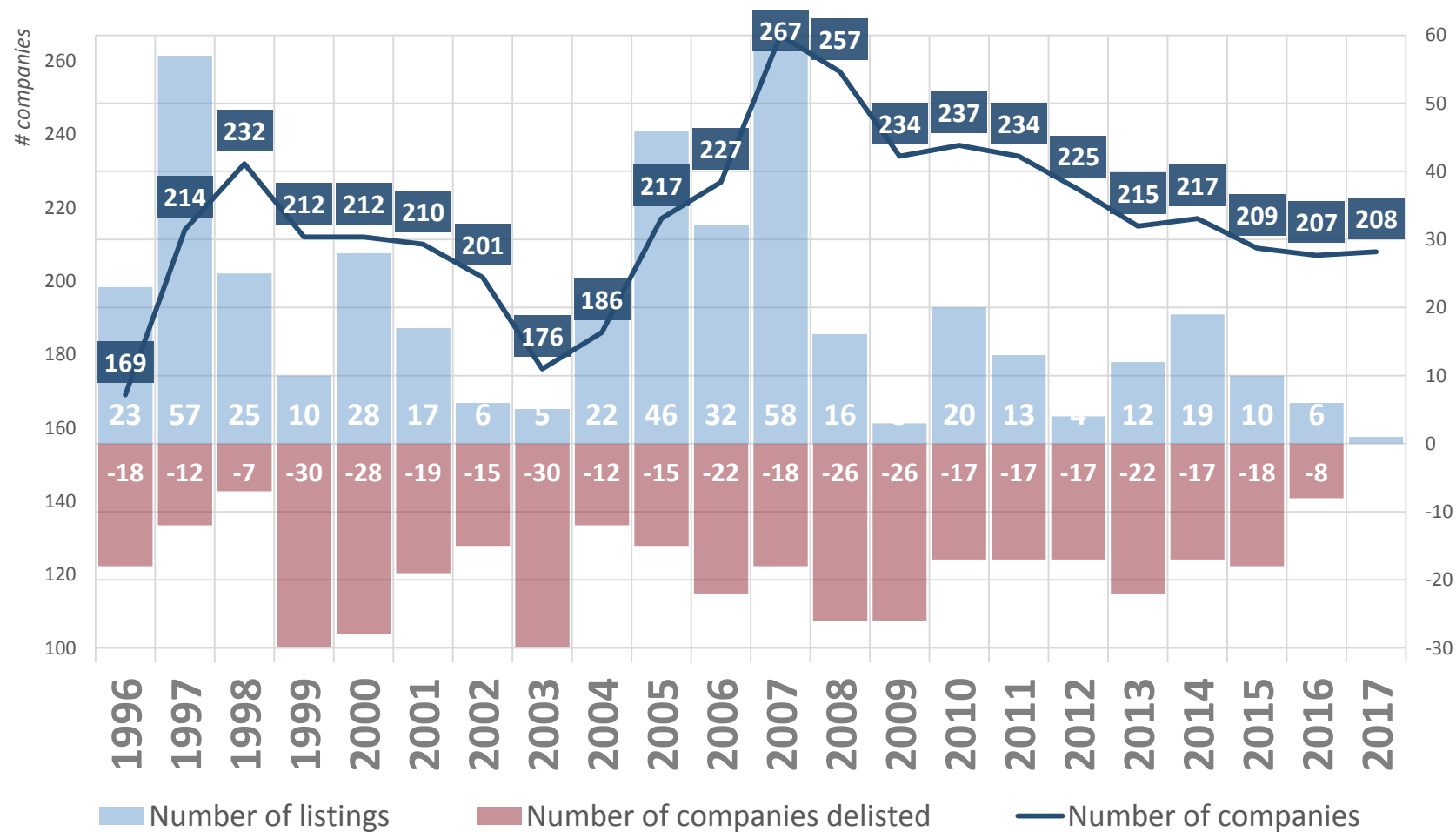
“Shadow ratings” have not been accepted for capital adequacy (CRD IV) or solvency purposes (Solvency II). Investors and other market participants use “shadow ratings” for information purposes and in investment mandates. As is recommended by the Norwegian Asset Manager Association (VFF), many asset managers require each issuance to be either publicly rated by at least one official rating agency, or “shadow rated” by at least two different broker firms or banks. «Shadow ratings» are also an important source of information for mark-to-model valuations.

Based on our experience, the concept of "shadow rating" could be a useful supplement to official ratings for the SME-market. We do, however, note that this probably would require an amendment to the Credit Rating Agency Regulation Article 2, in order to limit the scope of the regulation and extend the list of situations where the Credit Rating Agency Regulation does not apply.

Appendix 1

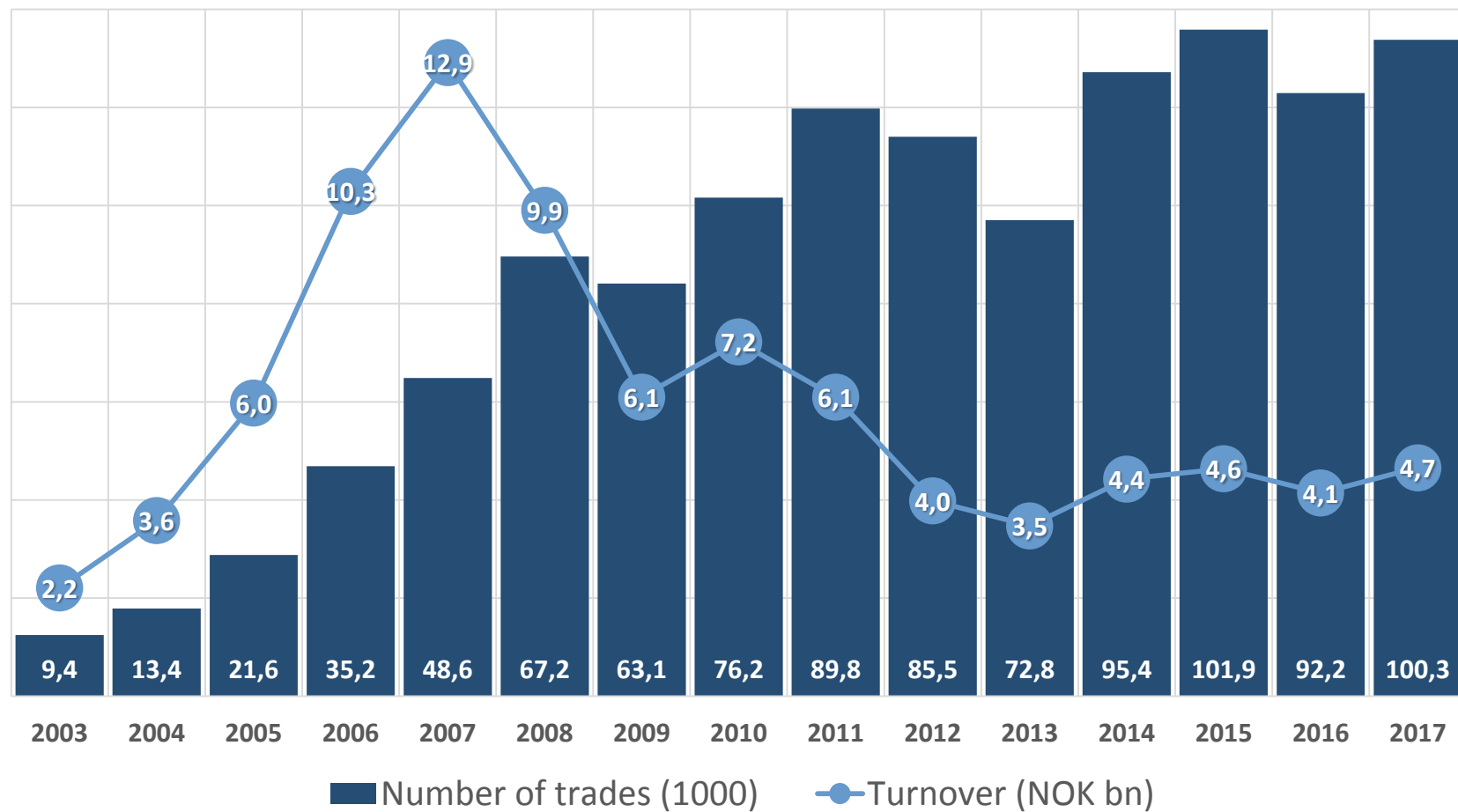
Number of companies, new listings and delistings

Oslo Børs and Oslo Axxess



Per 31.01.2017
Source: VPS / Oslo Børs

Turnover and number of trades

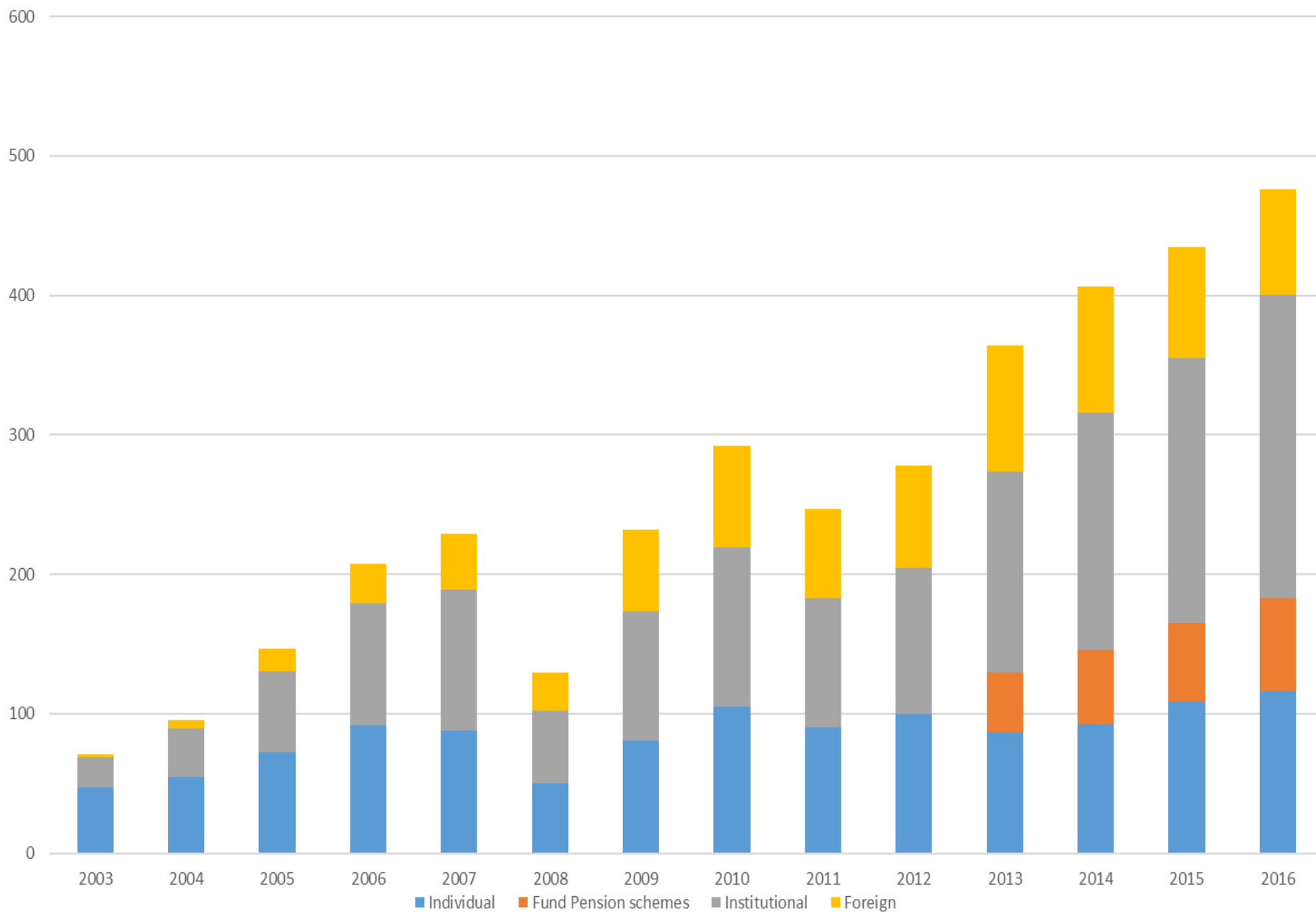


Appendix 3a

Norwegian equity funds 2003 - 2016

NOK Billion

Ownership sector

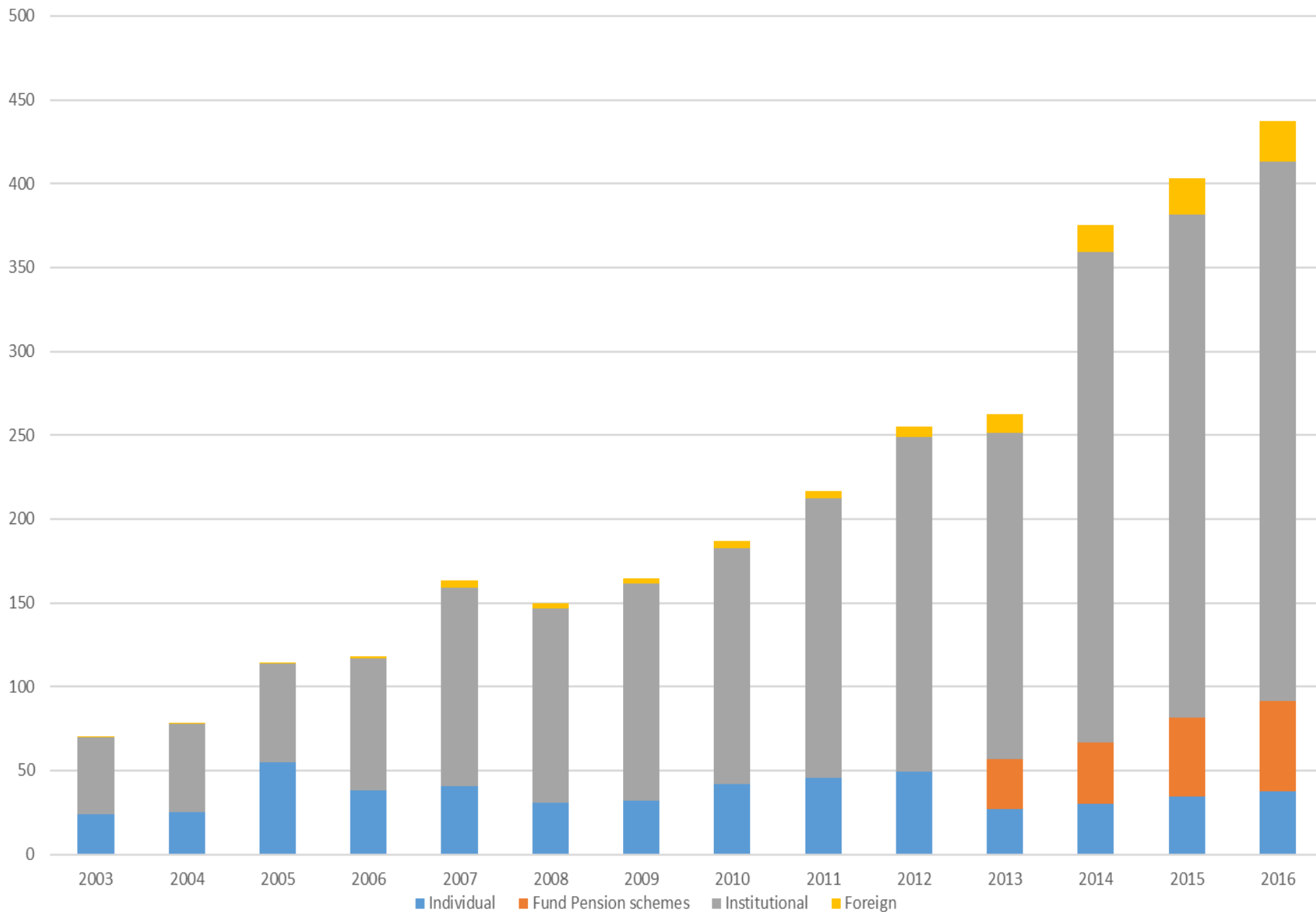


Appendix 3b

NOK Billion

Norwegian bond and moneymarket funds 2003 - 2016

Ownership sector



Appendix 4

*Number of issuers at year end**

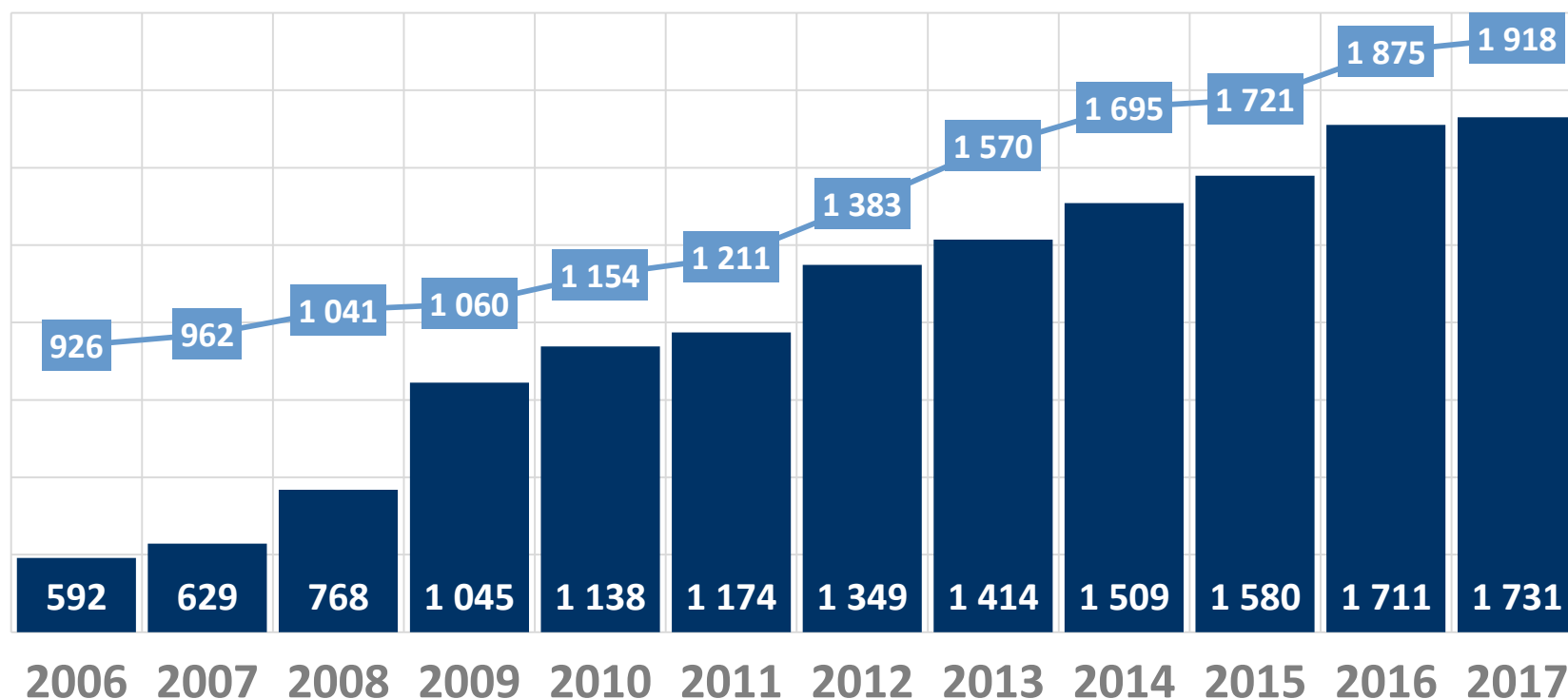
	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2011	2011	2012	2013	2014	2015	2016
GRAND TOTAL	158	178	202	196	178	173	172	157	143	119	107	105	110	122	134	192	195	253
BONDS																		
Government	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
Government guaranteed	4	2	3	3	3	3	3	3	2	1	1	-	-	-	-	-	-	-
Gov. owned enterprises	2	2	2	2	2	2	3	2	3	3	3	3	2	2	2	2	2	2
Local governm. & guar.	117	106	102	85	77	66	54	43	32	19	15	12	11	12	11	8	13	55
Covered bonds	-	-	-	-	-	-	-	-	2	4	5	10	11	12	15	16	17	17
Bank & insurance	41	43	46	54	49	45	38	36	30	26	24	20	17	14	15	22	20	25
Mortgage banks	7	7	8	9	10	11	10	9	9	8	7	8	7	8	7	7	5	5
Industry	29	33	37	44	46	57	67	70	69	59	54	57	64	76	86	109	108	112
Foreign	2	2	2	5	4	7	9	7	7	7	7	7	4	2	3	2	2	1
Perpetual Hybrid Tier 1	-	-	-	-	-	-	5	5	5	5	5	8	10	13	17	14	16	18
Total bonds	158	178	202	195	178	173	171	157	140	119	106	105	110	120	134	181	184	236
Of which:																		
Subordinated loan capital	20	20	21	20	20	22	16	12	13	12	10	6	5	5	6	9	10	12
Convertible incl. w/warr.	6	7	10	6	5	8	8	9	11	10	5	4	1	-	-	2	1	2
BILLS & CERTIFICATES																		
Treasury bills	1	1	1	0	1	1	1	1	1	1	1	1	1	1	1	1	1	1
Other certificates	3	2	4	5	6	9	10	9	12	8	15	11	9	16	12	10	10	16
Total bills & certificates	4	3	3	6	7	10	11	11	14	9	16	12	10	17	13	11	11	17

* One issuer may be represented in several industries.

Outstanding nominal value and number of issues

■ Outstanding nominal value Oslo Børs and Nordic ABM (NOK bn)

■ Number of issues Oslo Børs and Nordic ABM



Per 31.01.2017
Source: /Oslo Børs

Appendix 6

Turnover by value (NOK million) excluding repo

	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
GRAND TOTAL	959.550	737.905	659.176	736.808	948.843	745.706	646.370	690.402	617.390	677.143	1.332.515	1.653.203	1.436.161	1.392.103	1.308.541	1.008.716	1.044.997	1.044.640
BONDS																		
Government	637.393	488.194	423.030	443.335	527.063	357.706	312.859	350.295	293.045	319.405	294.919	332.269	302.086	290.703	372.763	362.164	436.284	406.672
Government guaranteed	25.516	14.198	1.193	944	3.445	519	65	53	265	430	-	-	-	-	-	-	34	298
Gov. owned enterprises	6.286	5.831	6.548	3.396	19.374	15.499	7.052	3.692	2.194	2.344	2.086	705	1.381	39	173	701	14.192	20.274
Local governm. & guar.	13.862	13.525	11.177	12.043	7.566	5.357	3.912	2.286	3.939	2.072	3.017	2.884	4.692	4.017	8.828	10.995	237.424	279.222
Covered Bonds	-	-	-	-	-	-	-	-	1.119	6.587	11.486	26.360	113.429	124.114	175.092	256.452	237.424	279.222
Bank & insurance	58.345	48.689	53.937	69.108	77.195	80.637	72.540	90.583	73.387	51.823	46.262	31.593	18.164	19.275	19.837	26.438	26.908	41.463
Mortgage banks	27.665	24.773	17.708	24.181	29.076	23.005	17.610	16.892	7.242	4.650	3.619	3.092	2.142	3.956	8.450	7.461	11.679	6.989
Industry	6.667	7.469	10.809	11.740	20.995	31.719	42.713	36.083	35.057	24.240	30.306	25.842	33.110	53.802	93.494	97.508	78.170	76.774
Foreign	630	31	2.545	3.622	2.109	331	800	2.619	2.007	132	2.074	712	877	746	2.110	774	417	101
Perpetual Hybrid Tier 1	-	-	-	-	-	68	504	344	146	113	63	314	247	594	2.197	2.720	2.326	2.756
Total bonds	776.364	602.710	526.947	568.369	686.823	514.841	458.055	502.848	418.402	411.796	393.832	423.771	476.128	497.246	682.944	765.213	807.434	834.549
Of which:																		
Subordinated loan capital	885	2.008	2.686	2.813	3.715	3.772	2.698	1.258	903	1.093	575	463	404	130	993	1.107	1.610	2.861
Convertible incl. w/warr.	374	371	122	186	136	600	510	287	457	120	547	269	745	17	-	170	26	876
BILLS & CERTIFICATES																		
Treasury bills	158.104	127.290	116.234	157.682	252.434	220.099	174.972	170.968	183.549	247.840	922.149	1.213.263	942.750	880.630	611.281	229.324	228.408	199.887
Other certificates	25.082	7.905	15.995	10.757	9.586	10.766	13.343	16.587	15.439	17.507	15.380	16.169	17.285	14.292	14.315	14.179	9.155	10.205
Total bills & certificates	183.186	135.195	132.229	168.439	262.020	230.865	188.315	187.555	198.988	265.347	937.529	1.229.432	960.035	894.921	625.597	243.503	237.563	210.092

Per 31.12.2016
Source: Oslo Børs

Ownership structure bonds and certificates

	BONDS																
	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%
Companies	6,7	6,9	5,8	5,8	6,1	6,6	5,9	4,6	5,7	4,3	3,3	4,2	2,4	2,1	1,9	2,2	2,3
Government & municipalities	3,3	3,5	4,5	5,3	4,5	4,3	3,6	3,4	2,6	2,1	2,0	1,9	2,0	1,9	2,1	1,9	1,4
The national bank	2,0	1,5	1,4	1,2	*	*	*	*	*	*	*	*	*	*	*	*	*
Social security administration	7,0	6,4	5,6	5,2	6,0	5,8	6,5	6,9	8,6	13,4	15,0	14,7	11,7	10,4	7,3	7,1	7,2
Banks	14,3	14,2	15,9	15,7	16,4	14,7	15,7	10,6	11,8	10,6	12,0	15,9	17,9	19,9	21,5	22,0	22,5
Mutual funds	5,4	6,9	5,9	5,8	8,1	10,2	11,1	9,5	7,1	6,6	5,9	5,6	6,2	5,9	7,8	7,9	7,8
Mortgage companies	4,7	4,0	4,6	4,0	4,5	3,3	2,5	2,0	1,5	2,9	3,9	3,7	4,8	5,8	4,3	5,8	7,4
Insurance & Private pension funds	36,5	37,7	37,9	38,4	38,6	37,9	34,7	32,6	32,0	27,8	23,7	22,7	21,9	23,2	21,6	20,3	19,5
Private investors	3,1	3,9	3,9	3,9	4,0	4,3	3,4	0,9	0,6	0,6	0,6	0,5	1,2	0,8	0,4	0,5	0,4
Foreign investors	16,8	14,4	14,3	14,3	11,4	13,1	16,7	29,4	30,1	31,5	33,6	30,8	31,8	29,7	32,5	31,8	31,1
Others	0,2	0,6	0,2	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,1	0,4	0,6	0,4	0,4
Total	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

	CERTIFICATES																
	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%
Companies	7,1	5,7	3,6	1,6	1,7	2,7	3,1	2,3	4,2	0,6	0,4	1,3	0,1	0,1	0,1	0,2	0,1
Government & municipalities	6,0	5,8	6,2	0,4	0,6	1,3	1,4	1,3	2,8	0,5	0,8	4,2	9,2	5,3	1,9	0,8	2,9
The national bank	2,1	1,7	5,5	*	*	*	*	*	*	*	*	*	*	*	*	*	*
Social security administration	4,8	2,8	1,0	13,4	12,9	8,3	9,3	10,5	20,3	7,9	7,8	9,0	9,6	12,0	24,3	24,9	33,4
Banks	17,2	13,6	11,9	12,0	12,3	12,7	16,0	10,3	15,9	48,9	40,2	34,5	36,9	37,1	20,2	16,9	16,2
Mutual funds	17,3	18,7	21,5	8,6	10,2	27,3	23,3	14,8	5,4	3,2	4,0	5,4	4,1	2,0	8,4	9,8	8,0
Mortgage companies	2,6	3,6	3,6	5,1	4,3	3,4	4,8	11,7	3,5	1,9	4,5	2,3	2,5	1,6	1,3	12,4	2,6
Insurance & Private pension funds	32,9	39,1	38,9	52,5	51,8	39,7	30,4	24,2	22,3	7,1	10,5	18,0	17,5	21,7	28,6	22,8	25,6
Private investors	0,2	0,2	0,1	0,0	0,0	0,0	0,0	0,0	0,7	0,0	0,0	0,0	0,1	0,8	-	-	-
Foreign investors	8,5	8,1	7,6	6,4	6,2	4,4	11,6	24,7	24,8	29,8	31,9	25,3	20,0	19,3	15,2	12,1	11,3
Others	1,3	0,7	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,2	-	-	-
Total	100	100	100	100	100,0	100	100	100	100	100	100	100	100	100	100	100	100