

Recent developments in non- bank financing of Spanish firms

Victor García-Vaquero and Irene Roibás

Abstract

The banking sector has traditionally played a key role in the financing of Spanish non-financial corporations (NFCs), much more substantial than other alternative sources, such as securities markets or venture capital. The past crisis evidenced that a high degree of dependence on a single source of funding may constitute an element of vulnerability for firms. Against this backdrop, in recent years there has been a process of financial disintermediation, with firms replacing part of their bank loan financing with the issuance of securities (bonds or equity) in official or alternative markets and with equity financing through venture capital entities. Specifically, in the period 2009-2017 NFCs raised funds for an average annual amount of €50 billion through securities markets, compared with an average annual decline of €34 billion through loans. Also, the recently created crowdfunding platforms have become a new alternative channel and although their volumes are marginal for the time being, they could experience stronger growth in the next few years, as has occurred in other European countries.

Keywords: Securities markets, financing of non-financial corporations, alternative markets, venture capital, crowdfunding platforms.

JEL codes: E44, G21, G24.

RECENT DEVELOPMENTS IN NON-BANK FINANCING OF SPANISH FIRMS

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Introduction

Traditionally, non-financial corporations (NFCs) have mostly been reliant on credit institutions to obtain external financing, while capital markets and, in general, non-banking intermediaries, have played a less significant role, except in the case of trade credit. This funding structure is explained, at least in part, by the characteristics of a business sector with a highly significant presence of SMEs (in 2016 they accounted for 99.7% and 64% of NFCs and NFC employees, respectively). SMEs encounter more difficulties than large firms in the issuance of securities owing to both the fixed costs which these transactions usually involve (they are a higher share of the total cost owing to the smaller amounts of the issues) and asymmetrical information problems deriving from the lower quality and quantity of information available on their economic and financial position. These difficulties are even greater in newly created companies, as they have no credit history, or in those engaging in innovative businesses, since their future performance is less certain.

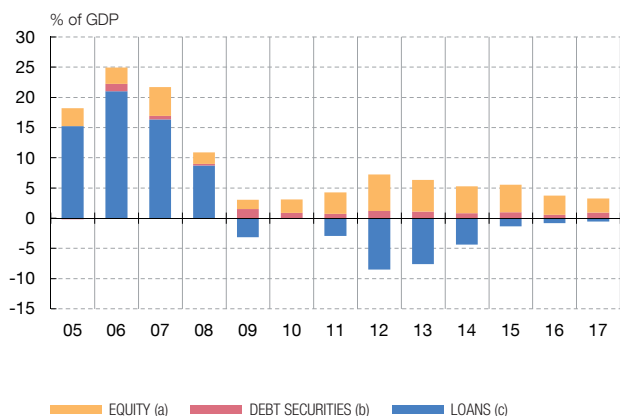
However, the recent crisis has underlined that an excessive dependence on a single source of funding is an element of vulnerability, particularly in times of strong macrofinancial tension. In this connection, different initiatives have been launched in recent years to encourage the development of non-banking sources of financing. Thus, EU and national authorities have fostered the development of both securities markets, such as the Mercado Alternativo Bursátil (alternative stock market, MAB by its Spanish acronym) and the Mercado Alternativo de Renta Fija (alternative fixed-income market, MARF by its Spanish acronym), and certain alternatives to bank-based financing, ranging from new types of venture capital companies (SME venture capital entities) to crowdfunding and crowdlending platforms. The launch of these initiatives, together with other factors, such as low interest rates, the introduction of a corporate debt securities purchase programme of the Eurosystem and financial regulations changes, has led to a greater diversification of sources of corporate financing. Additionally, an intense deleveraging process has been carried out by NFCs to reduce the high levels of debt, particularly bank debt, accumulated in the years running up to the financial crisis. All of this has been reflected in significant changes in the funding structure of NFCs, with an increase in the weight of own funds relative to debt and, within debt, in that of debt securities relative to bank loans. Loans have declined more sharply in Spain (from 32% of the total balance sheet in 2007 to 25% in 2017) than in the euro area (from 30% to 29%, respectively) (see Charts 1.1 and 1.2).

This financial disintermediation process has taken place across all industrialised countries. Thus, an increase is observed in the share of bonds in total liabilities throughout all developed countries (except Japan), although the euro area is still far behind the economies whose capital markets are more developed, such as the United States and the United Kingdom (see Chart 1.3). This change, however, has been particularly pronounced in Spain, where the importance of debt securities vis-à-vis total interest-bearing liabilities doubled from 7% in 2007 to 14% in 2017 (see Chart 1.4¹).

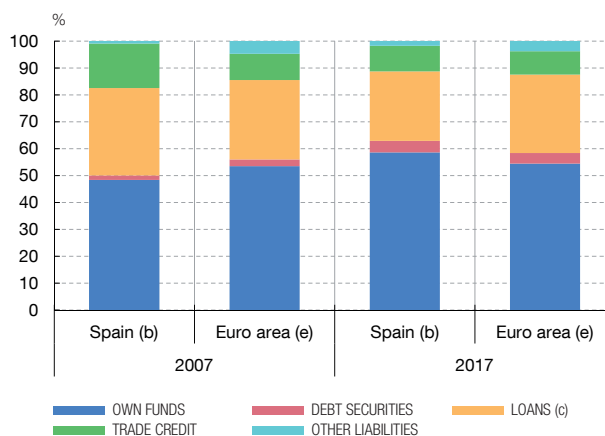
¹ The comparison of this indicator between Spain and the euro area should be regarded with caution, since in the case of Spain issuance by non-resident subsidiaries (which has a high weight in the total as mentioned later on in this article) is included, whereas this adjustment was not made for the euro area.

In recent years, there has been a process of financial disintermediation, with firms replacing part of their bank loan financing with the issuance of debt securities and equity instruments. This process of financial disintermediation has been widespread in all industrialised countries, although more intense in the case of Spain. Specifically, in the period 2009-2017, Spanish non-financial corporations raised funds for an average annual amount of €50 billion through securities markets, compared with the decline of €34 billion in financing through loans.

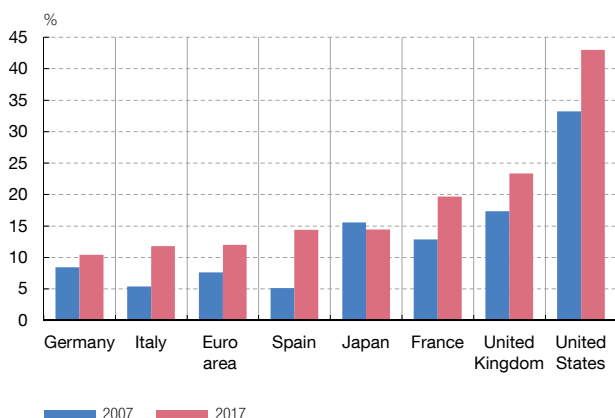
1 LOANS VS FINANCING IN SPANISH MARKETS. NET LIABILITY FLOWS



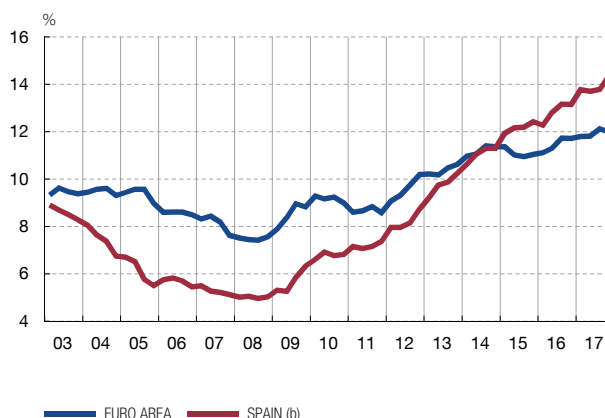
2 STRUCTURE OF NON-FINANCIAL CORPORATIONS' LIABILITIES (d)



3 DEBT SECURITIES AS A PROPORTION OF DEBT (f) International comparison



4 DEBT SECURITIES AS A PROPORTION OF DEBT Spain and the euro area



SOURCES: Eurostat, BIS and Banco de España.

- a Includes net issuance of shares by listed and unlisted companies, and other shares issued by companies whose legal form is not a public-limited company.
- b Debt securities include issuance by resident and non-resident subsidiaries.
- c Includes loans from resident credit institutions and loans from the rest of the world.
- d Includes intercompany positions.
- e Debt securities do not include issuance by subsidiaries.
- f Debt includes debt securities and total loans (bank loans and other loans). Data obtained from the BIS, except as regards the euro area (Eurostat) and Spain (Banco de España). Data for Spain include issuance by subsidiaries (resident and non-resident), not included for other countries, which may affect comparison of results.



The object of this work is to analyse recent changes in the sources of corporate financing constituting an alternative to that from banks. Following this introduction, this article comprises five further sections. The next two sections describe financing through the bond and equity markets, respectively. Section 4 focuses on the new securities markets for small firms. Section 5 describes venture capital financing and the last one discusses financing through crowdfunding platforms.

Bond markets

The number of Spanish firms raising funds through the issuance of bonds has increased substantially in recent years (the number of issuers rose sixfold from 2007 to 2017 (see Chart 2.1). This change was boosted by a general setting of economic recovery, particularly in connection with corporate productive investment, and by the lower relative cost of this type of funding in comparison with bank loans, partly owing to the Eurosystem corporate sector purchase programme (CSPP),² and by the introduction of several regulatory changes, which are described below.

The most significant regulatory change in this field is the approval of Law 7/2015 of 27 April 2015 on the promotion of business financing, which changed the bond issuance regime in two ways from April 2015. First, the quantitative limit on bond issuance by sociedades anónimas (public limited companies, Spanish SAs) was lifted.³ Second, sociedades limitadas (private limited companies, Spanish SLs) were allowed to issue uncovered bonds, which they were previously not allowed to do. However, this was quantitatively restricted to a maximum amount equal to twice their own funds, unless the issuance is secured (in which case there is no limit).

Additionally, from 2014 the issuance of bonds meeting certain requirements was permitted,⁴ in particular that they be admitted on a regulated market, including that of the Asociación de Intermediarios de Activos Financieros (Association of Securities Dealers, AIAF by its Spanish abbreviation) or on a multilateral trading facility (such as the MARF) by any company resident in Spain, and that they not be subject to withholding taxes or to taxation in Spain in the case of non-resident investors. Also, certain obligations to provide information to the tax authorities were lifted.

All of these factors, together with the boost given by the creation of the MARF (which is discussed in Section 4), led to an increasing prominence of medium-sized issues (between €5 million and €100 million) (see Chart 2.2). The increasing number of issues is in part associated with issuing firms that were smaller than usual and that traditionally had not used this channel for financing.

By economic sector, over the course of the period analysed, this form of financing spread to more economic sectors, such as wholesale and retail trade and hospitality activities, in line with the increase in the number and types of firms accessing this market. The most active sectors in recent years have been transport and communications, followed by industry, energy and other utilities and, more recently, real estate and construction (see Chart 2.3).

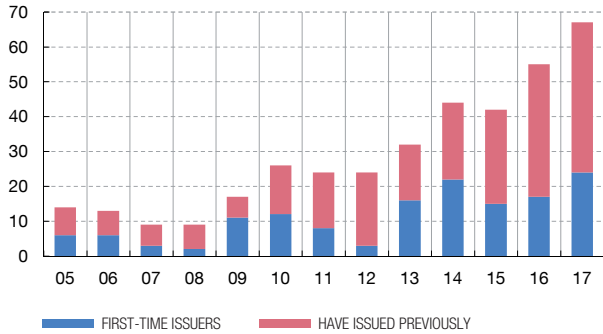
2 For further details, see S. Mayordomo “The Eurosystem corporate sector purchase programme and its effect on the external financing of Spanish non-financial corporations”, Economic Bulletin, November 2016, Banco de España.

3 Prior to the approval of Law 7/2015, the limit was equal to the paid-up share capital plus the reserves recorded in the latest approved balance sheet, unless certain guarantees were granted (although this limit was not applicable to listed SAs or to credit institutions).

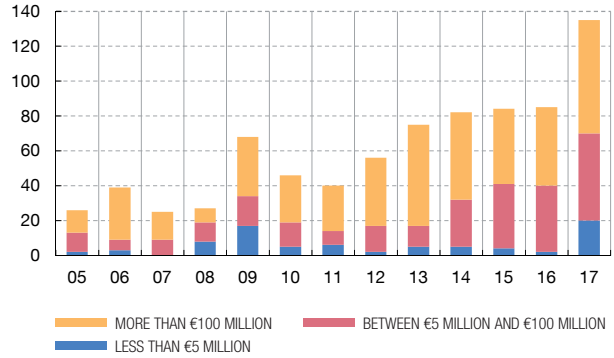
4 Pursuant to Law 10/2014 of 23 June 2014 on the regulation, supervision and solvency of credit institutions.

The number of Spanish firms that raise funds through the issuance of debt securities has increased notably in recent years, as have the number of issues, with medium-sized firms playing an increasingly prominent role (between €5 million and €100 million). Also, more sectors have been included, such as the wholesale and retail trade and hospitality sector. However, a substantial portion of issuance by the main corporate groups takes place abroad, through non-resident subsidiaries.

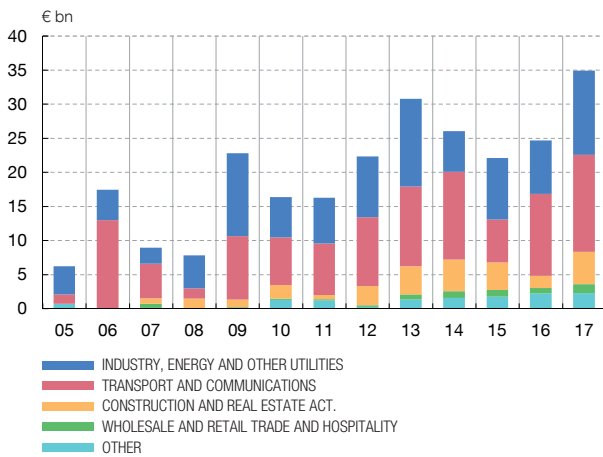
1 NUMBER OF ISSUERS OF DEBT SECURITIES. SHORT AND LONG TERM. (a)



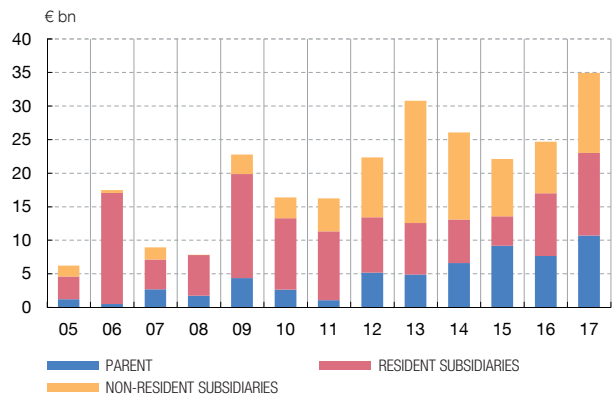
2 NUMBER OF ISSUES BY SIZE. LONG TERM



3 GROSS ISSUES OF DEBT SECURITIES BY SECTOR. LONG TERM



4 GROSS ISSUES OF DEBT SECURITIES. LONG TERM



SOURCE: Banco de España.

a Owing to the lack of historical data, first-time issuers are considered to be those firms issuing debt securities for the first time since 2005, with no outstanding balances in 2005 of prior years' issuance.



Finally another important feature of Spain's debt securities market is that a substantial part of issuance by leading corporate groups is performed abroad through non-resident subsidiaries (see Chart 2.4).

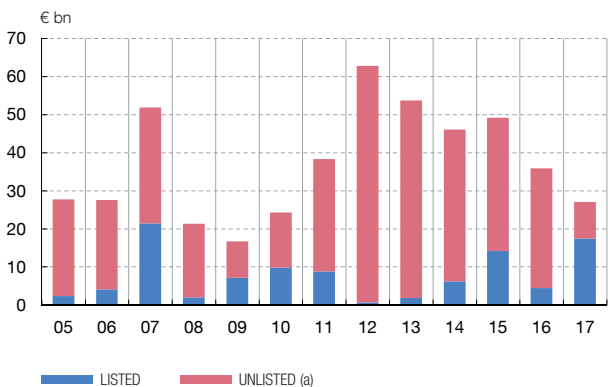
Equity markets

Since the start of the crisis, recourse to equities has been the main source of external financing for firms, with net flows that have always been positive over the period analysed (representing €37.1 billion in annual average terms, and €27.1 billion in 2017), which is consistent with the deleveraging process described in Section 1 (see Chart 1.1). As seen in Chart 3.1, the bulk of such issuance is by unlisted companies.

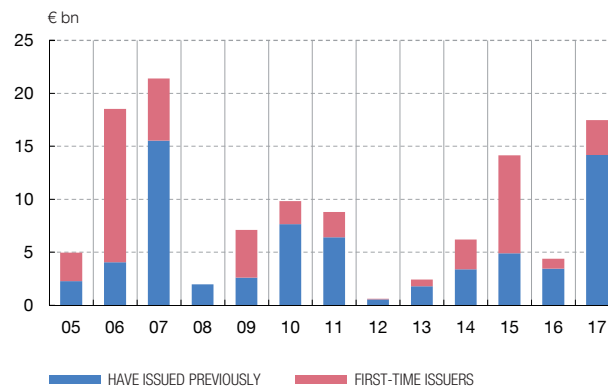
In the case of listed companies, for which the statistics available provide a more detailed breakdown, the volumes obtained do not show a defined trend over the period analysed (see Chart 3.2). This volatility in terms of financing volume obtained by NFCs through

Since the onset of the crisis, equity has been the main source of external funding of firms, with the bulk of such issuance being by unlisted firms. In the case of listed firms, for which available statistics provide a more detailed breakdown, the volumes raised vary greatly from year to year, as can also be observed in the breakdown by sector of activity. In recent years, new issuers have appeared, although their numbers as a proportion of the total continue to be limited.

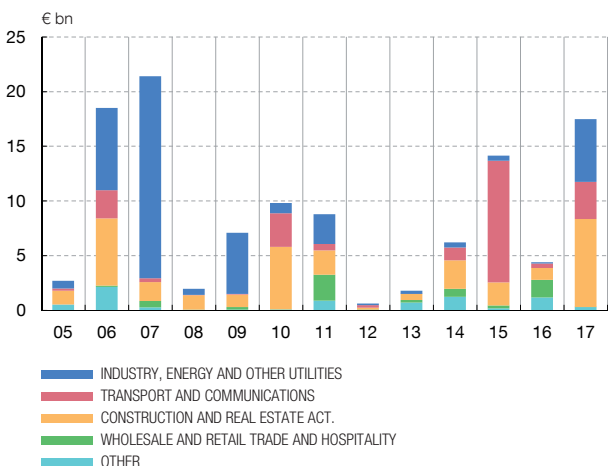
1 EQUITY ISSUES



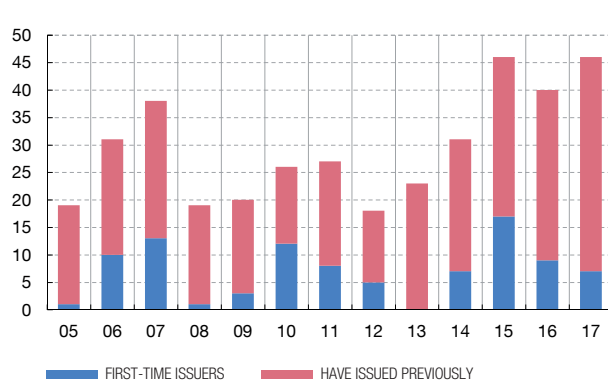
2 EQUITY ISSUES ON LISTED MARKETS, BY AGE OF ISSUER



3 EQUITY ISSUES ON LISTED MARKETS, BY SECTOR



4 NUMBER OF ISSUERS OF EQUITY ON LISTED MARKETS



SOURCE: Banco de España.

a Includes equity issues by unlisted non-financial corporations regardless of their legal form.



shares in listed markets is also seen in the breakdown by sector of activity. Traditionally the most active branch of activity has been industry, energy and other utilities, which accounted for 38% of total funds raised through the issuance of shares over the period 2005-2017 (see Chart 3.3). In recent years, however, there has been a significant increase in financing obtained by transport and communications firms, which in 2012-2017 was four times that in 2008-2012, and by the real estate and construction sector, which in 2017 accounted for 46% of the total volume issued.

The information on the number of issuers in listed markets also reflects an uneven pattern, with an average of approximately 30 issuers per year (see Chart 3.4). As with the bonds market, in the last few years new issuers have entered the market, although the proportion relative to the total is smaller.

The alternative markets

Spain, the same as other European countries, has recently created alternative stock markets, first for equities and then for fixed income, to provide more specialised fund-raising mechanisms for firms whose nature (highly innovative, recently created or simply small, such as SMEs) requires an environment different from that offered by the regulated markets where large companies usually raise funds.

The MAB is a multilateral trading facility set up in 2006 as an unofficial market to enable fund-raising through the issuance and trading of shares and units by firms in the growth stage which are not large enough to raise funds on a traditional stock market. The MAB has various segments: *empresas en expansión* (growth-stage firms),⁵ real estate investment trusts (REITs), open-end investment companies (SICAVs), funds, *entidades de capital riesgo* (venture capital entities, ECRs by their Spanish abbreviation) and *sociedades de inversión libre* (hedge funds, SILs by their Spanish abbreviation). This article analyses only the companies in the MAB segment of growth-stage firms because it is the only segment containing non-financial corporations, as the other segments consist of financial firms. The MARF is also a multilateral trading facility and was set up in 2013 to channel funds mainly to SMEs through fixed-income securities. The requirements for accessing this market are more flexible than those for the regulated official markets and this allows securities issues to be processed more rapidly at a lower cost. The securities traded are short term, such as commercial paper, and medium and long term, such as bonds, which may be either uncovered or asset-backed.

Regulatory changes have been made to support these initiatives. In the tax area, some regional governments and the Spanish state have introduced various incentives in the purchase of shares of newly created companies or of those listed on the alternative stock exchanges, provided that they meet certain requirements as to investment duration and firm size. In the commercial area, the MARF benefited from amendments to the legislation governing insurance companies and pension funds to allow them to purchase securities listed on these fixed-income markets.

Chart 4 illustrates how the activity of non-financial corporations on these alternative markets has trended upward in recent years. Thus the number of firms admitted to trading has grown continuously (see Charts 4.1 and 4.2), exceeding 40 issuers in both cases in 2017. In the MAB, the most active sectors since its inception have been, by number of issuers, the transport and communications sector and the industry, energy and other utilities sector (see Chart 4.3). In terms of the volume of funds raised (see Chart 4.5), these same sectors also lead the field, followed by the wholesale and retail trade and hospitality sector. As regards the MARF, issuances are concentrated in the industry, energy and other utilities sector and in construction and real estate activities, in terms of both the number of issuers and the volumes issued (see Charts 4.4 and 4.6).

Despite the growth shown by these two alternative markets, the volumes of funds raised in relative terms compared with the total equity and fixed-income markets are still very low. Thus in both the MAB and the MARF, the volumes reached in the past year are less than 1% of the total funds raised by non-financial corporations through securities (see Charts 4.7 and 4.8).

Venture capital

Venture capital is defined as that provided by financial investors which take temporary minority stakes in the equity capital of unlisted companies (although they may also take holdings in debt) and thus become shareholders, sharing directly in the risks and rewards of the business

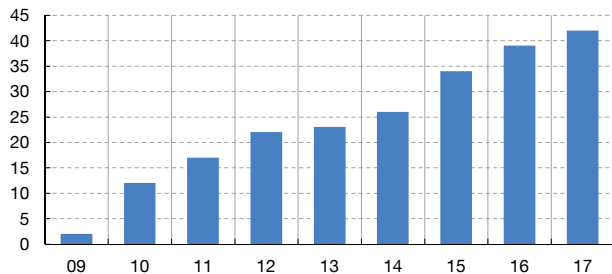
⁵ The growth segment of the MAB consists of small-cap non-financial corporations seeking to grow through the issuance of equity instruments.

THE ACTIVITY OF FIRMS ON THE ALTERNATIVE STOCK MARKETS HAS TRENDED UPWARDS IN RECENT YEARS

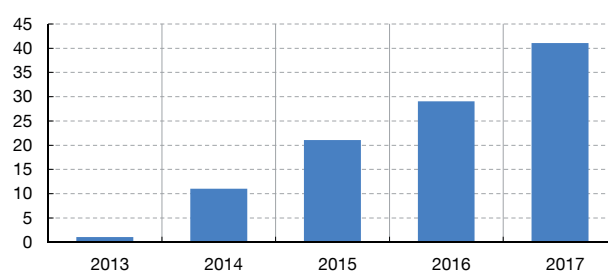
CHART 4

The number of firms admitted to trading on alternative stock markets has grown continuously. In the MAB, the most active sectors since its inception have been the transport and communications and the industry, energy and other utilities sectors. As regards the MARF, the industry, energy and other utilities and the construction and real estate activities sectors lead the field. Despite the growth shown by these alternative markets, the volumes of funds raised in comparison with the total equity and debt securities markets are still very low.

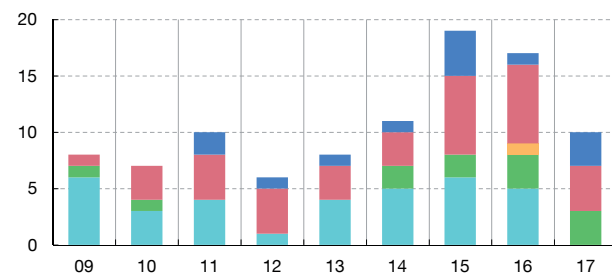
1 NUMBER OF FIRMS LISTED ON THE MAB



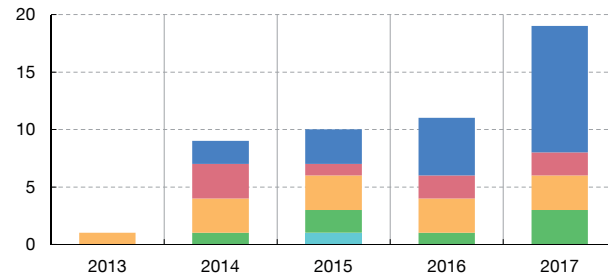
2 NUMBER OF FIRMS LISTED ON THE MARF



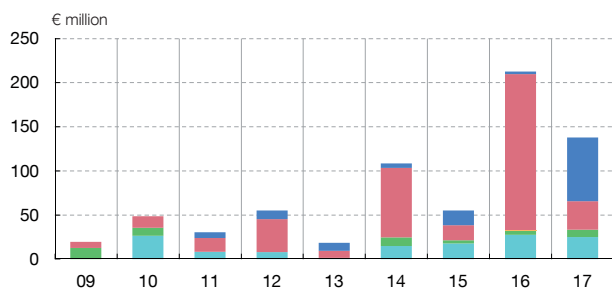
3 NUMBER OF ISSUERS IN THE MAB, BY SECTOR



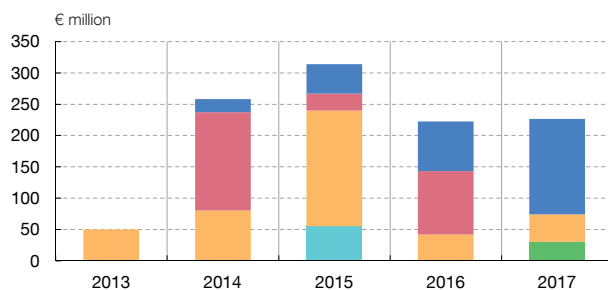
4 NUMBER OF ISSUERS IN THE MARF, BY SECTOR



5 VOLUME ISSUED IN THE MAB, BY SECTOR

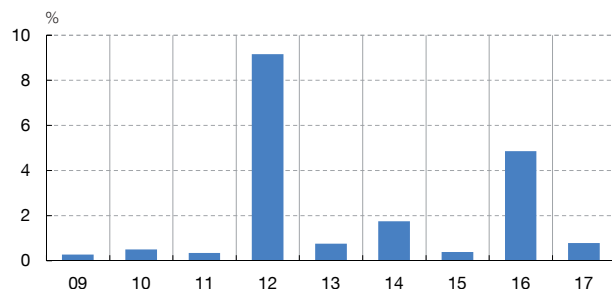


6 VOLUME ISSUED IN THE MARF, BY SECTOR. LONG TERM

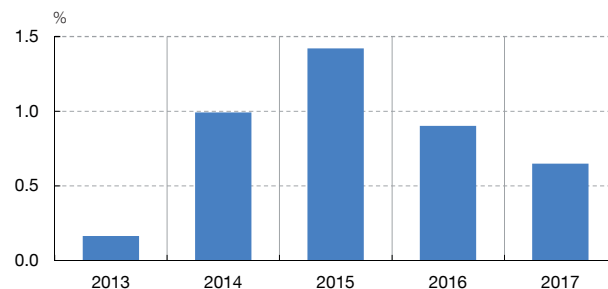


■ INDUSTRY, ENERGY AND OTHER UTILITIES ■ TRANSPORT AND COMMUNICATIONS ■ CONSTRUCTION AND REAL ESTATE ACT.
■ WHOLESALE AND RETAIL TRADE AND HOSPITALITY ■ OTHER

7 MAB ISSUES COMPARED WITH TOTAL EQUITY ISSUES IN LISTED MARKETS



8 MARF ISSUES COMPARED WITH TOTAL DEBT SECURITIES ISSUES IN LISTED MARKETS. LONG TERM



SOURCES: MARF, MAB and Banco de España.



project. Venture capital investors in the broad sense may be either specialised entities or individuals and diverse terms are used to refer to them (private equity, business angels, accelerators, venture capital funds, first shareholders) and they may use formal or other means of financing. In the case of Spain, a prior step to listing on official or alternative exchanges is often the raising of debt or equity through so-called venture capital entities (ECRs). ECRs are financial institutions regulated by the CNMV whose main purpose is to take temporary holdings in the capital (or debt) of companies other than real estate or financial firms which, at the time the stake is acquired, are not listed on the first market of stock exchanges or any other equivalent regulated market. The investment (in debt or equity securities) in a firm by an ECR represents for the investee not only the advantage of a source of alternative funding, but also, through the participation of skilled professionals on its governing bodies, an infusion of knowledge and experience potentially contributing to improved management efficiency. ECRs were first regulated in Spain in November 2005⁶ and recently regulatory changes have been made to foster their development. Specifically, the approval⁷ in November 2014 of SME venture capital entities (*ECR-Pyme* by the Spanish abbreviation) introduced more flexible legal formation requirements and changed the investment assets with respect to ordinary ECRs, particularly by allowing the greater use of participating loans and debt to provide financing to these SMEs and by permitting involvement in their management and in advisory tasks.

The statistical information analysed in this article is based on data from national and international venture capital associations which are broader⁸ than Spanish ECR statistics. Also, within venture capital, a number of investment types are usually distinguished according to the development stage of the firms or their projects. Thus, venture capital can be classified, within the initial stages, as follows: seed capital, which is investment in firms which have either just been created or have not yet begun their business activities and whose products or services are still in the process of definition; start-up capital is that provided to firms which already exist but need financing to commence operations (they have not yet begun production or distribution of the product or service and usually have not yet earned any profit). Late-stage capital, usually invested in firms already producing and selling and earning a profit, is intended to initiate strong growth, often with a view to a subsequent flotation. As regards the subsequent stages,⁹ investment is in firms undergoing growth or already firmly established and usually divided into the following types: growth-stage capital is invested in firms which already have a mature product and wish to increase their income and profits through geographical, product or customer expansion; leveraged capital, i.e. leveraged buy-out (LBO), management buy-out (MBO) and management buy-in (MBI), relates to investments aimed at acquiring a firm, for which a significant amount of borrowed funds (bonds or loans) is used; replacement capital is that used in transactions in which the investing company replaces one or more shareholders (who are uninterested in continuing with the investment); and turnaround capital is that used to change the strategy or management of the firm. These latter three types do not normally involve the provision of fresh funds to the firm.¹⁰

6 By means of Law 25/2005 of 24 November 2005 regulating venture capital entities and their management companies.

7 By Law 22/2014 of 12 November 2014 regulating venture capital entities and other closed-end collective investment undertakings and their management companies, and amending Law 35/2003 of 4 November 2003 on Collective Investment Institutions.

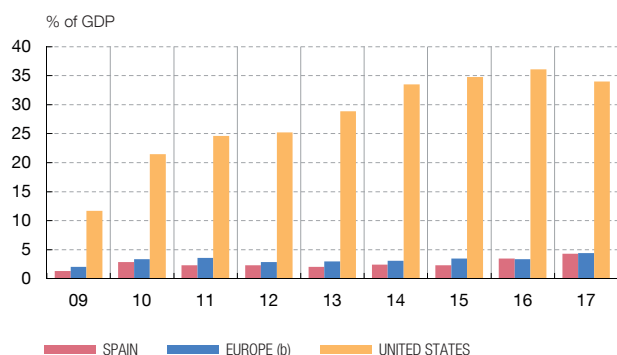
8 In this respect, the Spanish association Asociación Española de Capital, Crecimiento e Inversión (ASCRI) counts as venture capital both that of ECRs and so-called private equity (which encompasses private start-ups, equity funding rounds, and business angels' and accelerators' transactions).

9 These stages are also known in the literature as private equity.

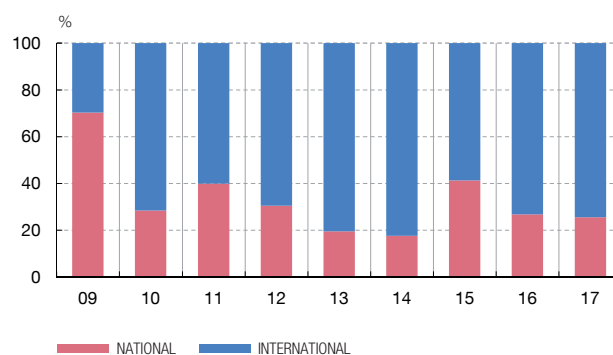
10 Growth-stage capital in the broad sense includes leveraged capital and that used to replace growth-stage capital. Investments effectively disbursed in shares and corporate bonds by ECRs through the primary market constitute new financing and are included under the financial transactions heading of the Financial Accounts as equity instruments and debt instruments, respectively.

In recent years, the volume of venture capital funding to Spanish firms has been similar to that of European firms (in GDP terms), but well below the venture capital figures in the United States. The bulk of funds provided to Spanish firms come from outside Spain, with most venture capital activity focused on the advanced stages of development. These transactions are concentrated in industry, energy and other utilities, followed by transport and communications, and wholesale and retail trade and hospitality.

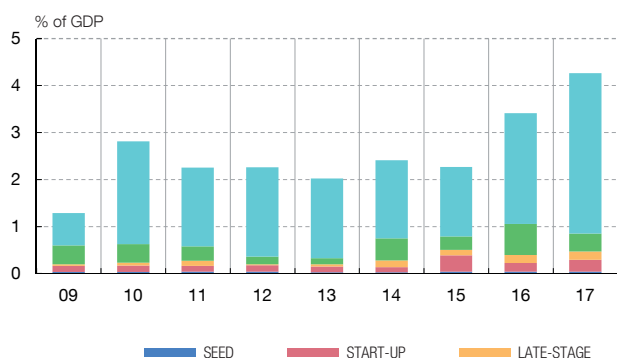
1 TOTAL INVESTMENT, BY COUNTRY OF DESTINATION



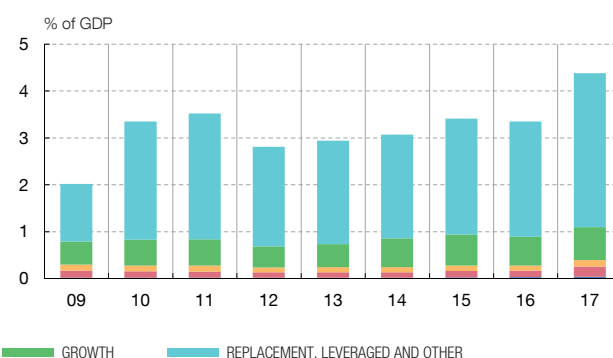
2 INVESTMENT IN SPANISH FIRMS, BY COUNTRY OF ORIGIN OF CAPITAL



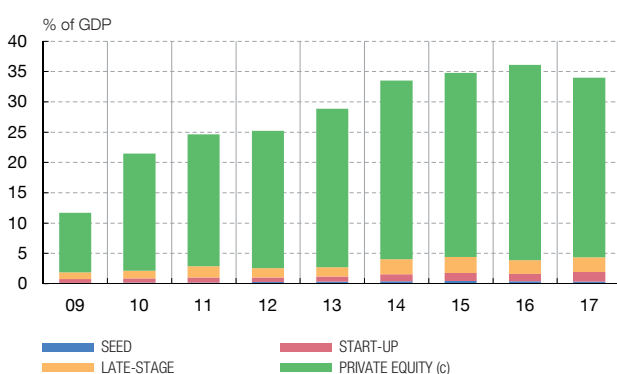
3 INVESTMENT IN SPANISH FIRMS, BY DEVELOPMENT STAGE (b)



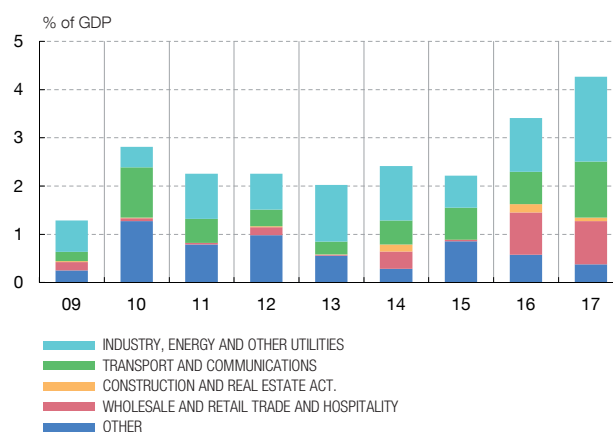
4 INVESTMENT IN EUROPEAN FIRMS, BY DEVELOPMENT STAGE (b)



5 INVESTMENT IN US FIRMS, BY DEVELOPMENT STAGE (b)



6 INVESTMENT IN SPANISH FIRMS, BY SECTOR



SOURCES: ASCRI, Invest Europe and National Venture Capital Association.

- a Due to a methodological change, the variable "investment" now refers to investment in domestic firms by national and international private management companies, and does not include investment of domestic private management companies abroad.
- b Includes Austria, Baltic states (Estonia, Latvia and Lithuania), Belgium, Bulgaria, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Luxembourg, Netherlands, Norway, Bosnia-Herzegovina, Croatia, Macedonia, Montenegro, Serbia, Slovenia, Slovakia, Poland, Portugal, Romania, Spain, Sweden, Ukraine and the United Kingdom.
- c No data available on the breakdown of private equity investment for the United States.



Chart 5 illustrates the recent development of venture capital received by Spanish firms and compares it with that received by European and US firms. Chart 5.1 shows that, according to Invest Europe statistics,¹¹ the volume of venture capital funding to Spanish firms (2.6‰ of GDP in 2017) in recent years is similar to that received by European firms on average (3.2‰ of GDP), but well below the venture capital figures in the United States (2.8% of GDP). Chart 5.2 shows how the bulk of funds provided to Spanish firms comes from outside Spain. Although in the last three years activity has risen in the initial phases (seed, start-up and late-stage capital), most venture capital activity is concentrated in the subsequent stages, both in Spain and in the rest of Europe and the United States, particularly through leveraged transactions (LBO, MBO and others, see Charts 5.3 to 5.5). By economic sector, Chart 5.6 shows that these transactions were concentrated in industry, energy and other utilities,

Crowdfunding platforms

Crowdfunding platforms (CFPs), regulated in Spain in April 2015, are a mechanism for directly channelling savings to productive investment which supplements that of stock markets and alternative markets. In particular, a distinction is made between equity crowdfunding, in which fund-raising is channelled through equity, and crowdlending, in which the instrument used is debt. At the end of 2017 the CNMV had authorised 26 CFPs, of which eleven were through shares, ten through loans and five were combined share-loan projects. Official statistics are not yet available on their activity because they are still at an early stage of development. However, initial estimates indicate that funds channelled through this mechanism in the form of shares or debt, although marginal compared with total financing, are growing rapidly. Thus, it is estimated¹² that, on average, in the last three years the total funds raised by these platforms worldwide have grown by more than 40% annually, exceeding €9.4 billion in total in the period January-June 2018. Noteworthy by geographical area is the high share of China, which in this period accounted for 80% of the world's volume of crowdfunding, followed by the United States with 11% and, at a considerable distance, the United Kingdom (2%), Japan (1%), France (1%) and Spain (0.2%).

15.11.2018.

¹¹ The venture capital and private equity platform Invest Europe includes Austria, the Baltic states (Estonia, Latvia, Lithuania), Belgium, Bulgaria, the Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Luxembourg, the Netherlands, Norway, Bosnia-Herzegovina, Croatia, Macedonia, Montenegro, Serbia, Slovenia, Slovakia, Poland, Portugal, Romania, Spain, Sweden, the Ukraine and the United Kingdom.

¹² Statista. <https://www.statista.com/outlook/335/100/crowdfunding/worldwide>