Executive summary

This report presents indicators and analysis of capital structures, corporate performance, the use of market-based financing, corporate ownership structures and payout policies over the last two decades. It reviews regulatory and financial support measures related to the COVID-19 crisis in the areas of corporate governance and corporate finance. It then presents key indicators relating to the non-financial corporate sector's use of public equity and corporate bond markets during 2020, and reviews central bank policies related to the corporate bond markets. Using an analysis of structural weaknesses in both the public equity and corporate bond markets worldwide, the report focuses on the role that capital markets can play on the road to recovery and resilience. It also identifies key corporate governance policy issues that may require further attention in the post-crisis era.

Supporting the recovery. Stock markets play a key role in providing companies with the equity capital that gives them the financial resilience to overcome temporary downturns, while meeting their obligations to employees, creditors and suppliers. In 2020, already-listed non-financial companies raised a record of USD 626 billion in new equity. Since 2005, however, more than 30 000 companies have delisted from stock markets globally - equivalent to 75% of all listed companies today. These delistings have not been matched with new listings, resulting in a net loss of listed companies. This means that several thousand fewer companies today are able to tap public equity markets directly and at a relatively low cost. Many advanced markets have also experienced a structural decline in listings of smaller growth companies, distancing a larger portion of these companies from ready access to public equity financing.

These trends have raised concerns about structural weaknesses in the stock market ecosystem. First, the shift from retail direct investments to large institutional investors has created a bias towards large listed companies, as the average share of institutional ownership in large listed companies is significantly higher than their ownership in smaller companies. Second, the structure of investment banking activity is an important factor behind high listing costs, as high underwriting fees and stock price discounts have discouraged companies from going public. The systematic acquisition of smaller growth companies - especially by large technology companies - may also contribute to the drying up of the IPO pipeline of smaller independent companies that could potentially increase competition and challenge the status quo.

Corporate governance frameworks. With the COVID-19 crisis preventing many companies from meeting certain legal and regulatory obligations, governments around the world have taken steps to adjust these requirements. Although some of these adjustments are considered temporary, they may also have a lasting impact on how companies are governed, their capital structure, their ownership structure and how they manage their relationship with shareholders and stakeholders. This gives new impetus to the discussions on a number of long-term developments that may call for an adaptation of corporate governance policies and regulations in the post-COVID-19 era.

Experiences from the pandemic call for improvements in the frameworks for risk and crisis management as well as related issues such as audit quality, stock price manipulation and insider trading. Countries should also benefit from their experiences in order to advance or clarify the regulatory frameworks for remote participation in shareholder meetings. Recent practices by some companies related to altering the

terms for executive remuneration following the crisis also call for renewed scrutiny of the conditions and procedures for deciding and overseeing performance-related pay.

Importantly, there has been an increase in **ownership concentration** at the company level in global stock markets. Institutional investors have considerably increased their assets under management over the last 15 years while the number of listed companies in many advanced equity markets has decreased. These opposing trends have resulted in a growing amount of money being allocated to a diminishing number of companies and the resulting re-concentration of ownership in the hands of large institutional investors. For example, the three largest institutional investors in the United States now hold a combined average of 23.5% of the equity in listed companies.

The concentration of ownership in some other markets reflects the importance of company group structures. For example, private corporations and holding companies in several Asian economies hold more than 30% of the total equity capital in publicly listed companies. The increase in ownership concentration can also be attributed to the presence of public sector ownership. Globally, the public sector, including central governments and sovereign wealth funds, owns USD 10.7 trillion of listed equity, which amounts to 10% of global market capitalisation.

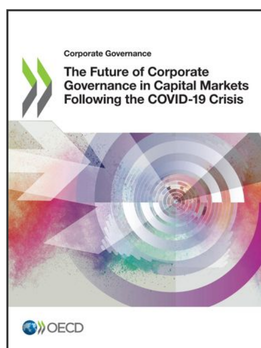
Environmental, social and governance risks. Accelerated by the COVID-19 pandemic, many investors are paying greater attention to ESG considerations when making their investment and voting decisions. Policy makers and regulators need to ensure that investors have access to consistent, comparable, and reliable material information, notably climate-related information, when managing their savings and assets. This would also help the corporate sector to meet increased expectations when it comes to recognising and appropriately balancing the interests of all stakeholders and their contribution to the long-term success of corporations.

The non-financial corporate sector. Not all firms have been equally affected by the COVID-19 crisis. This is partly related to differences in financial soundness going into the crisis, with high leverage levels making some companies more vulnerable. In the aftermath of the 2008 financial crisis, global corporate bond markets saw a significant and lasting increase in issuances, doubling from a yearly average of USD 890 billion between 2000-2007 to USD 1.87 trillion between 2008-2020. The COVID-19 outbreak accentuated this trend and 2020 recorded a historical peak of USD 2.9 trillion in issuances by non-financial companies, resulting in an all-time high of USD 14.8 trillion in outstanding non-financial corporate bonds.

Even before the COVID-19 crisis hit, however, the declining quality of the outstanding stock of corporate bonds and the increase in borrowing by companies with lower quality credit ratings were raising widespread concerns about excessive risk-taking in some parts of the corporate sector. One example has been the use of corporate bond markets to finance share buyback operations by high-risk non-investment grade companies. Since 2000, the share of corporate bond offering documents that explicitly mention share buybacks or dividends among the intended uses has increased from 2% to 11%.

Rapid developments in the corporate bond market have revealed some **structural challenges**. The share of newcomers to the corporate bond market has given way to recurring active issuers. The share of first-time issuers in 2020 amounted to only 27%, with their share of total issuance at an all time low of 12%. This, along with evidence from the 2008 financial crisis, underlines that an established relationship with the corporate bond market provides an advantage for attracting new capital immediately following a crisis.

With respect to risk transparency, the significant increase of BBB rated bonds - the lowest investment grade rating - before the COVID-19 outbreak was actually coupled with a declining number of downgrades relative to upgrades. This, together with the fact that the 1-notch downgrade probability is lowest for bonds just above non-investment grade status, may suggest that credit rating agencies are mindful of downgrading BBB issuers due to their special status just above the non-investment grade threshold. Such rating stability concerns may limit the ability of credit ratings to properly inform investors about the risks of individual bonds.



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