

Europe's 19,3 Trillion Capital Shortfall



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Summary

- Europe is falling behind, despite efforts by the European Commission and various European countries to better allocate savings towards financing productive investment. However, without structural reforms, it will be impossible to recover lost ground.
- Although the scale of Europe's decline is widely acknowledged, and the importance of savings is frequently emphasised, the long-term savings gap is frequently underestimated.
- Europe suffers from two major deficits: underdeveloped retirement savings and low stock market capitalisation, amounting to €19,700 billion and €19,300 billion, respectively, in 2023.
- While unifying markets is desirable, and financial and insurance regulations should be made more flexible to encourage investment equity, these approaches alone cannot compensate for the significant decline in European long-term capital.
- Only the widespread introduction of pension funds in European countries where they are currently lacking will significantly enhance economic financing, improve pension value for money, and help reduce public deficits.

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Introduction: Is Europe's long-term savings deficit limited to €300 billion annually?

Can Europe catch up with the action plans introduced by the European Commission and various national governments, which aim to better reallocate savings towards financing productive investments?

That remains uncertain. Without structural reforms, recovering lost ground may prove impossible. Although the extent of Europe's decline is undisputed, and the importance of savings is frequently discussed, there is a real risk that the European response will fall far short of what is needed – primarily due to a misjudgement of the true scale of the long-term savings gap.

According to Enrico Letta, former prime minister of Italy, €300 billion of European savings are diverted abroad each year, mainly to the US. That is money that could have otherwise supported the development of companies within the EU. The reason for this diversion of funds, Letta argues, is the fragmentation of Europe's capital markets and financial system (Letta 2024). In just a few months, this number – €300 billion – has become central to discussions among central bankers and EU representatives.

Given Europe's economic challenges, this claim of an annual €300 billion in transfers to the US – echoed by several European leaders – may be significantly underestimated, even anecdotal.

For example, the Draghi report estimates that additional investment needs in the EU will exceed €750 billion per year between 2025 and 2030 (Draghi 2024), including €450 billion for the energy transition¹ and nearly €300 billion annually to close the digital and productivity gaps. The EU's rearmament requirements are estimated to come to €800 billion over several years.² In addition, there are national projects, such as the revival of the French nuclear industry, estimated at €80 billion (Sapy 2025), and the modernisation of German infrastructure, estimated at €500 billion (Grasland 2025).

In the EU Compass to Regain Competitiveness and Secure Sustainable Prosperity, the European Commission highlights the importance of finding ways to better finance competitiveness (European Commission 2025b). It emphasises in the press release that 'the EU lacks an efficient capital market that turns savings into investments' (European Commission 2025b). To address this, it plans to introduce a 'European Savings and Investments Union to create new savings and investment products, provide incentives for risk capital, and ensure investments flow seamlessly across the EU'. According to the Commission, a financial union could unlock an additional €470 billion in private investment annually.³

However, this approach is likely to fall short of what is needed, as it underestimates the challenges involved. As this briefing demonstrates, the actual long-term savings gap is unrelated to the figures commonly cited.

¹ This is potentially an underestimate. The additional financing required to achieve carbon neutrality in Europe is estimated at between €410 billion and €620 billion, according to 'Quel financement de la

Insufficient funding for innovation in Europe

The lack of European leadership in innovative technologies has become a defining characteristic of the continent's economic and industrial landscape. As noted by Fuest et al.⁴, Europe's industry appears to be caught in a middle-technology trap, exhibiting a significant divergence from that of the US.

While both continents were still heavily invested in the automotive industry in 2003, their paths have since diverged. The technology sector dominates research and development (R&D) in the US, while Europe continues to rely on the automotive industry. Twenty-five years later, the automotive sector still accounts for the lion's share of R&D in Germany, whereas in the US, the automotive and pharmaceutical sectors have been largely supplanted by the industries of the new industrial revolution, namely information and communication technologies.

Europe remains focused on traditional sectors, which are undergoing a significant technological transformation; however, European industry is failing to take the lead. As a whole, the continent is struggling to drive innovation in sectors with the highest potential for added value.

At the macroeconomic level, investment remains insufficient to meet productivity and growth challenges. European R&D business investments account for just 1.2 per cent of the GDP – significantly lower than in the US, where R&D represented 2.4 per cent of the GDP in 2021. This means Europe invests 50 per cent less in R&D as a share of GDP.

Several factors explain this overall lack of investment. Many analysts point to market fragmentation, limited venture capital, and inadequate support for innovation as key obstacles to European business creation and growth. This view is echoed by the European Commission, which notes that 'European start-ups have a hard time expanding within the Single Market because of persisting regulatory barriers' (European Commission 2025a, p.4). It also highlights that 'they also have less access to venture capital and other forms of risk capital than their US peers: the share of global venture capital funds raised in the EU is only 5%, compared to 52% in the US and 40% in China'.

Transition : bâtir les ponts entre les besoins et les ressources,' At the Les Rencontres de l'Institut de la Finance Durable, 22 April 2024 (<https://www.banque-france.fr/fr/interventions-gouverneur/quel-financement-de-la-transition-batir-les-ponts-entre-les-besoins-et-les-ressources>).

² 'Guerre en Ukraine : l'Europe dévoile un plan à 800 milliards pour muscler sa défense', Les Echos, 4 March 2025 (<https://www.lesechos.fr/monde/europe/guerre-en-ukraine-leurope-devoile-un-plan-a-800-milliards-pour-muscler-sa-defense-2151893>).

³ 'Lagarde blames European "laziness" for holding the continent back', Euractiv, 23 January 2025 (<https://www.euractiv.com/section/economy-jobs/news/lagarde-blames-european-laziness-for-holding-the-continent-back/>).

⁴ 'Reforming innovation policy to help the EU escape the middle-technology trap', VoxEU CEPR, 19 April 2024 (<https://cepr.org/voxeu/columns/reforming-innovation-policy-help-eu-escape-middle-technology-trap>).

Europe's Shortfall in Long-Term Capital for Global Competitiveness

The North American model – which features a comprehensive ecosystem for financing innovation, from venture capital to the stock market, which is supported by long-term investors such as pension funds at every stage of development – is largely absent in Europe. Many European countries, devastated by the two world wars, did not rebuild their pension capital, which had been eroded by inflation or confiscated during wartime. To this day, they rely almost exclusively on pay-as-you-go pension systems.

In the post-war years, characterised by state-led reconstruction efforts such as the Marshall Plan, rebuilding retirement savings was not a priority. In Italy, France, and Germany, SMEs and mid-cap companies managed to recover by funding their incremental growth through self-financing, bank loans, or investments from insurers. However, these traditional financing methods are ill-suited to supporting disruptive innovation – particularly as the lending capacity of banks and the investment capacity of insurers have been significantly constrained by prudential regulations (e.g., Basel and Solvency), thereby reinforcing the critical role of pension funds.

This contributes to delays in innovative sectors, increased European dependence on technologies developed in the US and in Asia, and thus even a loss of sovereignty. The remarkable dynamism of American digital and tech companies stands in stark contrast to the struggles of their European counterparts, as noted by Andrew McAfee⁵ (Figure 1).

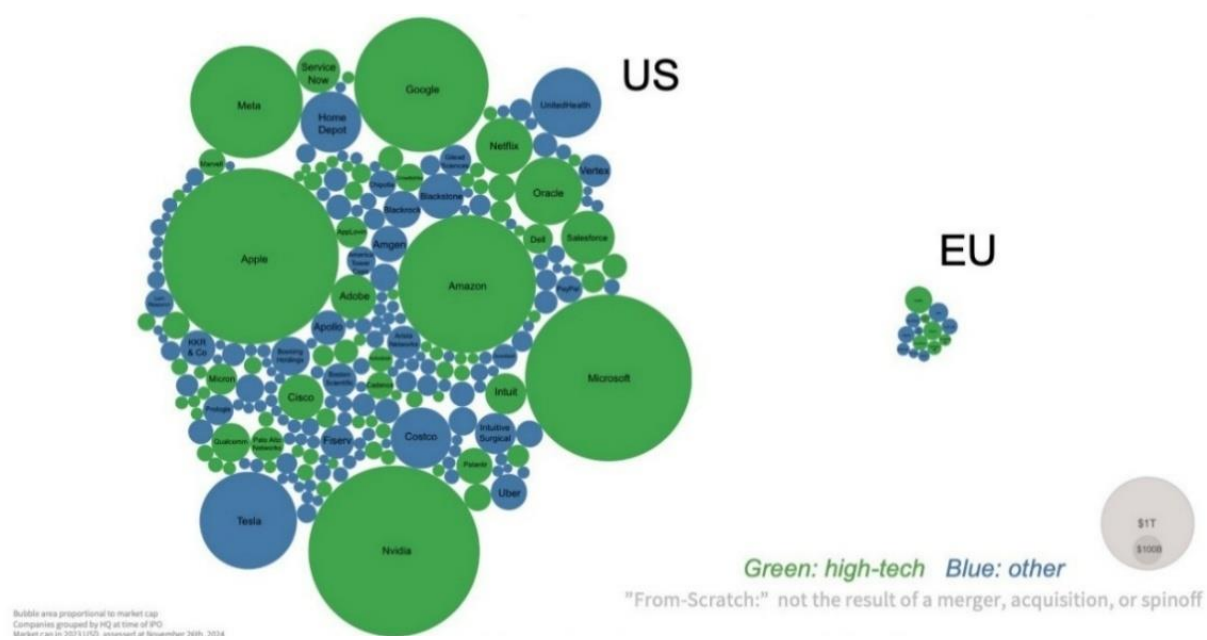
For every young tech leader in Europe, there are 17 in the US. At the end of 2023, European stock exchanges listed only 14 companies under 50 years old with a market capitalisation of \$10 billion or more, compared to 241 in the US. The combined market value of these European firms was just \$434 billion, whereas their American counterparts were worth \$29,566 billion – 68 times more.

This disparity is partly due to the abundance of retirement savings in the US – largely invested in equities – which help fuel innovation through markets such as the Nasdaq (Figure 2).

In a world where equity capital drives disruptive innovations, the low market capitalisation of European companies means that they are falling behind in the race to innovate – and, as a result, are losing out economically.

⁵ 'A visualization of Europe's non-bubbly economy', The Geek Way (blog), 2 December 2, 2024 (<https://geekway.substack.com/p/a-visualization-of-europes-non-bubbly>).

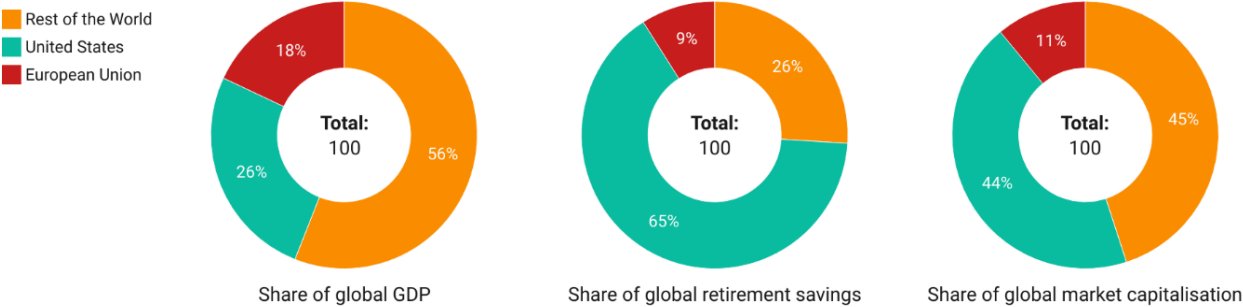
Figure 1: Public From-Scratch US and EU companies less than 50 years old, with a market capitalisation of \$10 billion or more



Source: McAfee (2024); bubble size proportional to market capitalisation. Market capitalisation in 2023 USD, assessed as of 26 November 2024.

Figure 2: The US leads in retirement savings and market capitalisation (2023)

While the US accounts for 26% of global GDP, it represents 65% of retirement savings and 44% of global market capitalisation, enabling it to finance disruptive innovations and remain at the forefront of global innovation.



Source: Calculations by the Institut économiue Molinari, based on data from the World Bank, OECD, and World Federation of Exchanges (WFE).

Europe lags by €19.3 trillion in stock market capitalisation

Despite efforts by some stock exchanges to enhance their attractiveness, European market capitalisation has grown more slowly over the past ten years. The EU has been overtaken by the US and is also losing ground compared to equity markets in the rest of the world – crucial instruments for financing innovation.

At the end of 2023, the market capitalisation of EU companies stood at 65 per cent of the GDP, compared with 177 per cent in the US. This 112-percentage-point gap corresponds to a shortfall of €19.3 trillion in European market capitalisation (Figure 3).

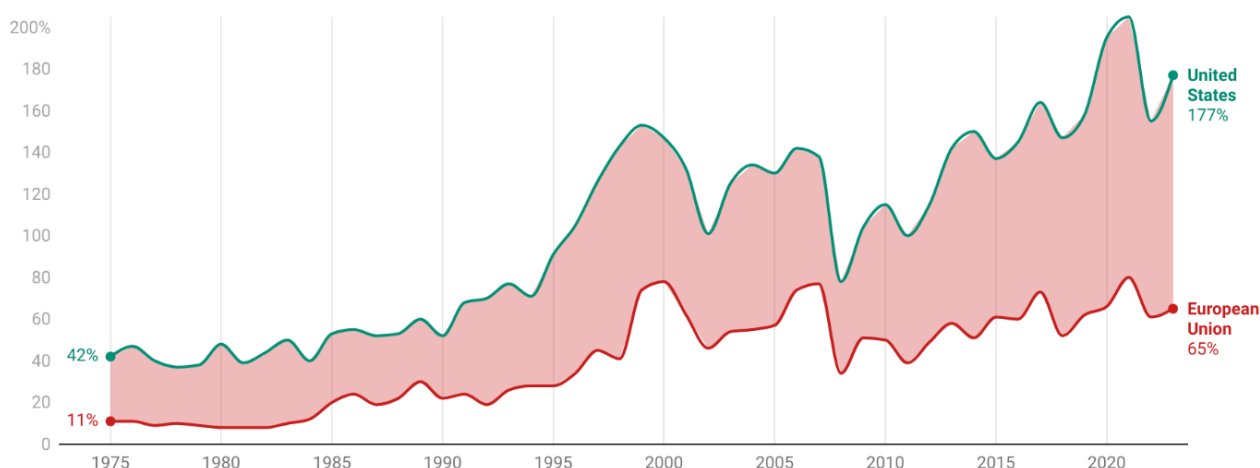
The digital dependence index (DDI) of Germany, France, the UK, and Italy on the US for infrastructure and platforms stands at 0.98 (where 1.0 indicates total dependence), reflecting an almost complete reliance on US technology. According to Mayer and Lu (2023), ‘European countries are falling behind in every dimension compared to China, South Korea, and the US. In the last decade, Europe’s digital autonomy has eroded as digital interactions have become more asymmetric with China (ICT trade dependence), with the US (infrastructure and platform dependence), and the East Asian region (IP dependence).’

At the end of 2024, the total market capitalisation of EU stock exchanges stood at €9.7 trillion – roughly one-sixth the size of US stock exchanges, which reached €62.2 trillion for the NYSE and Nasdaq combined. The EU’s largest stock exchange, Euronext, was just one-fifth the size of the NYSE (traditional US stocks).

This is not a matter of competence – either on the part of European companies or stock exchanges – as the necessary tools and expertise are in place. Rather, it reflects the scarcity of long-term savings in Europe, stemming from the limited emphasis on capitalisation-based pension systems in many continental countries.

Figure 3: Europe lags behind in market capitalisation (as a percentage of GDP, 1975–2023)

In the EU, market capitalisation represented 65% of GDP in 2023, i.e., a deficit of 112% of GDP when compared with the US where it was equivalent to 177% of GDP.



Source: Calculations of the Institut Economique Molinari based on data from the World Bank, FESE (EU 2018–2023) and WFE (US 2023) • Créé avec Datawrapper

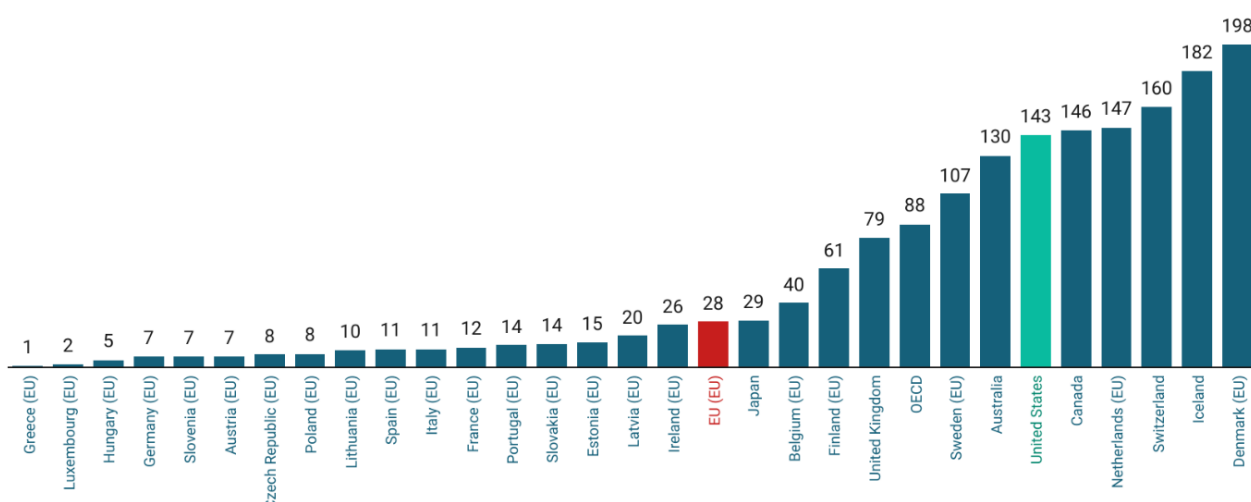
Source: Institut Economique Molinari calculations based on data from the World Bank, FESE (EU 2018–2023), and WFE (US 2023).

Europe faces €19.7 trillion retirement funding gap. Except for Scandinavia and the Netherlands, the EU is an economic area where pension capital remains underdeveloped. In much of the world, a significant share of pension benefits is financed through collective or individual capitalisation, with the capital being partly invested in the local economy. The EU, however, benefits far less from this source of funding.

The major European countries – Germany, France, Italy, and Spain – have low levels of retirement savings, amounting to just 7 per cent to 12 per cent of their GDPs. In contrast, the United Kingdom, Switzerland, and Iceland – none of which are part of the EU – have retirement savings ranging from 79 per cent to 182 per cent of their GDPs. Within the EU, only Sweden, the Netherlands, and Denmark exceed the OECD average, with retirement savings representing between 107 per cent and 198 per cent of their GDPs at the end of 2023 (Figure 4).

Compared to the US, the EU was lagging behind by €19.7 trillion in retirement savings at the end of 2023. In Europe, retirement savings accounted for 28 per cent of the GDP, versus an average of 143 per cent in the US – a gap of nearly 115 per cent of GDP (Figure 5).

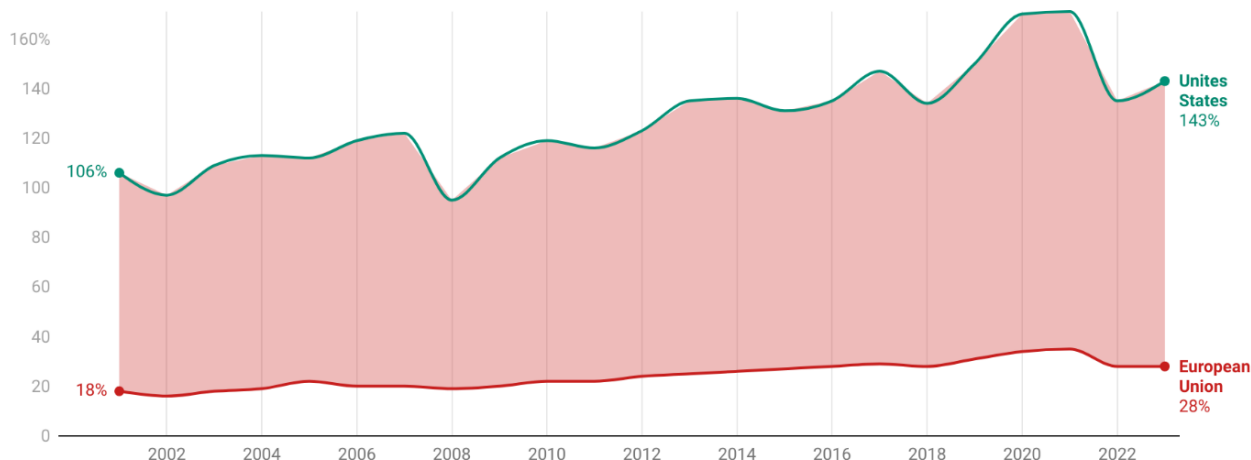
Figure 4: Retirement savings as a percentage of GDP (2023)



Source: Institut économique Molinari, based on OECD data.

Figure 5: Europe is falling behind in terms of retirement savings (% of GDP, 2001–2023)

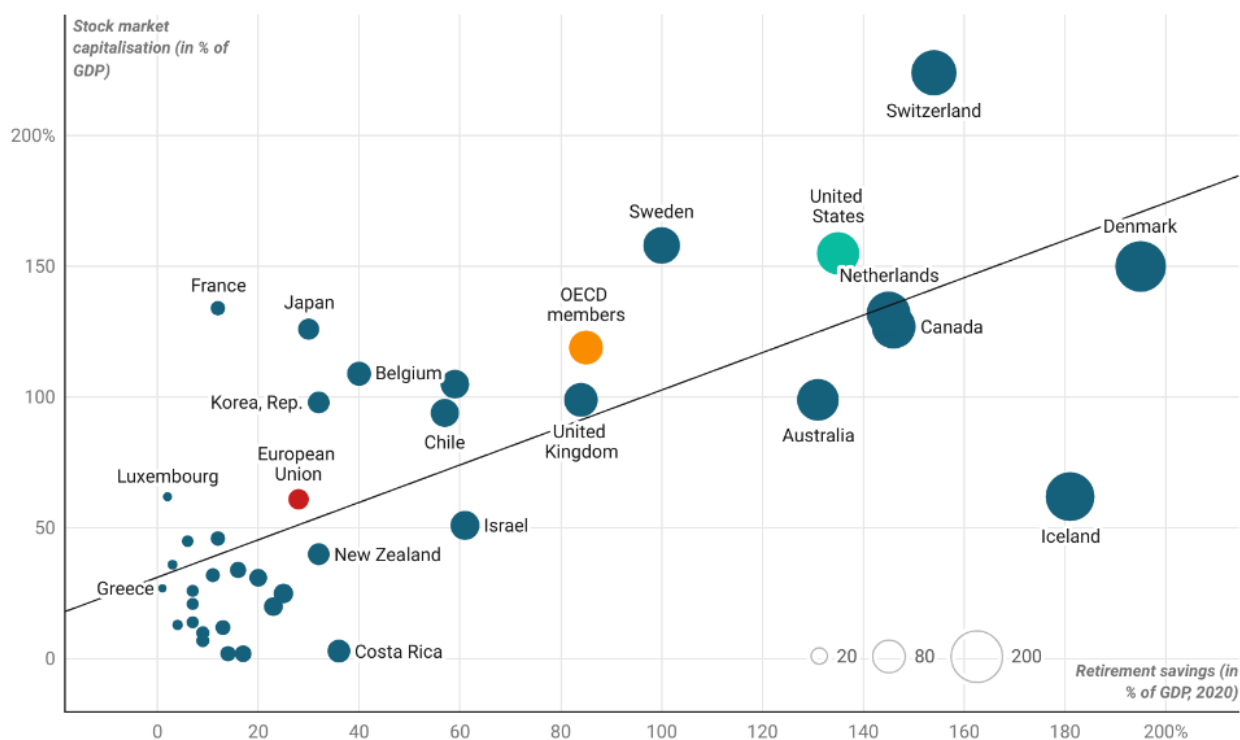
In the EU, retirement funding represented 28% of GDP in 2023, i.e., a deficit of 115% of GDP when compared with the US, where retirement funding was equivalent to 143% of GDP.



Source: Calculations of the Institut Economique Molinari based on data from the OECD • Created with Datawrapper

Source: Institut Economique Molinari calculations based on OECD data.

Figure 6: Growth in retirement savings and stock market capitalisation go hand in hand (per cent of GDP at the end of 2022)



Source: Institut Economique Molinari calculations based on data from the World Bank, CEIC, and OECD; $R^2 = 0.52$.

Conclusion: The only solution is the widespread use of pension funds

For all these reasons, the notion that Europe already possesses a large stock of savings and simply needs to reallocate it is an illusion. Europe faces significant twin deficits – stemming from the underdevelopment of retirement savings and stock market capitalisations – amounting to €19,700 billion and €19,300 billion, respectively, in 2023.

While unifying markets and making financial and insurance regulations more flexible to encourage investment are desirable steps, they are insufficient to compensate for how far Europe has fallen behind in terms of long-term capital.

Only the widespread introduction of pension funds in all European countries where they are currently absent will significantly improve economic financing, improve pension value for money, and help reduce public deficits (Marques 2023b).

France and the European Commission aim to reallocate existing savings, but this is insufficient to bridge the gap between Europe and the US. A significant share of household wealth is held in property or very short-term investments. Even life insurance does not compensate for the absence of pension funds in Europe, as it remains accessible at any time and therefore cannot be invested in equities to the same extent as long-term retirement savings.

For Europe to catch up, the most effective solution would be the widespread adoption of pension funds – both in the private sector and to finance civil servant pensions in the public sector. Accordingly, the Compass for the EU would benefit from being supplemented by two measures: first, the creation of sovereign funds to provide for government employee pensions in countries where these are managed separately from private-sector schemes; and second, an increase in the share of funded pensions in the private sector (Marques 2023a).

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