Lucas Papademos: Presentation of indicators of financial integration in the euro area

Opening remarks by Mr Lucas Papademos, Vice President of the European Central Bank, to the press briefing, Frankfurt am Main, 30 September 2005.

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Ladies and Gentlemen,

Welcome to the European Central Bank and thank you for attending this press briefing on "Indicators of financial integration in the euro area". We will start with some introductory remarks from my side. My colleague on the ECB's Executive Board Ms Gertrude Tumpel-Gugerell will then present the indicators of financial integration in more detail. With us on the podium are the Director General Statistics, Mr Steven Keuning, and the Deputy Director General Economics, Mr Philippe Moutot. All of us will be available to answer any questions that you might have regarding this publication.

The publication of the indicators for financial integration in the euro area is a first for the ECB. For this reason, and also in order to underscore the importance which the ECB attaches to European financial integration and to highlight the particular informative value of these indicators, we considered it appropriate to mark the publication of this report by inviting you to this event.

Let me begin by addressing some fundamental questions which might be asked in this context: Why did the ECB decide to produce such a set of indicators? What is the purpose of this publication? The ECB seeks to foster further integration in European financial markets in various ways and through a number of initiatives for the following reasons.

First, financial integration is important for the smooth and effective implementation of the single monetary policy. It also facilitates and speeds up the transmission of the effects of monetary policy on the euro area economy. Moreover, a financial system with well-developed capital markets, being intrinsically forward-looking, can provide us with useful and timely information about future economic developments.

Second, financial integration has implications for financial stability. As you are certainly aware, the Treaty (Article 105(5)) calls upon the Eurosystem to contribute "to the smooth conduct of policies pursued by the competent authorities relating to the prudential supervision of credit institutions and the stability of the financial system". To this end, an understanding of the links between financial integration and financial stability, and, in particular, of the implications of financial integration for financial stability is essential. On the one hand, deeper and more integrated financial markets offer better opportunities for financing and risk diversification, and thus also help to improve the capacity of the economies to absorb shocks. On the other hand, intensified cross-border financial links also harbour the potential that shocks could be transmitted more rapidly through the euro area. A potentially increased risk of financial contagion alters the challenges to financial stability that we are facing. Against this background, the monitoring of progress towards more fully integrated markets – as we are seeking to do with this new set of indicators – is useful for our assessment of the outlook for financial stability.

Finally, and more generally, financial integration can help to promote the development and modernisation of financial markets, institutions and infrastructures, thereby helping, through various channels, to support economic activity and raise the potential for economic growth. Deeper and wider markets encourage savings, offer more and better investment opportunities, reduce the cost of capital and intermediation, and facilitate a more efficient allocation of financial resources. In this way, they contribute to higher growth. It is for this reason that the objective of fostering financial integration in the European Union is a key aspect of the Lisbon agenda. In fact, financial integration has arguably been one of the most successful components of the Lisbon strategy and further progress towards more integrated financial markets is undoubtedly desirable.

The ECB has taken a proactive stance towards, and has been involved in several initiatives aimed at fostering, financial integration, given its importance not only for the performance of the basic tasks of the Eurosystem but also for the welfare of European citizens. It goes without saying that we are also in close cooperation with the European Commission in our efforts to promote financial integration. The pertinent initiatives of both institutions support and complement each other. Regarding the specific fields of activity and expertise of the ECB and the Eurosystem, we distinguish between four kinds of contribution.

First, public authorities can make a contribution by fostering collective action to overcome possible coordination problems in the private sector. Right from the start of Monetary Union, the ECB has sought to play this “catalyst role”. The most recent example in this respect is our support of the initiative for a Single Euro Payments Area.

Second, we provide central banking services that are conducive to financial integration, most prominently by operating Europe’s leading large-value cross-border payment system, TARGET.

Third, we offer advice on the legal and regulatory frameworks for the financial system. For example, the Eurosystem recently commented on the review of the Lamfalussy process[1] and on the European Commission’s priorities for financial services policy over the next five years.[2]

Finally, the ECB also seeks to provide economic analysis and research on financial integration, in order to raise the awareness of economic agents and policy-makers about the benefits of financial integration for the euro area economy. The ECB is in a unique position to produce in-depth economic analysis and comprehensive statistics for the euro area as a whole, by drawing on the expertise of its staff, by relying on direct interaction with major financial players and by building on its role as a supranational institution at the helm of the Eurosystem.

The publication we are presenting today belongs to this fourth type of initiative. In discussions on European financial integration, the relevant arguments are often of a qualitative nature. However, in order to properly monitor and assess the state of financial integration, quantitative information in the form of indicators – as contained in our report – is not only useful, but essential. We wanted to devise a way in which to capture, in quantitative terms, the various dimensions of financial integration and to have a toolbox at our disposal to monitor developments, measure progress and assess the state of integration of the different components of the European financial system, that is, financial markets, financial institutions and financial infrastructures.

The indicators that we have compiled focus on markets and cover the main financial market segments of the euro area, ranging from the money market to retail loans and wholesale equity trading. The statistics indicate that the degree of integration varies greatly depending on the market segment. The unsecured money market has been fully integrated since shortly after the introduction of the euro. The repo market is also highly integrated, albeit to a lesser extent. Government bond markets have integrated significantly. The indicators for the corporate bond market, which has grown considerably since the introduction of the single currency, also point to a high degree of integration. Progress has also been made in the

[1] See http://www.ecb.int/pub/pdf/other/lamfalussy-reviewen.pdf.

[2] See http://www.ecb.int/pub/pdf/other/ecgreenpaperfinancialservicespolicy2005en.pdf.

integration of euro area equity markets, in which equity returns are increasingly determined by common factors. However, banking markets are generally much less integrated.

These general findings – and I only wanted to refer to them very briefly – already demonstrate that the indicators contained in the report will contribute to enriching the discussion on the progress of financial integration with tangible evidence. I would now like to give the floor to Ms Tumpel-Gugerell, who will present in greater detail these new indicators and the report.

Thank you very much for your attention.