



EUROPEAN CENTRAL BANK

EUROSYSTEM

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ECB

# **Financial Integration in Europe**

**2015 Report**

Brussels  
27 April 2015

Joint conference of the European Commission  
and the European Central Bank on  
“European Financial Integration and Stability”

## Background

- **Since 2005 ECB publishes indicators of financial integration in the euro area\* and assesses annually the integration of main market segments (10-year anniversary)**
- **Experience that despite EMU not all markets fully integrated**
- **Since 2007 further developed ECB report on “Financial Integration in Europe”**
  - Monitors and assesses financial integration
  - Overview of Eurosystem activities relating to financial integration
  - Discussion of topical issues (special feature articles)
- **Crisis made financial fragmentation a serious problem**
- **Since 2010 released together with European Commission’s European Financial Stability and Integration Report in joint conference**



*\* For the research that developed the first set of indicators see the ECB Occasional Paper no. 14 “Measuring financial integration in the euro area” by Baele et al., April 2005*

## 2015 contents

- **Key messages and overview**
- **Chapter 1: Financial integration developments (core of presentation)**
- **Chapter 2: Progress with Banking Union**
  - Single Supervisory Mechanism
  - Single Resolution Mechanism
  - EU macro-prudential framework
- **Chapter 3: Eurosystem activities for financial integration**
- **Special features**
  - A. Bank funding conditions and retail lending rates (see annex slides)
  - B. Banking Union and financial integration (speech D. Nouy next session)
  - C. Financial sector in the New National Accounts Framework (joint by ECB and Commission staff)
- **Annexes (incl. full set of financial integration indicators)**

## Rebound in euro area financial integration

- Returned to overall level comparable to before sovereign debt crisis
- Progress visible across money, bond and banking market segments
- Equity market segment more mixed
- Still room for further improvement, crucial for credit to real economy

## Driving forces include

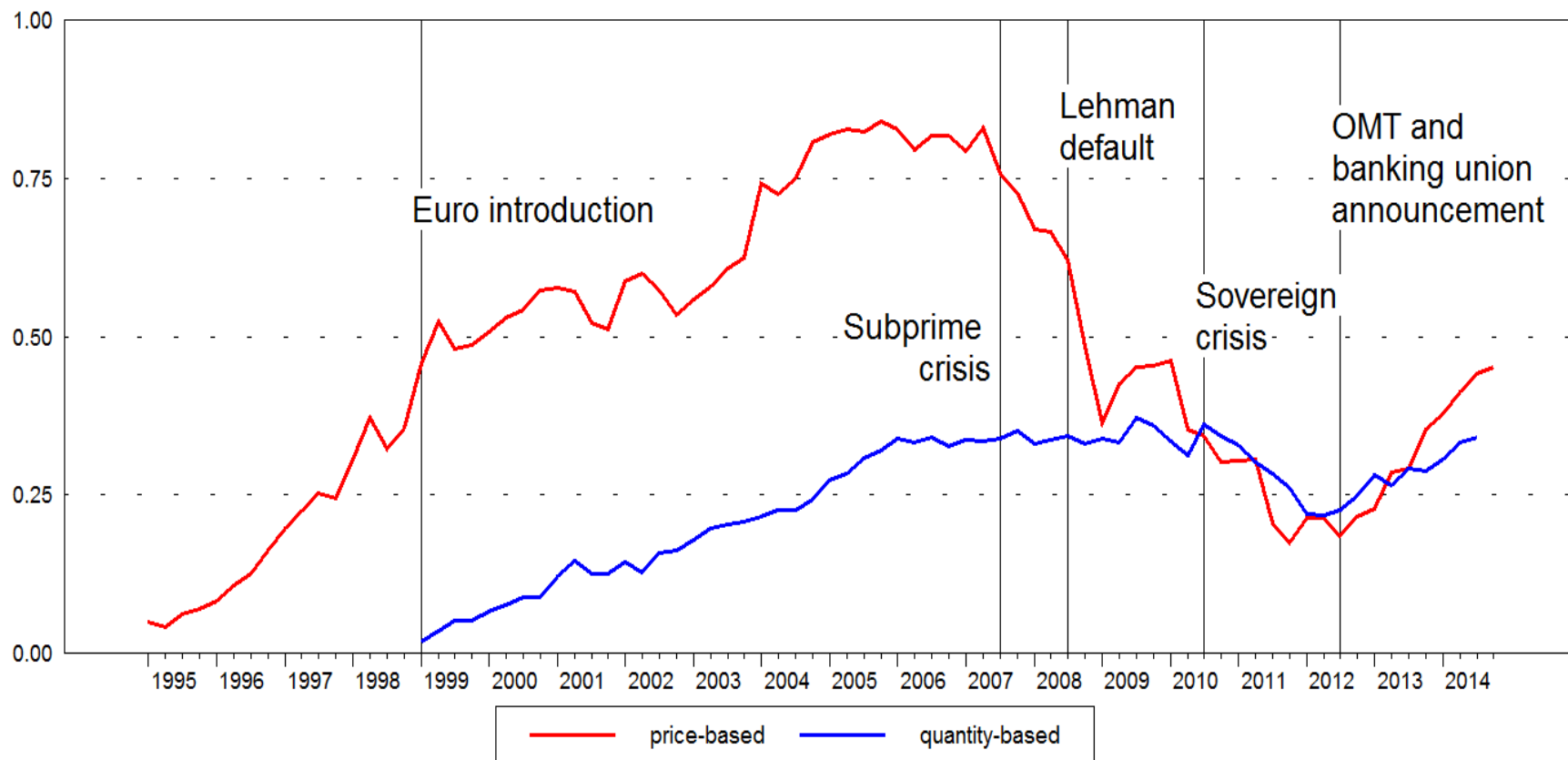
- Establishment of European Banking Union
- Series of ECB non-standard monetary policy measures

## Further progress depends, inter alia, on

- Effective further implementation of Banking Union
- Establishment of an ambitious Capital Market Union
- Continued implementation of monetary policy actions that counter financial fragmentation and its adverse effects on the real economy
- Other confidence building policies

## Overall financial integration: Recent material recovery

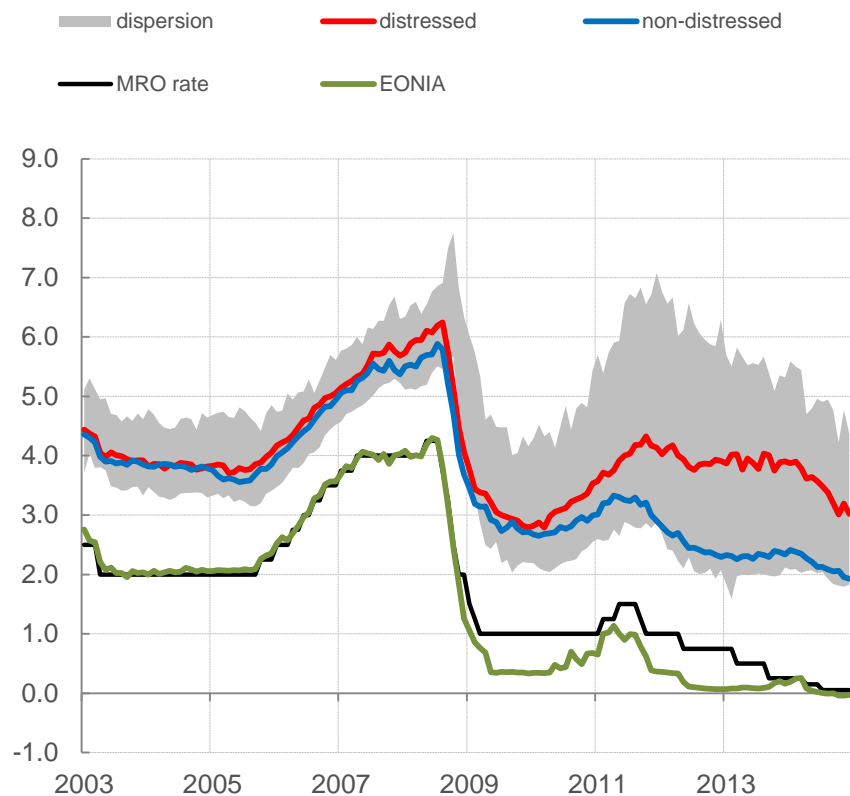
### Euro area Financial INTEgration Composites (FINTECs)



Sources: ECB and ECB calculations (based on Hoffmann, Kremer and Zaharia (2015), FINTEC – A composite indicator of financial integration in Europe, mimeo., see charts 2 and S5 in report)

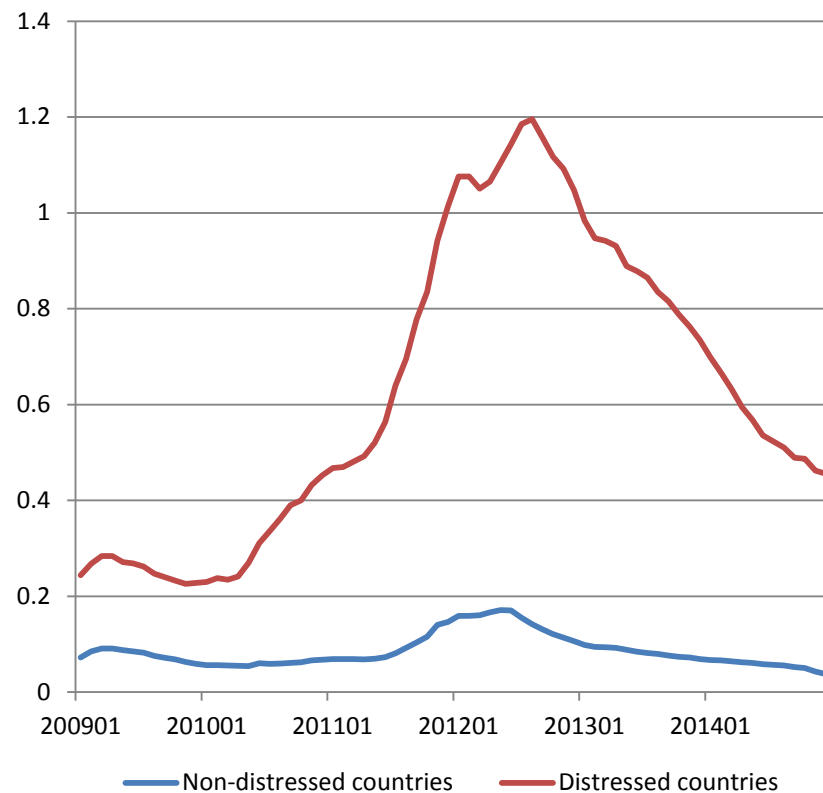
## Banking markets: Some improvement during 2014...

Bank lending rates to non-financial corporations (NFCs, % p.a.)



Sources: ECB and ECB calculations (see charts 27 and S32 in report)

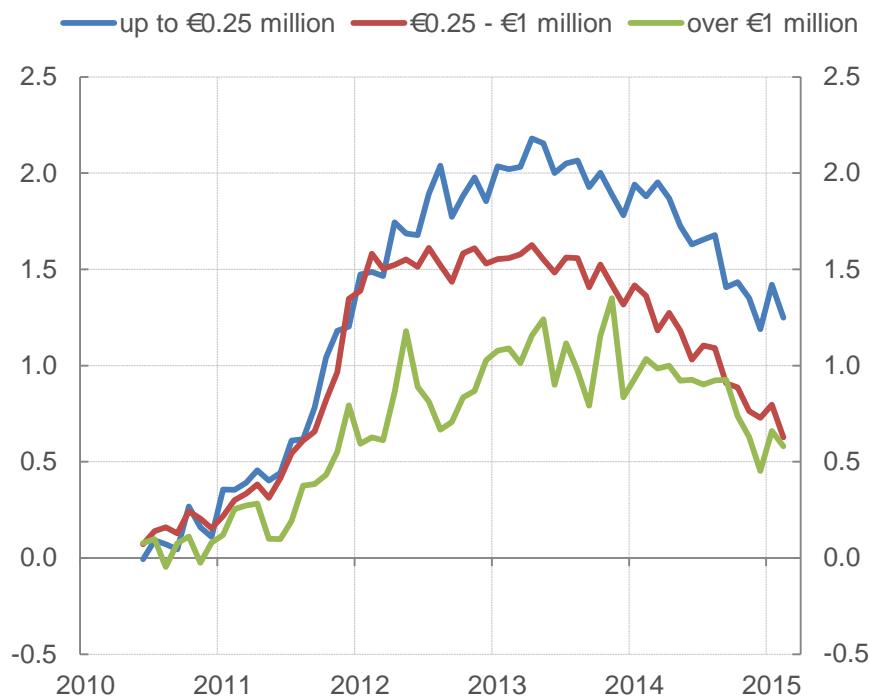
Sovereign tension component in bank lending rates to NFCs (p.p.)



Sources: ECB and ECB calculations (derived from methodology in chart 29 in report)

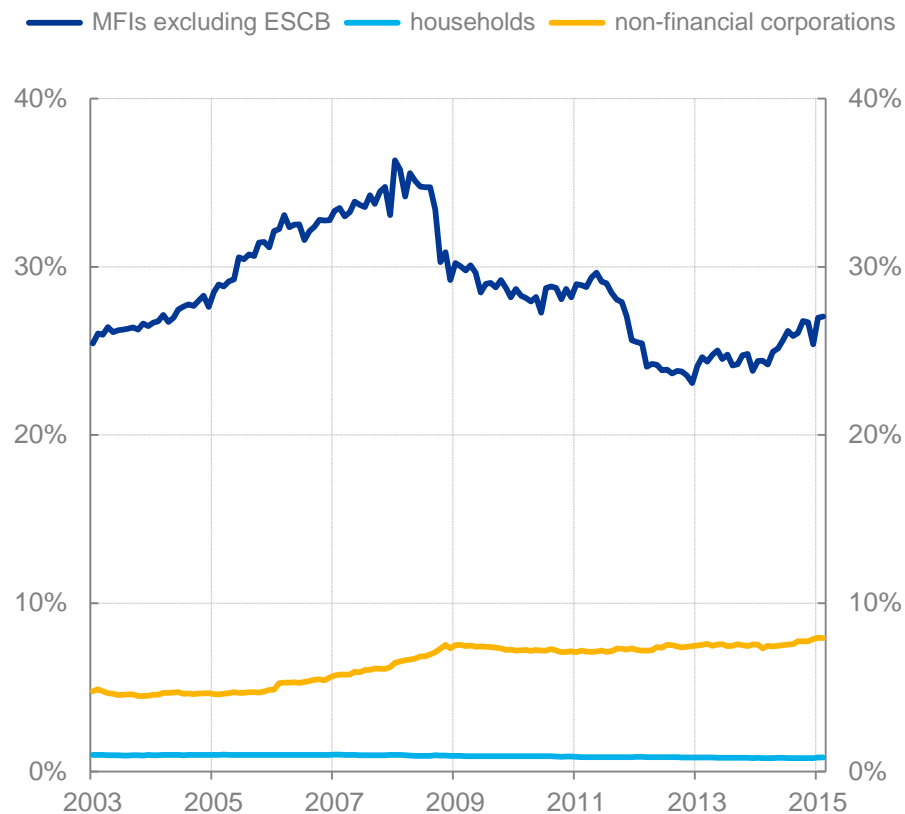
## Banking markets: ...reaching SMEs but quantities sluggish

Rates of small, medium and large bank loans to NFCs: Spreads between distressed and non-distressed countries (% p.a.)



Sources: ECB and ECB calculations (see charts 28 in report)

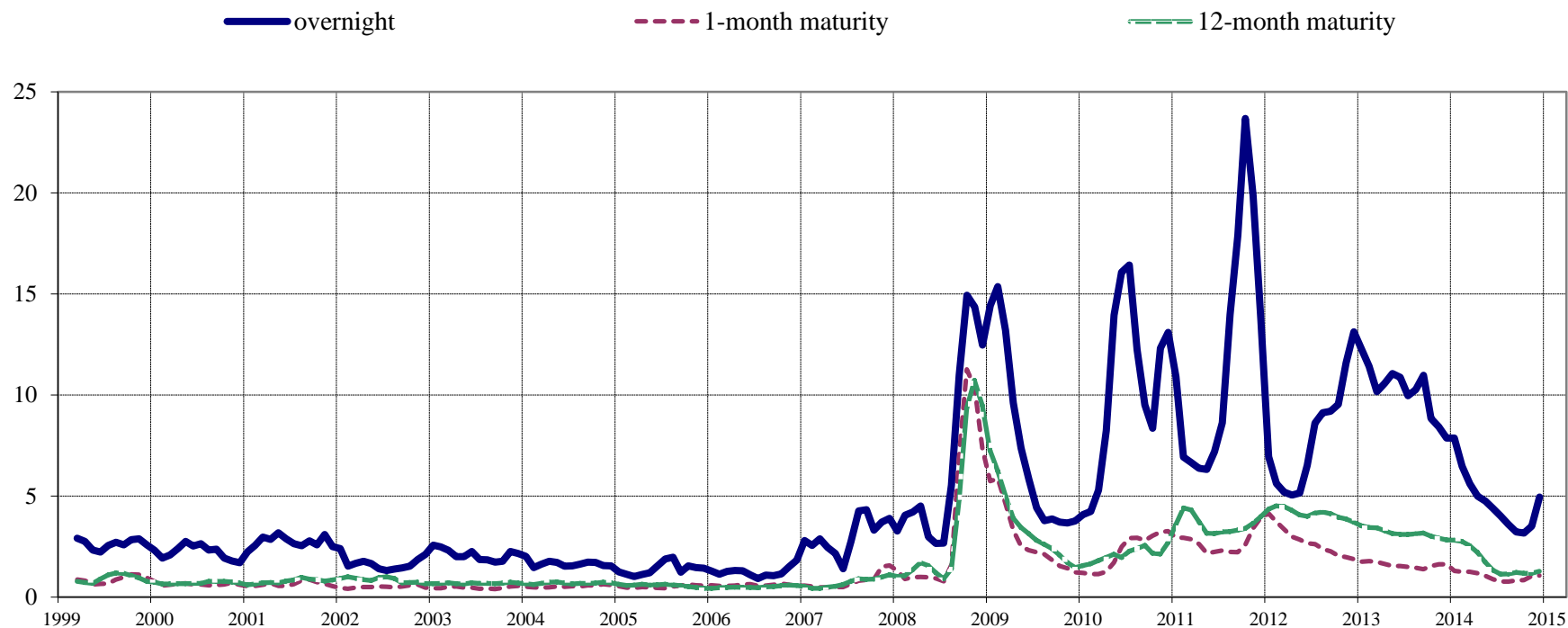
Share of euro area cross-border in total bank loans, by sector (%)



Sources: ECB and ECB calculations (see chart 34 in report)

## Money markets: Further decline of fragmentation for most of 2014

Cross-country dispersion of unsecured interbank lending rates, by maturity (b.p.)

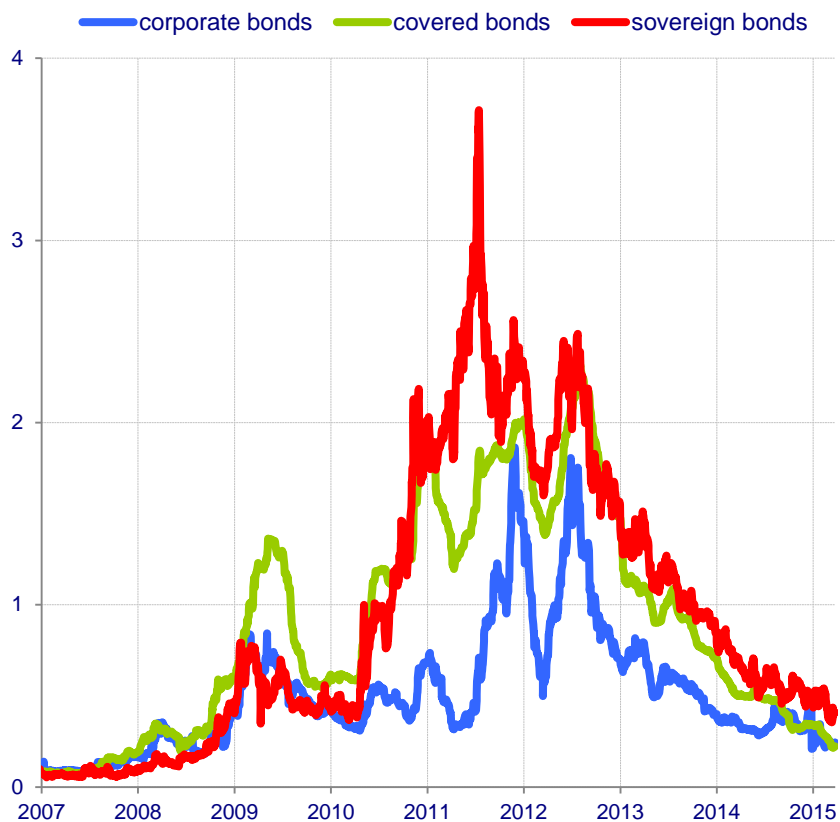


Sources: EBF-Euribor and ECB calculations (see charts 7 and S7 in report)



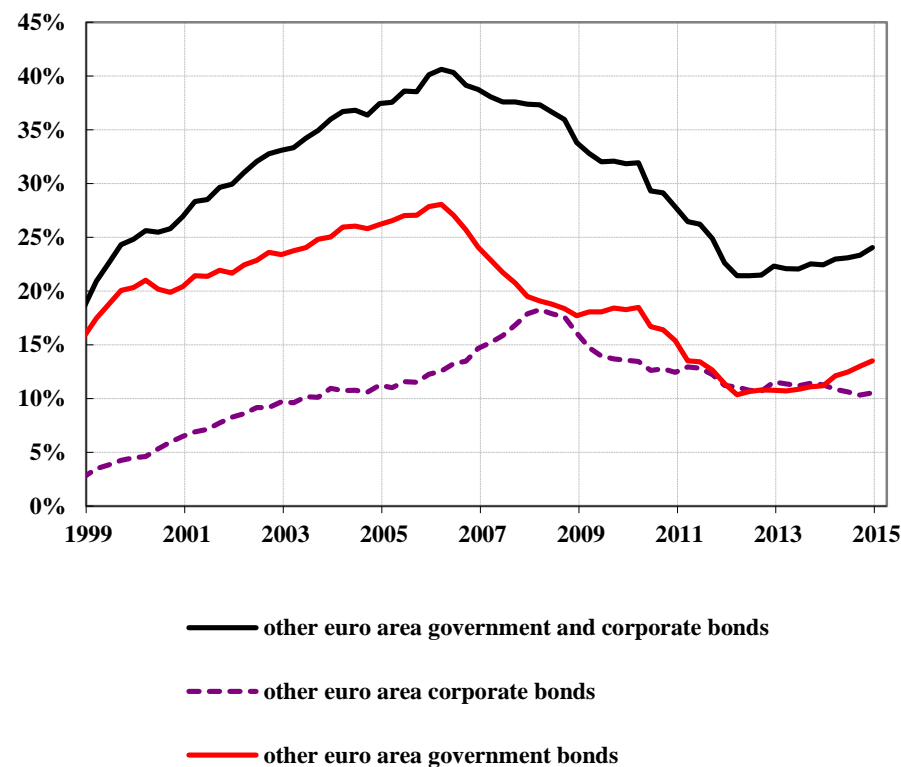
## Bond markets: Fragmentation receded further during 2014

**Cross-country dispersion of bond yields, by bond type (p.p.)**



Sources: Datastream Thomson Reuters and ECB calculations (see chart 16 in report)

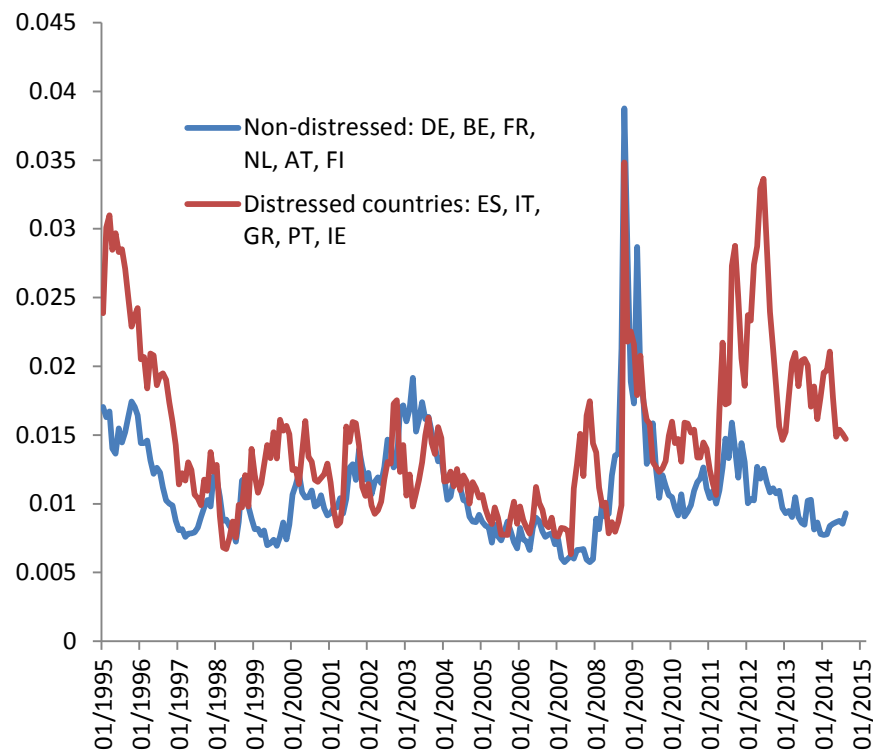
**Share of banks' euro area cross-border debt-securities holdings in total, by bond type (%)**



Sources: ECB and ECB calculations (see charts 15 and S23 in report)

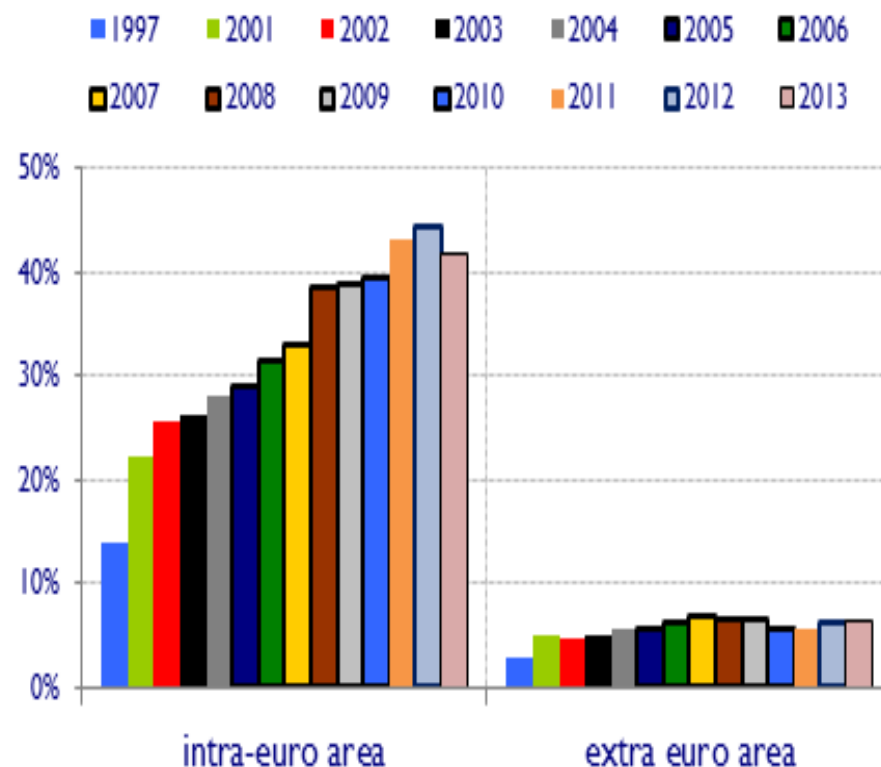
## Equity markets: More mixed integration developments

Industry earnings yield average relative to euro area, by country group



Sources: Thomson Reuters and ECB calculations (based on Bekaert et al. (2011), What segments equity markets?, Review of Financial Studies, 24(12), see charts 23 and S22 in report)

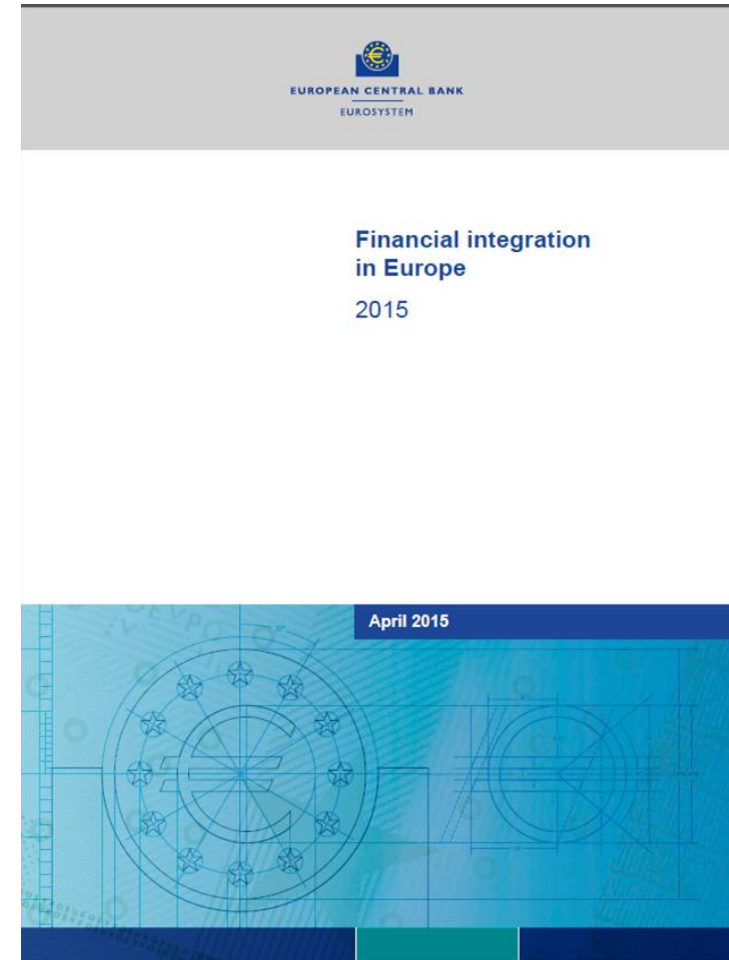
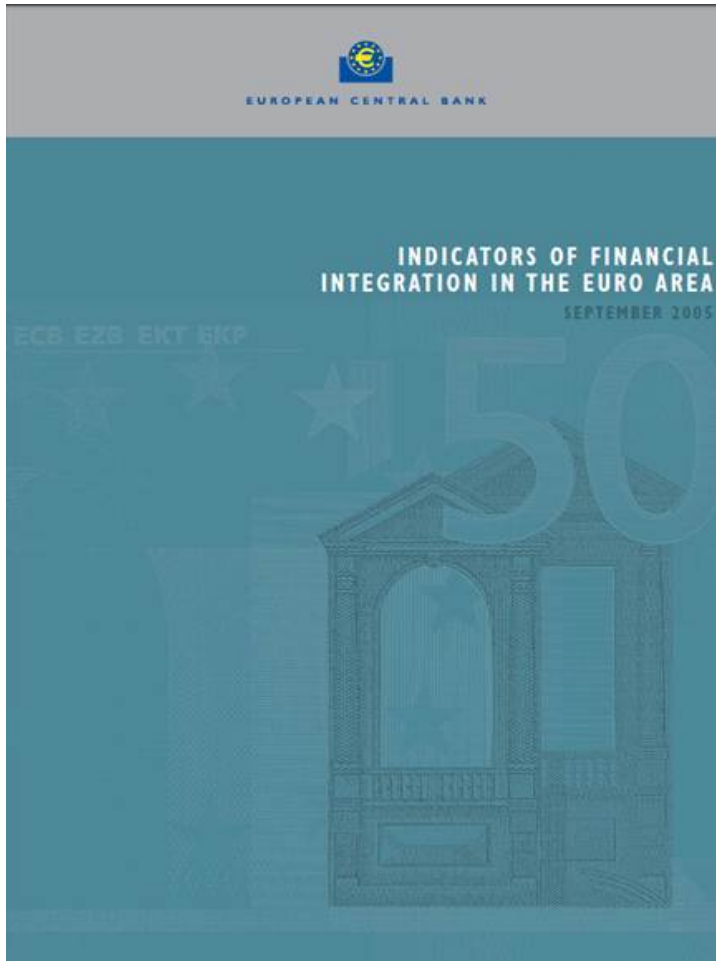
Share of equity issued by euro area country residents held by residents of other countries, by region (%)



Sources: IMF, Thomson Reuters and ECB calculations (see charts 26 and S26 in report)

# 10 Years of ECB Financial Integration Reporting

**2005**



**2015**

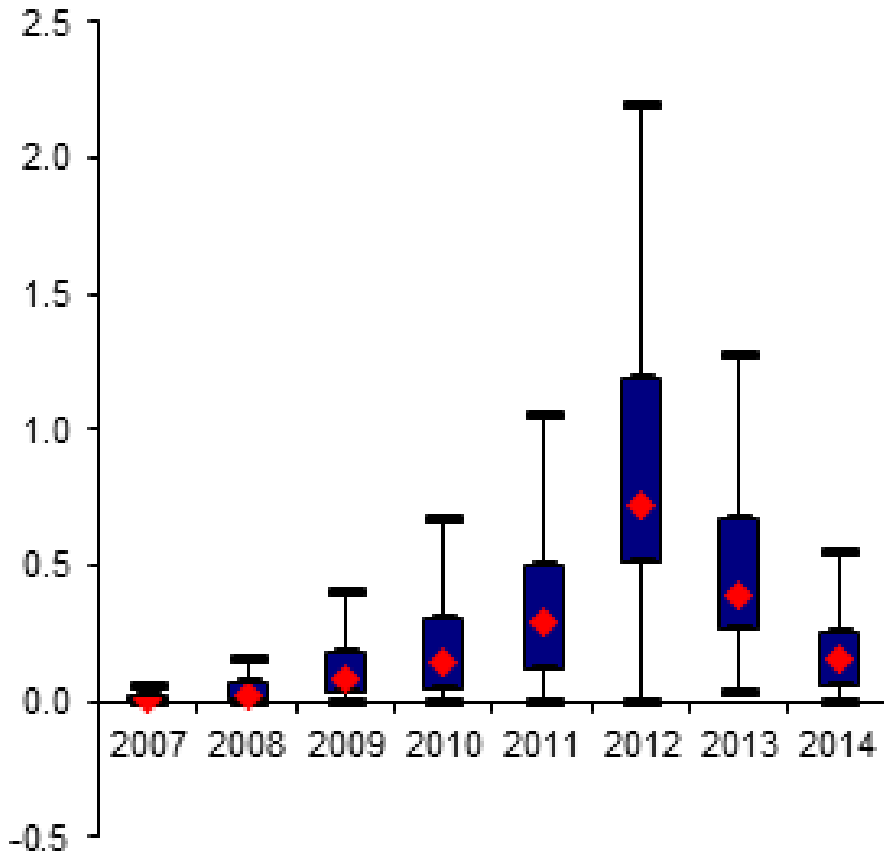
# Annex

## Summary of results on the relationship between bank funding costs and retail lending rates

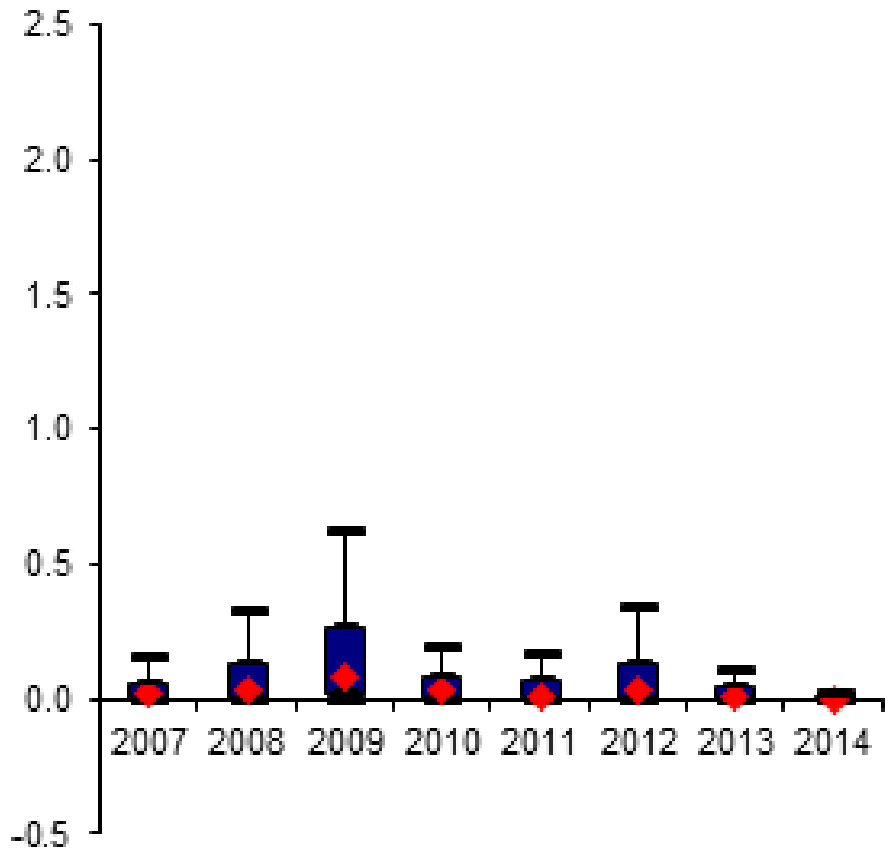
- **Higher loan rates in distressed countries reflect**
  - firms' higher macro risks and
  - banks' higher market funding costs
- **Loan rates in distressed countries react faster to funding cost shocks**
- **Rates of small loans react stronger to funding cost shocks and this effect is more pronounced in distressed countries**
- **One set of reasons why conventional and unconventional monetary policy actions reduce bank funding costs**
  - work against financial fragmentation and
  - benefit SMEs, in particular in distressed countries

## Simple exercise simulating banks' funding cost relief from Eurosystem operations (% p.a.)

### Distressed countries



### Non-distressed countries



Sources: ECB, IBOXX and ECB calculations (see chart 43 in report)