

**COMMISSION STAFF WORKING DOCUMENT**

**FINANCIAL INTEGRATION MONITOR  
2004**

The present report is the first annual report on indicators of economic benefits from financial integration, as announced in the Commission Services Working Document “Tracking financial integration” in follow-up of the July-2000 Ecofin request.

It comments on the main messages resulting from an extensive analysis of the EU financial system, published as a DG Internal Market Working Document.

# Financial Integration Monitor 2004

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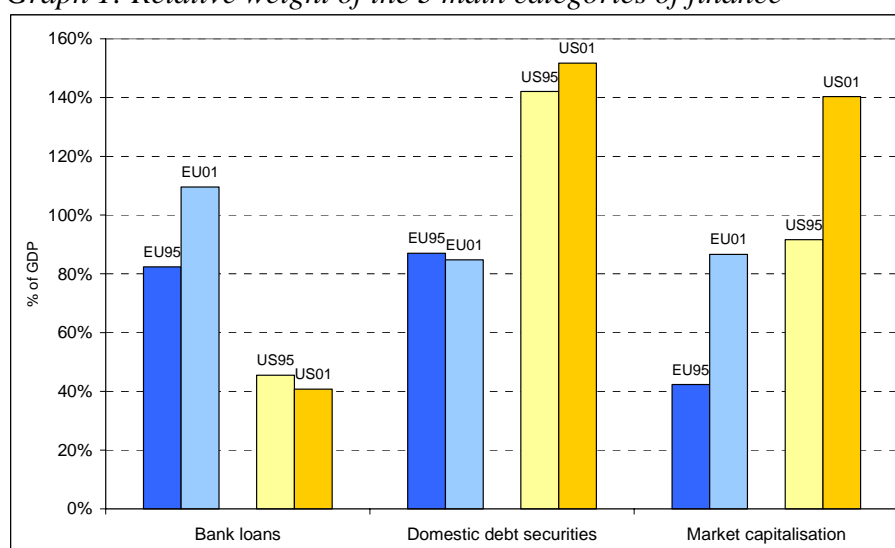
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# Financial Integration Monitor 2004

1. The European financial landscape has changed significantly over the past decade. Market-based financing has gained in importance, fuelled by a demand for market-based investments and the emergence of a population of institutional investors to service that demand. EU financial markets have been characterised by a deepening of liquidity and by an expansion in the range of financing techniques and products. Driving these changes, have been a number of profound structural factors – globalisation, technology, the relentless search for consolidation-based efficiency gains, conglomeration. In Europe, these changes have been facilitated by the introduction of the euro and ongoing action to remove regulatory and other public policy impediments to the pan-European organisation of financial business.

*The EU financial landscape has changed over the past decade with the emergence of funds, new financing techniques, conglomerates and the euro.*

*Graph 1: Relative weight of the 3 main categories of finance*



Source: ECB, BIS, OECD

2. At the same time, certain features of European markets have remained constant over the past decade. Bank lending (109.6% of GDP) remains the predominant source of external finance in the EU15<sup>1</sup>. Moreover, although all Member States have shared in the broadening and deepening of European financial markets, national financial structures continue to exhibit important differences. For example, the three principal sources of finance (bank loans, securities, bonds) play a different role as a source of finance in the different Member State economies. There are marked differences between Member States in the types of vehicle (pension, insurance and mutual funds) which are used to manage the long-term savings and pensions of households and employees. Enlargement will accentuate the diversity of financial structures and levels of

*Some features remain such as the importance of bank lending and the differences between national financial structures.*

<sup>1</sup> Unquoted shares and other equity represent 31% of total corporate financing.

financial development.

3. The present report describes some of the headline trends which have impacted European financial markets in recent years. The first section of the report is devoted to assessing the current state of integration across the main financial segments. The second section examines whether increased integration has been reflected in changes in intensity of competition or market structure in previously fragmented Member State markets. The third section seeks to document whether efforts to foster financial integration have been accompanied by any changes in efficiency and prices. The fourth section examines whether this period has witnessed any intensification in the channels through which financial risk may spread across Member State financial systems (and beyond). A final section briefly considers some of the main features of the new Member State markets which may be pertinent in assessing the relevance of EU financial policy for these fast-developing economies.
- The present report describes the main trends unfolding in EU financial markets, linked to the integration process,*
4. The Financial Integration Monitor (FIM) does not aim to disentangle the specific drivers of integration or to ascribe causality to the financial integration process. It seeks to document trends in the European financial system as an input to further policy discussion. The document follows an eclectic approach, bringing together material from a variety of sources. This is because conclusions on the progress of integration or other policy objectives (competition, efficiency, stability) cannot be based on the observation of one single indicator or trend. In each section, a number of indicators are charted.
- and this, without unravelling the specific drivers of the financial integration process.*

## I. FINANCIAL INTEGRATION

### MAIN MESSAGES

Financial integration is progressing:

- Progress is not the same in all market segments, as witnessed by the variety in the evolution of prices and volumes of cross-border trading flows: the two extremes of the spectrum are the unsecured money market and the market for consumer loans to households

Intra-EU market access takes place in direct and indirect ways:

- Establishment-based trade is relatively widespread, contributing to the emergence of a number of groups or entities with significant presence in other EU-countries than the home country.

- Direct cross-border activity mainly takes place in big volume markets. Direct cross-border offer of retail financial products remains the exception rather than the rule.
- Delivery of many products to the end-investor continues to be organised through local distribution networks (branches or local intermediaries).

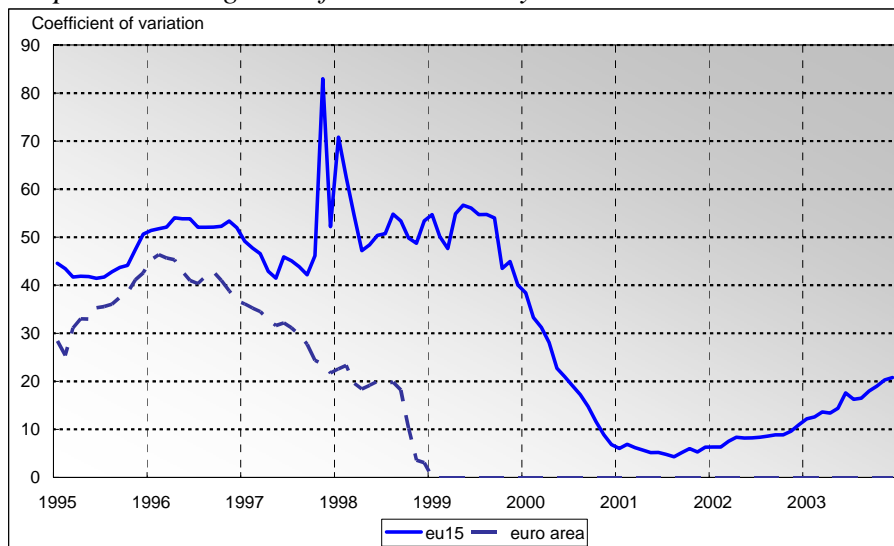
5. It is clear that conclusions on the advance in integration cannot be based on the observation of one single indicator or trend. In each of the market segments, the trends observed in terms of prices and quantities are combined in the analysis with data on market structure and product availability. The resulting snapshot provides us with an indication of the state of integration in each of the market segments.

## 1. Access to capital: progress in terms of integration

### 1.1. Credit markets

6. The unsecured money market is a fully integrated market within the euro area as indicated by the convergence in interest rates (see graph 2 below)<sup>2</sup>. In addition, there has been a step-change in the volume of cross-border money market flows. In unsecured money markets, cross-border trades represent 30% of total value processed on a daily basis.

Graph 2: Convergence of 3 month money market rates



*Full convergence of the unsecured money market rates for the euro area indicate that this market segment has been fully integrated since January 1999.*

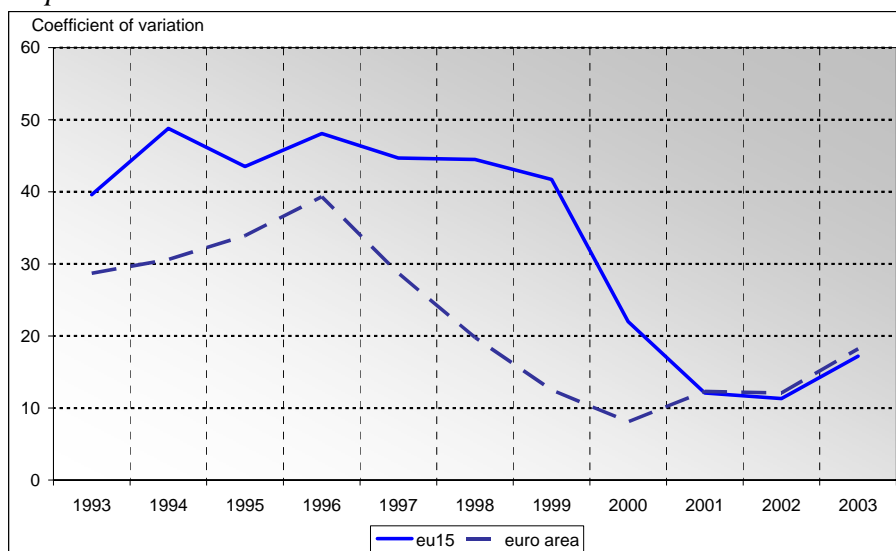
Source : ECB and Commission Services

<sup>2</sup> Convergence as measured by the coefficient of variation (standard deviation /mean).

7. The secured money market is slightly less integrated as there is still differentiation according to the origin of the collateral which is reflected in the couple of basis points difference in the pricing.
8. When charted over time, the level of dispersion in *national bank lending rates* has trended downwards. This convergence process seems to have pre-dated the introduction of the euro but has been further boosted by the latter. From 2001 onwards, the convergence seems to have slowed for most of the markets (graph 3 for the short term loans to enterprises), both for the euro area and EU15, with the exception of the medium-to-long term loans to enterprises.

*The degree of convergence in bank lending rates varies according to the market segment*

*Graph 3: Convergence in bank lending rates: short term loans to corporations*



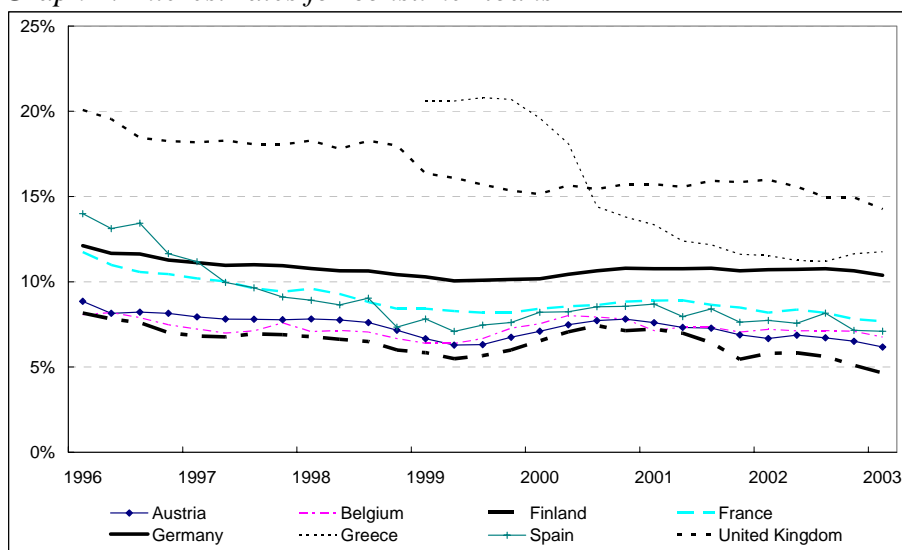
Source: ECB and Commission Services

9. The remaining dispersion in euro area bank lending rates is chiefly linked to the local character of some lending activity and broadly similar to the degree of dispersion that can be registered within some of the larger Member States. Rates for consumer loans within Germany, for example, vary between 5.5% and 13.7% for loans up to €100.000<sup>3</sup>. Dispersion of those rates over the German benchmark rate is approximately 9% (graph 4).

*Rate dispersion in largely local markets comparable to domestic markets.*

<sup>3</sup> Deutsche Bundesbank, Monthly Report, July 2003.

Graph 4: Interest rates for consumer loans



Source: ECB

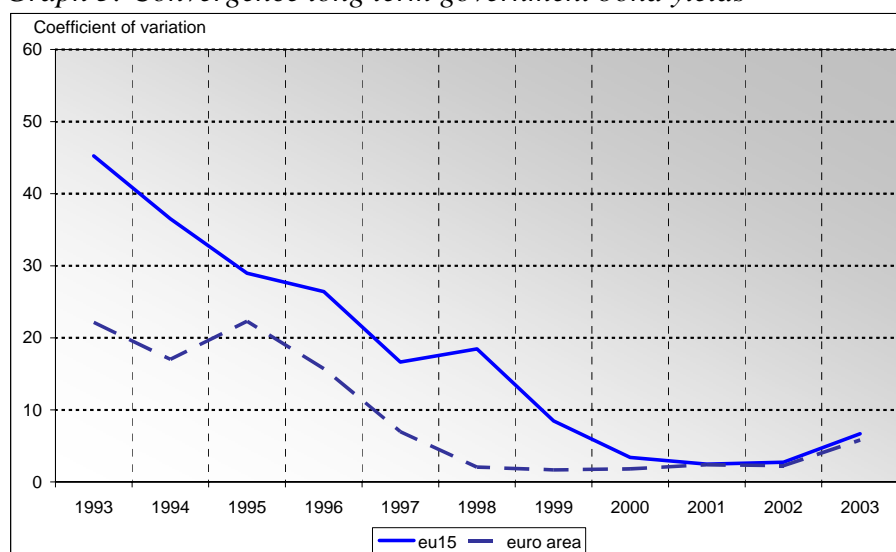
10. Convergence of interest rates may be observed independently of any significant increase in cross-border lending. The convergence of rates can also be due to perceived contestability of the markets: the threat of entry by partner country institutions may be sufficient to force incumbent banks to set competitive interest rates. Alternatively, competition between local incumbents may be sufficient to force all operators in the local market to pass-through the benefits of the lower cost of capital in the wholesale markets. *Price convergence only constitutes a first indication for integration*
11. A typical example here is the EU mortgage market. When considering headline rates, a certain degree of convergence can be witnessed. Yet, in addition to the influence of monetary policy on mortgage rates, they also conceal many differences still prevailing between countries in terms of tax and rate definition. Looking at cross-border volumes, it is clear that hardly any cross-border provision of services is taking place as far as home loans are concerned.

## 1.2. Markets for securities and other financial instruments

12. There has been a genuine pooling of liquidity at European level for common tradable assets, reflected in large flows and a broad participation. In those markets, cross-border trading is becoming a significant part in total activity.
13. Bond yields have been converging in parallel with the convergence in interest rates. Dispersion of sovereign bond yields between countries has decreased substantially over the past decade, but has stayed at roughly the same levels since 2001 (increased dispersion in the last 6 months). Trading of corporate bonds has also become increasingly pan-European. *Bond yields have converged broadly in parallel with the interest rate trend.*

Analysis of data on corporate-bond yields reveals that country-premia are low and only slightly above the country premia reflected in sovereign bond yields.

*Graph 5: Convergence long term government bond yields*



*The remaining variation in sovereign bond yields is largely determined by the “national issuer” and the absence of a single bond yield curve*

Source: ECB and Commission Services

14. In the bond markets, partial data<sup>4</sup> on trade settlements suggest that there has been a significant increase in cross-border volume. The data on trades settled by Euroclear shows that in 2003 the turnover of “international bonds” denominated in euro amounted to 20% of the turnover of “domestic bonds” denominated in euros. This has to be compared with a proportion of 17% for 2002.
15. Equity returns have become increasingly sensitive to European shocks, rather than to pure local shocks. According to recent calculations<sup>5</sup>, not only the proportion of EU stock variance explained by pure euro area shocks has increased considerably in the last decade (close to 25% for the period 99-03 from around 13% for 86-91), also in the run-up to the EMU (1992-98), but these pure euro area shocks have also a more homogeneous effect on equity returns (85% of the shock intensity transmitted to stocks for the period 99-03, vs. 65% for the period 86-91). This importance of common news as driver of euro area stock returns indicates a considerable degree of integration.
16. On equity markets, the proportion of shares held by non-residents exceeds 20% in almost all European exchanges, and 35% for the more open ones<sup>6</sup>. Another example related to equity markets is the Spanish exchange where foreign investors represent almost 2/3 of the total trading volume (in value). This indicates the importance of cross-border trading. Similarly, the increasing share of foreign holdings in the Swedish stock exchange is the result of liquidity

*And cross-border volumes are increasing.*

*Equity returns have become more sensitive to global shocks.*

<sup>4</sup> Euroclear Yearly Statistics.

<sup>5</sup> Baele et al., *Measuring financial integration in the euro area*, ECB Occasional Paper no. 14, Apr. 04.

<sup>6</sup> FESE, “Share ownership structure in Europe”, 2002.

redistribution across European equity markets.

## 2. Intra-EU market access

### 2.1. Re-organisation of the value-chain at EU-level

17. The refocusing and pan-European organisation of certain upstream business functions has contributed to the emergence of entities where certain back-office and strategic activities are organised on a multi-state group level. For those entities, the redeployment of activities has been accompanied by an optimisation of costs and business functions across Europe. Functions in direct contact with financial markets are the first to be rationalised.
18. Clear examples here are balance sheet management in the insurance field and centralised liquidity management in the banking sector. But these market activities are not the only ones and related functions (e.g. strategic planning, risk control, product development) also tend to be gradually more organised at European level.
19. Financial institutions have rebalanced their *asset and liability management activities* from a purely domestic to a European perspective. This appears, for example from the balance sheet of euro area banks: an increasing proportion of assets and liabilities relates to euro area counterparties and this, at the expense of purely domestic activities. Similarly, the share of European assets held by investment funds has been growing, while the one of domestic assets has been decreasing. *Financial institutions get organised at the European level*
20. The traditional national bias is progressively being replaced by European investment horizons. Domestic and other EU investments are increasingly regarded as close substitutes by market participants. The share of third country exposure remains constant, reflecting the fact that these have non-substitutable characteristics (links to underlying commercial/real transactions, geographical diversification benefits). *Exchanging the domestic bias for a European investment perspective.*
21. Pan-European operations of financial institutions are facilitated through the development of *more integrated market infrastructures*. The typical example here is the interbank cash market and the target payment system but, also in other big volume markets, pan-EU trading and post-trading infrastructures have been and are emerging. *Pan-European market infrastructures emerge,*
22. They have organised their European trading activities according to market segmentation rather than geographical localisation. This means that a company will usually have a single trading room for all European equity products, rather than having a trading room in each city with an exchange. *And financial institutions not only reorganise their trading activities*

23. Risk management is another activity organised at pan-European, if not worldwide, level. Integrated markets for derivatives and other risk transfer tools (e.g. securitization techniques such as Mortgage Backed Securities) allow companies to rationalize their risk management practices at the group level, rather than at a national level, just as is the case for their trading activities. *But also their risk management on a pan-EU basis.*
24. Large companies in general have, in the context of their treasury management, reorganised both liquidity and risk management on a pan-European scale.

## 2.2. Cross-border market-entry strategy

25. In areas where service providers face sophisticated clients and/or sell simple services or products, the integration process has propagated all along the value chain. Cross-border provision of services takes place. This is in particular the case for investment banking activities, and more generally for services to other financial institutions and large non-financial companies. (cf. also large risk insurance). *In dealings with sophisticated clients, cross-border provision of services occur*
26. At the other end of the product/service-chain, where the interaction of services providers with the individual customer takes place, activities remain largely locally organised when targeted at consumers and SMEs. On these markets, hardly any direct cross-border provision of services takes place. *Whereas, in the interaction with the consumer, hardly any takes place.*
27. Markets addressing the individual customer, such as bank lending/deposits and life/non-life insurance markets, have by and large kept their local character. This is reflected primarily in the local character of the channels for marketing and distribution of mainstream financial products. *Business to consumer remains largely local*
28. Establishment takes place either via subsidiaries, branches or the development of cross-ownership structures *and takes place through establishment*
29. *In the banking sector of many EU-15 countries, national establishments remain prominent. But, in the new Member States and in some regional clusters (such as Benelux or Nordic countries), this has evolved towards schemes more frequently found in the insurance sector, with the emergence of large cross-border players, acting through subsidiaries. The next step perceived in this process, as envisaged for instance in the Nordic countries, is to change subsidiaries into branches.*

30. Concluding from this that there is no integration at all in these markets, would be too hasty a conclusion. The example of the insurance market shows that cross-border activity is taking place indirectly through subsidiaries and, to a lesser extent, branching
31. Moreover, when assessed from a longer term perspective, a dynamic pattern may be observed. Even though distribution at this end of the market is initially locally organised and very different from one country to the next, a homogeneous integration process for the distribution end of the chain may take hold, following the integration and rationalisation of back-office functions, as is the case in the insurance sector.

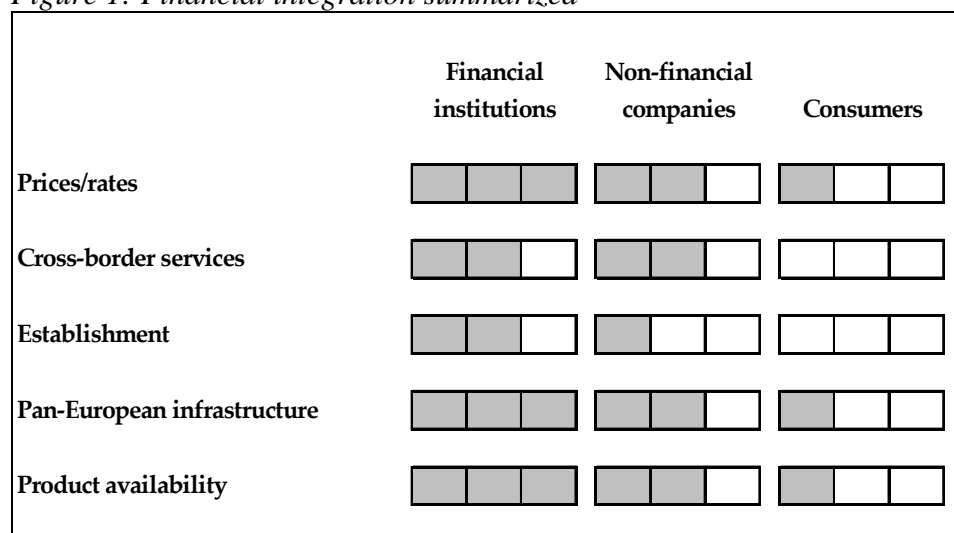
### 3. A snapshot of integration across markets

32. The above analysis can be summarised by the synthetic cockpit below. It provides an appreciation of the degree of integration in terms of price convergence, cross-border volume, the possibilities in terms of market access and the existence of pan-European infrastructures. The table also refers to product availability to complete the picture<sup>7</sup>. *The degree of integration related to the size of the counterparty.*
33. From the above analysis it is clear that markets are most integrated for financial institutions: they have access to common infrastructures such as Target, common trading platforms and post-trading infrastructures (Euroclear/Clearstream). Cross-border operations represent an important share of their total volume (e.g. for cash management operations on the unsecured money market). *Financial institutions operate in the most integrated environment.*
34. Non-financial companies have access to a wider choice of products compared to some years ago: in addition to the traditional products, new (EU-wide) products have become available such as Commercial Paper, corporate bonds, swaps and risk capital. Cross-border operations are possible (e.g. in terms of equity markets), be it intermediated or not. *Non-financial companies, depending on their size and sector, are situated between the financial institutions and the individual customer*
35. The larger non-financial companies are, the closer they come to the situation prevailing for the financial institutions. For SMEs, the situation is closer to the one described of the individual consumer.

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<sup>7</sup> Product availability has not been elaborated upon in this report but will be given more emphasis in the next report and should be interpreted in this context as the access to products previously not domestically available

Figure 1: Financial integration summarized



Source: DG Internal Market

## II. COMPETITIVE STRUCTURES

### MAIN MESSAGES

The potential impact of integration on competition structures is dual:

- A better match of supply and demand on an enlarged scale;
- Driver for a consolidation process.

Three patterns of competition structures are emerging:

- Competition within national markets;
- Multi-domestic competition with cross-border entities;
- Competition on an EU basis.

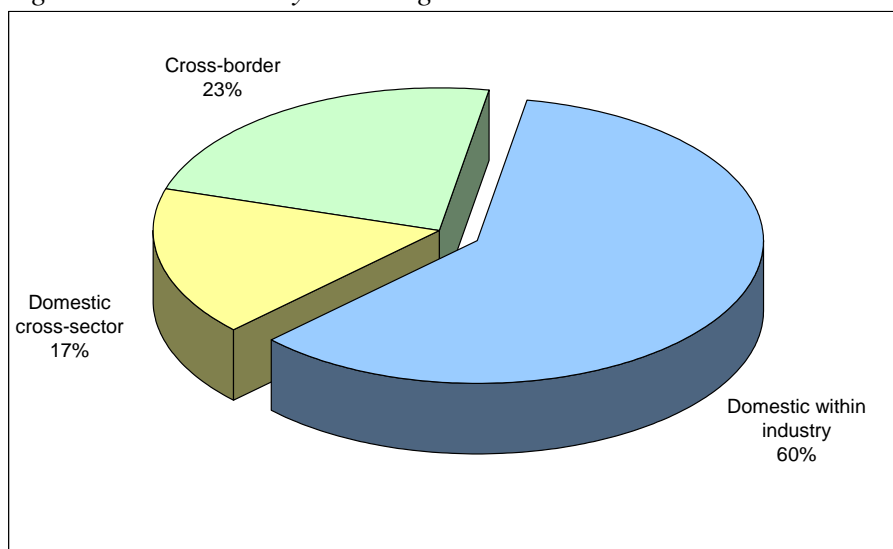
These structures correspond to different degrees of integration, and evolve as integration progresses.

36. This section examines whether supply and demand for the end-product interact on a cross-border basis or whether – despite integration further up the value chain - markets for the end financial product are organised locally within national boundaries.
37. Three patterns of competitive structures have been identified. They coexist in the different market segments and evolve as the integration process proceeds.

## 1. Competition within national markets

38. *In a first competitive structure*, markets are organised locally within national boundaries. Under this scenario, the absence of cross-border consolidation or provision of services confines both customers and services providers to the national market. Integration taking place in other parts of the financial sector may, however, encourage consolidation and exert upward pressure on concentration levels<sup>8</sup> of the concerned market segment, thus resulting in the creation of national champions. *In the first situation, integration elsewhere may result in the creation of national champions.*
39. This is typically the case for the EU retail banking sector (see graph below), with the exception of the regionally integrated Benelux and Nordic markets, and the investment fund industry, with the exception of the UK. *Both customer and provider are confined to the national market*

Figure 2: M&A activity involving EU credit institutions



Source: Thomson Financial

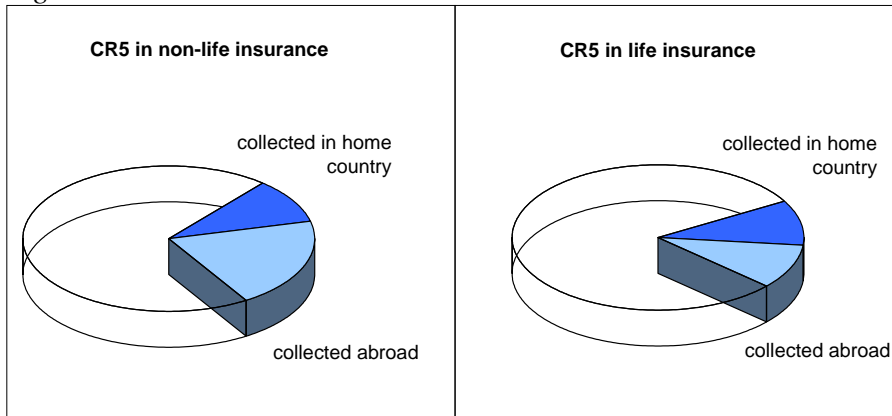
## 2. Multi-domestic competition with cross-border entities

40. In a second structure, customers are confined to their national markets, which are dominated by a few, large companies. Yet, under these circumstances, some are part of pan-European groups. Although consolidation is taking place at the domestic level, it chiefly happens on a cross-border basis through acquisitions, resulting in significantly increased concentration levels at pan-EU level. From a company perspective, an important share of business takes place in countries other than the home country. From a customer point of view, choice does not improve as no cross-border provision of services is taking place. *Multi-domestic competition with cross-border establishment*  
*Intermediate stage: no change for the end-user.*

<sup>8</sup> CR5: concentration ratio, reflecting the market share in terms of gross premium of the 5 largest companies.

41. This is the case for the insurance sector (see graph below) and the retail banking sectors in the Benelux and the Nordic countries.

Figure 3: CR5 in the EU insurance sector

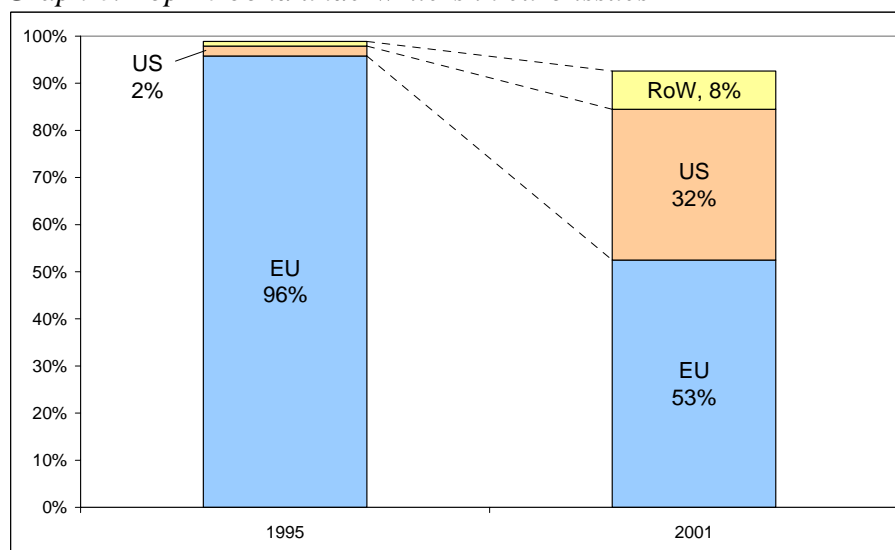


Source: CEA

### 3. Competition on an EU-wide basis

42. The third competitive structure is the one traditionally associated to a fully integrated market. It is characterized by the presence of companies operating in several EU countries, either through branches or directly via cross-border provision of services. New entrants from outside can easily acquire a significant market share. Financial markets in the EU are to a large extent organised this way. *Both customer choice and competitive pressures are enhanced*
43. For instance, in the investment banking area where the US investment banks are amongst the top 20 bond underwriters. As is shown by the graph below, they have increased their market share considerably in a period of 6 years, indicating the openness of the market to new entrants.

Graph 6: Top 20 bond underwriters in euro issues



Source: Thomson Financial

### III. EFFICIENCY

#### MAIN MESSAGES

Integration is expected to deliver benefits in terms of:

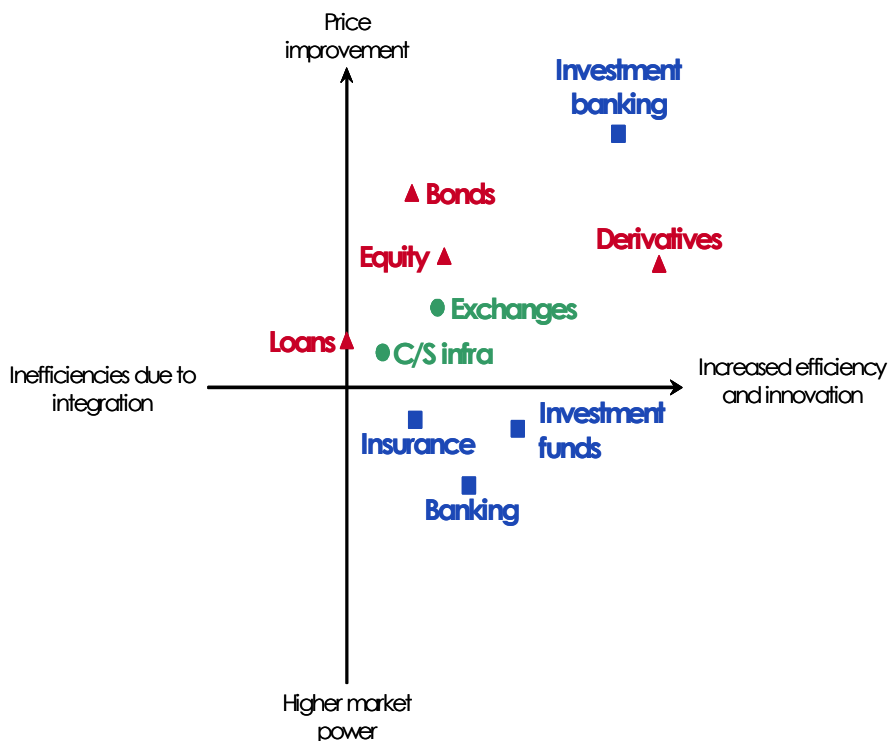
- Economies of scale and scope;
- Better risk allocation;
- Innovation.

We can observe the following trends:

- Overall efficiency has improved, even in less integrated segments;
- The integration process spurred innovation in all segments;
- But the situation is more contrasted at the level of prices.

It seems that it is only in the more integrated segments that efficiency gains are distributed along the value chain.

Figure 4: Efficiency spectrum

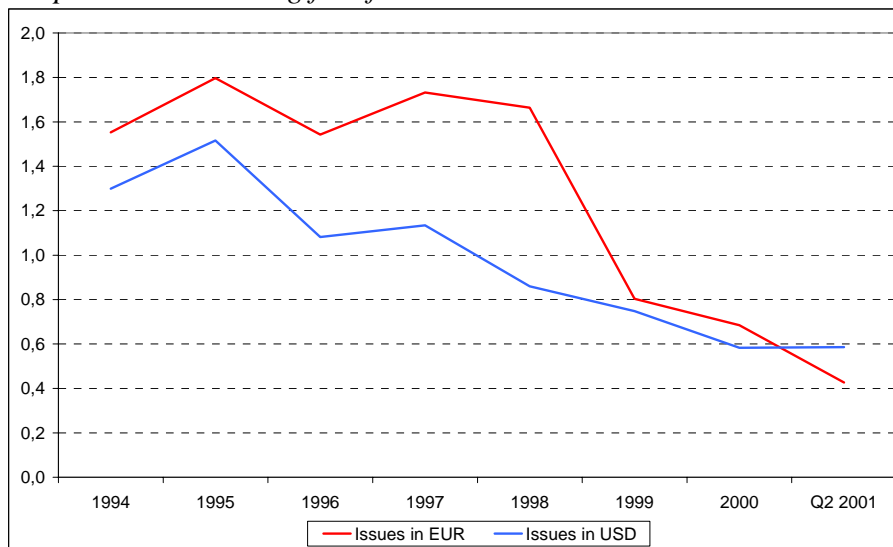


Source : DG Internal Market

## 1. Economies of scale and scope

44. An immediate corollary of integration is the creation of a deeper, more liquid and thus more efficient market. The resulting wider pool of participants will increase the variety of the risk profiles and facilitate the risk diversification, resulting in a possible prices reduction when compared with the smaller pre-existing markets. *Efficiency and risk allocation are enhanced in a deeper and more liquid market.*
45. Further efficiency gains can be realised by service providers at a rather early stage of the integration process and this through the process of back-office integration. This improves not only corporate profitability but also enhances product availability. *Efficiency gains will propagate,*
46. Propagation between market compartments can induce efficiency gains even within segments that remain largely nationally organised. For instance, the development of integrated money markets allows banks to have a more efficient and cheaper liquidity management, and thus has consequences for the domestically-organised consumer loan offer. *even to slightly less integrated market segments.*
47. However, price improvements for the end-customer only seem to occur in those market segments which are fully integrated. As an illustration, one might refer to the highly competitive investment banking activities, such as the bond underwriting fees where fees have substantially decreased.

Graph 7: Underwriting fees for Euro bond issues

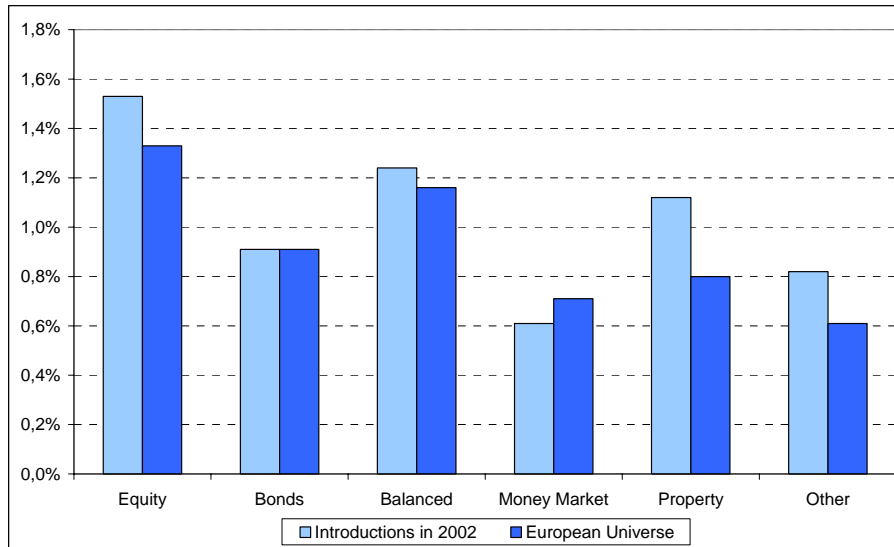


*For the integration process to be translated into price reductions for the end-customer, full integration seems to be required.*

Source: Santos and Tsatsaronis, *The cost of barriers to entry: evidence from the market for corporate euro bond underwriting*, BIS working paper No. 134

48. On the contrary, in the less integrated investment fund business, fees have on the whole increased in 2002 .

*Graph 8: Investment fund fees: annual management fees*



Source: Morningstar, published by DWS Eurofund, 2002

49. Price improvements only take place in those market segments which are at a rather advanced stage of integration and thus which are open and competitive.

## 2. Innovation

50. Market integration is expected to foster innovation, not only in terms of new methods or tools to improve existing products but also in terms of new products and services. *Innovation in terms of products and market infrastructures is fostered by market integration.*
51. For instance, the initial fixed costs implied by the developments of new and more efficient infrastructures are more easily distributed among a larger number of participants. Therefore, such developments clearly require that markets reach a “critical size”, in order for them to enhance market efficiency and foster demand for existing, as well as new, services and products.
52. Increased liquidity, coupled with wider possibilities of risk diversification, also opens up new opportunities for investments in less standardised products. For instance, funds raised in the context of European risk capital have multiplied by a factor of 10 in the past decade.
53. Innovation resulting from integration can also disseminate to less integrated market segments such as the ones of the end-consumer. A good illustration in this context is the 60% increase in the number of investment funds in the period 97-2002 which has resulted in a wider choice of products to the individual consumer while the distribution of the products chiefly remained organised on a national basis. *Innovation can propagate to less integrated market segments.*

## IV. FINANCIAL STABILITY

### MAIN MESSAGES

An increasingly integrated EU financial system can have the following effects on financial stability:

- The increased scale of financial institutions implies that many national markets have become vulnerable to a few, systemic institutions;
- The resulting cross-border and cross-sector inter-linkages normally contribute to an efficient distribution and allocation of risk across the EU but may propagate financial contagion across sectors and countries.

Those cross-border links in every market segment of the EU financial markets imply that financial stability concerns are no longer exclusively a national concern but have also become an issue of European interest.

### 1. Scale developments

54. In recent years, the EU financial sector has been through a strong consolidation phase which has changed the structure of the financial system towards larger and more complex financial institutions and group structures. A growing number of financial institutions have attained a critical size, allowing them to monitor their risks with more advanced tools in a more efficient way.

55. At the same time, the stability of the EU national markets has become increasingly dependent on a few systemic institutions. Concentration ratios in some Member States have reached levels that have raised the concerns of the competent competition authorities. The average market share of the 5 largest institutions in EU15 countries comes close to 60% in both banking and insurance sectors (life as well as non-life).

*Financial institutions have become “big at national level”.*

56. At a pan-European level, there are only a few systemic financial groups to date. Concentration levels at European level are considerably lower than at the respective national levels. Even if they do not pose a concentration problem at the EU level to date, the high national concentration levels can pose an EU-wide problem in case of risk transmission.

*Even if they do not pose a concentration problem at the EU level to date, the high national concentration level can pose a contagion issue.*

## 2. Cross-sector linkages

57. One of the most striking developments in European financial markets in recent years is the emergence of a tier of complex groups and conglomerates as European financial institutions have implemented broader diversification strategies to evolve away from the traditional banking/insurance split. These strategies have involved the creation of financial conglomerates spanning a combination of banking, insurance, investment services and collective portfolio management. As a weighted average, financial conglomerates account for approximately 30% of the deposits and 20% of premium income in EU15 Member States. However, in the smaller one, their market share exceeds 50%. In relation to assets, financial conglomerates have a considerably higher market share. *Two main types of cross-sector linkages can be distinguished: financial conglomerates*
58. In addition to the emergence of financial conglomerates, cross-sector links have been reinforced in recent years through the development of instruments for credit risk transfer and hedging. *and, risk transfer mechanisms.*

## 3. Cross-border linkages

59. At the EU level, cross-border (both financial and ownership) linkages exist in each segment of the financial sector. These well-developed risk transmission channels at pan-European level normally contribute to the efficient distribution of risks, which has a stabilising impact. However, the transmission channels are also potential vehicles of cross-border risk contagion. *In terms of cross-border linkages,*
60. *Financial linkages* are particularly important to monitor from a stability perspective in markets where few participants dominate the activity such as the unsecured money market and the market for reinsurance. Common platforms for trading, payment and settlement also constitute important financial links. *the emerging pan-EU market infrastructure*
61. *Ownership linkages* also constitute risk transmission channels. In EU-15 banking sector, for instance, foreign ownership accounts for 30% on average of assets/capital of the national banking systems. Ownership linkages can constitute a true challenge to supervisors as an increasing number of financial organisations are setting up operations in other Member States through branches and may require closer cooperation between national supervisors. *and, ownership links, constitute important risk transmission channels,*
62. Increasing inter-linkages between sectors and Member states allow for a more efficient risk allocation. At the same time, however, it creates new challenges for pan-European risk management and supervision, raising the financial stability issue to the EU-level. *giving financial stability an EU dimension.*

## V. 10 NEW MEMBER STATES

### MAIN MESSAGES

On May 1st, 10 New Member States officially join the Internal Market for financial Services. In next year's report, they will be included in all sections of the report. For this year's report, we draw on some of the main features of their financial systems.

Apart from the banking sector and, with the exception of Cyprus and Malta (where domestic financial sectors largely reflect the average EU profile), the acceding countries clearly lag behind the EU in terms of insurance, asset management, degree of liquidity, institutional investor base and stock market capitalisation.

The economies of the acceding countries are growing at a faster pace than the EU average and their demand for capital is important. Access to the pan-European capital markets and banking systems upon accession may unleash part of their financial potential.

63. Diversity in the importance of the main categories of finance can also be detected among the accession countries: the importance of the two main categories of insurance varies considerably between the 10 countries, stock market capitalisation in 2002 varied between 7.7% of GDP and 41.9%, debt securities between 3 and 68%. The bank sector is the most developed and dominant source of finance. *The financial structures of the new Member States vary considerably.*
64. EU ownership interests in the banking systems of the new Member States are particularly strong. Foreign (mostly EU) ownership exceeds 70% in the banking systems of Slovakia, Estonia, Poland and Hungary. *Between the EU15 and the new Member States, strong ownership linkages already exist.*
65. Sometimes, ownership originates from one particular dominating country, e.g. Swedish interests hold substantial ownership (90%) in the Estonian banking sector.
66. Also in the insurance sector, foreign ownership is important: of a total of 255 companies in 2002, 91 were subsidiaries of EU companies and 40 branches.
67. The majority of accession countries have potential for further financial development: on average, the size of their banking sector, as measured by assets/GDP is around 80%, against 260% for the incumbent member States. Stock market capitalisation is around 16% compared to an EU-15 average of 67%. *The potential for further financial development and growth is high.*