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Financial Capital Markets Integration in Europe

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Ladies and Gentlemen,

It is a great pleasure to be here today, and I would like to thank Reuters for offering me the opportunity to share with you some of my thoughts on financial capital markets integration.

Integration has become a second nature of Europeans. Because in Europe we have understood that with local policies, continued fragmentation and frictions, we will never be successful in the long term. Too often in our history we have learned this lesson the hard way, by war, bloodshed and tears. However, over the last six decades, we have fought this challenge in boardrooms – an approach which is much less damaging and a lot more comfortable.

I am very well aware integration is not just a European feature. Day-in, day-out, we experience more worldwide integration of markets and this will further develop as – in the end – it will mean real tangible benefits for all stakeholders involved. There is an obvious need for increased international cooperation to address these developments most effectively. Continuous cooperation between European and Chinese authorities, and those in other parts of the world, is therefore crucial.

Doha and Services

In this context, I would like to say a word about the negotiations in WTO. The so called Doha Development Round is now in a crucial phase. Negotiations should be finalised by the end of this year, but much work still remains to be done. I am particularly concerned that Services, which make up for 60-70% of GDP and jobs in most countries, have until recently not been given sufficient attention. Our potential gains from a positive outcome in the GATS Services negotiations would be substantial.

The financial services industry in the EU is very well placed to take advantage of new possibilities that further liberalisation would bring. Likewise, China and other significant and emerging players stand to gain. I believe a broad and balanced package is still within reach and I appeal to all major players to leave tactics behind and together work on realistic solutions.

The importance of global standards

Globalisation cannot be restricted to a purely economic process. It brings about changes in our ways of life, our cultures and our perception of others. But it is undeniable in the economic sphere, and singularly in the financial sector, where changes have been most profound.

It is therefore obvious that if we are to harness globalisation for the good of all, if we are to make it sustainable and workable, there have to be rules. As the interdependence of markets grows, so the downsides of widely differing regulatory systems become ever more apparent. They present significant obstacles to trade or to investments. In the worst scenario they can even lead to insurmountable conflict of laws.

To avoid this and to offer a proper reply to globalisation, we must all, the EU included, become much more outward-looking. Our legal structures must be adequately attuned to the global economic framework and to key marketplaces.

Most importantly, we need international standards in order to remove regulatory barriers to world trade and to create a business-friendly climate – a climate based on trust, transparency, predictability, legal certainty, and offering carefully calibrated levels of consumer and investor protection. Everyone will benefit.

International bodies like WTO are important, but can never be sufficient. They must be complemented by direct bilateral activities. That is why I am here in China.

Our experience within the EU Commission shows that intensified informal cooperation with the regulators from relevant third countries - working upstream of the political process to ensure market access and to achieve convergence or equivalence on basic regulatory principles - works.

Integration of financial markets

Today, I will not only look forward – to the big challenge Europe and China face in terms of integration, a globalising economy, global standards and best-practices. I would first like to take a step back and share with you the lessons we have learned in Europe after a decade of intense capital market integration. At a time when China is implementing an ambitious financial sector reform, I believe that these lessons might be helpful to further improve the functioning of financial markets in China.

As you all know, financial markets play a key role in the economy. These markets efficiently allocate financial resources and thereby enable the whole economy to expand and develop optimally. The larger the market, the better the allocation in principle should be.

However, the financial sector is often constrained in the performance of its functions. Fragmentation of markets and applicable regulation was recognised as one of the main constraints in Europe only a decade ago. Europe consisted of many fragmented national markets, not of a single European market. At global level, Europe's competitiveness was sub-optimal as it could not benefit from its significant size potential.

However, in the last seven years, financial integration has really moved forward in Europe. The foundations for an integrated financial market in Europe have been laid. Major political and legislative advances have been made. We are on the way to creating one of the world's biggest financial market places – an open and competitive market place – encouraging innovation, creativity and flexibility. The challenge now is to consolidate the progress made.

My job as Member of the European Commission is to promote and defend the principles that underpin the internal market and the free flow of capital, goods, services and workers in Europe. Where artificial barriers remain or new ones are introduced, I will go after them; where competition law is not complied with, authorities at national and European level will act; where regulation is not complied with, infringement procedures and prosecution will follow.

It is my personal challenge, to create, in Europe, the best financial framework in the world. Only then we will be an attractive market place and able to deliver real, tangible benefits for the citizens and businesses in Europe and other parts of the world.

Benefits of integration

The overall expected benefits of integrating financial markets consist of six elements:

Firstly, benefits of integration for international trade and cross-border investments

Financial integration will support the development of cross-border trade. We see that European markets have become more attractive for domestic capital and foreign capital inflows, attracting inward investments. Conversely, building liquid financial markets may provide companies easier access to larger markets and provide them with the home base needed to expand internationally.

Secondly, benefits for competition

Financial integration will ensure a level playing field across the different markets, as well as foster competition between services providers, to the benefits of end-users in terms of lower prices, improved quality and increased product variety.

Thirdly, benefits for firms in terms of investment, operating costs, products and services

Financial integration will allow the financial sector companies to benefit from economies of scale and scope, leading to improved and more innovative products and services at lower prices.

In addition, in the non-financial sector, small and medium sized entities can access a wider availability of more innovative and lower cost finance to fuel their growth, while larger companies profit from an overall reduction in the cost of capital and a wider range of financial products.

Fourthly, benefits for firms in terms of administrative burden

Aligning national regulatory approaches to a common regulatory system is challenging and may entail considerable "ex-ante" adjustment costs for national enforcement agencies and market participants. However, over time, successful harmonisation can considerably reduce the administrative burden for businesses that operate internationally, by replacing many different sets of diverging rules by a single set.

Fifthly, benefits for consumers

The impact of further integration on consumers is twofold. First, there is a direct effect of increased product variety, improved quality and lower prices. There is also an indirect positive impact. Through pooling of liquidity and risks across financial markets and improved efficiency of capital allocation, consumers have access to wider investment opportunities, can benefit from improved returns over a longer period, and from reduced financing costs.

Sixthly, and finally, overall macroeconomic impact

Given its size, growth potential and its role in financing other sectors of the economy, the financial sector has a direct and decisive impact on the aggregate competitiveness of modern economies.

With integration, financial stability can improve. The public sector can meet its financing needs at lower cost. Integration supports society in financing structural economic challenges. Be it the long run pension deficit Europe faces, or the rapid growth in the economy – with high pressure on commodity prices – here in China.

The European case: the FSAP

Five decades ago, six European countries decided to combine their strengths in what we now call the European Union. It has been a success so far. Since May 2004, the Union consists of 25 Member States, all recognising the benefits of working together, of integration.

However, even less than a decade ago, Europe's financial markets remained fragmented and segmented. With the introduction of a common currency in Europe, the euro, there was a unique window of opportunity to equip Europe with a more modern financial apparatus.

The European Commission came forward with an inspirational programme for rapid progress towards a single financial market, the Financial Services Action Plan, in 1999. European Heads of State and Government have called for the completion of the Action Plan by 2005 and the integration of the European securities market by the end of 2003: a demanding, but necessary, timetable.

The Action Plan has triggered European financial integration. One of the reasons for this success is that the Commission listens to market participants very carefully. They assist us in assessing the strengths and weaknesses of various proposals and advise the Commission on future priorities. And we have listened carefully to regulators, Member States and the European Parliament as well. The open way we have been working is a strength and has helped to build confidence in the process of integration.

Although it is still too early to judge the exact impact of the Action Plan, evidence suggests that European markets are integrating, particularly in the wholesale market. Markets are beginning to restructure. Rationalise. The financial industry is developing European strategies. A large, deep and well-functioning euro bond market has been created. International issuance in euros is increasing strongly. IPOs and private equity are strong. We see a growing presence of financial institutions in partner country markets. We see evidence of increased competitiveness and efficiency and an extension of the range of products available at domestic level. And profits in the industry are good – in all sectors.

International Accounting Standards

One of the most important elements of the Action Plan was the requirement for all European companies listed on a stock exchange to prepare consolidated financial statements prepared on the basis of a single set of financial reporting requirements. It has received much attention from the press, Member States, companies and many other stakeholders and therefore deserves a closer look.

Comparable, transparent and reliable financial information is fundamental for an efficient and integrated capital market. Lack of comparability will discourage cross-border investment because of uncertainty as regards the credibility of financial statements. Only two years ago, European companies had to comply with the standards of the different Member States in Europe.

Investors and other stakeholders faced difficulties when comparing financial statements of companies registered in different parts of Europe. The financial markets in Europe were functioning sub-optimally.

However, since last year, European companies should be able to raise capital throughout Europe using financial statements prepared on the basis of a single set of financial reporting requirements.

At the same time, we are aware that capital-raising does not stop at the European frontiers. Our companies may also wish to raise finance on international capital markets, on Chinese markets and others. So a solution was sought to enhance comparability within the European market which would also mirror developments in internationally accepted best practice. International Financial Reporting Standards were seen as the most appropriate benchmark for such a single set of financial reporting requirements.

Now, effort is still required to ensure that the benefits of having a single set of standards across Europe are obtained. To this end it is important that issues regarding consistent application, interpretation and enforcement are addressed as they come to light. To allow the financial market to function effectively, regulatory and supervisory mechanisms need to be strengthened and joined-up across Member States. This also implies further enhancing global cooperation in the financial field – across the Atlantic as well as the Pacific Ocean.

Like I said, the IAS Regulation envisaged the idea of globally accepted standards and since its adoption, this idea has developed, with movements towards global convergence across the globe.

Supervisory convergence

The IAS/IFRS requirement is an important step to simplify the lives of businessmen and financiers. Their time should be spent largely on business, not complying with reams of regulation – filling in bureaucratic forms. I think there is broad consensus that not only the rules and standards should converge, but also supervisory practices – in Europe and globally. A real European – and ultimately global - supervisory culture should develop, with mutual trust and confidence.

Another big challenge for the coming years is to make sure that the benefits of integration – be it at national, European or global level – are passed through to the final consumer. Not only the big global financial players should benefit, but especially all the citizens in Europe, China and other parts of the world. As only then support for integration will be durable.

Conclusion

Ladies and gentlemen,

In my vision, financial market integration is the best way to stimulate competition and therefore improve the competitiveness of an economy in a global setting.

European financial markets have come a long way over the last seven years in terms of integration, due to the measures contained in the Financial Services Action Plan, the introduction of the euro and of course also more global technological developments, like the increased access to Internet. Today, the European financial markets are open and reliable and the balance between economic freedom and investor protection is right.

Our companies are now better able to exploit opportunities, be it in Europe or elsewhere. Therefore, the focus of the European Commission's strategy over the next few years is to enhance global cooperation and convergence to international standards in as many different areas as possible. My presence in China is a testimony of this commitment.

The discussions I had so far with my Chinese counterparts and with representatives of the industry have reinforced my conviction that Europe and China cannot afford not to talk to each other. When we are faced with so many common challenges, we can, and should, learn a lot from each other's experience.

The major global players should be able to work together, compete fairly with each other without being hindered by artificial fragmentation. Today, it is in our remit to start defining the future world standards. It is in our remit to create the best financial framework in the world in the coming years. It is in our remit to deliver the tangible benefits that the average citizen can expect from politicians and industry leaders.

Thank you.