

Financial Markets in the Euro Area: Realising the Full Benefits of Integration

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Abstract

This paper explores the role of financial integration in supporting economic adjustment and convergence under monetary union. It discusses experience since the inception of EMU, based in part on research with a Dynamic Stochastic General Equilibrium (DSGE) model of the euro area. It finds that financial market developments, including declines in risk premia and increases in financial integration, have played a larger role than anticipated when EMU was created. Drawing on this experience, it underscores the importance of well-designed macroeconomic and structural policies in ensuring that the full potential gains of financial integration are tapped, and it links these lessons to the opportunities and challenges facing Cyprus in the immediate aftermath of its adoption of the euro.

Keywords: Euro Area, Monetary Union, EMU, Financial Integration, Financial Liberalisation, Financial Services Action Plan.