

Euro area Financial Market Conditions

**Policy research meeting on financial
markets and institutions**

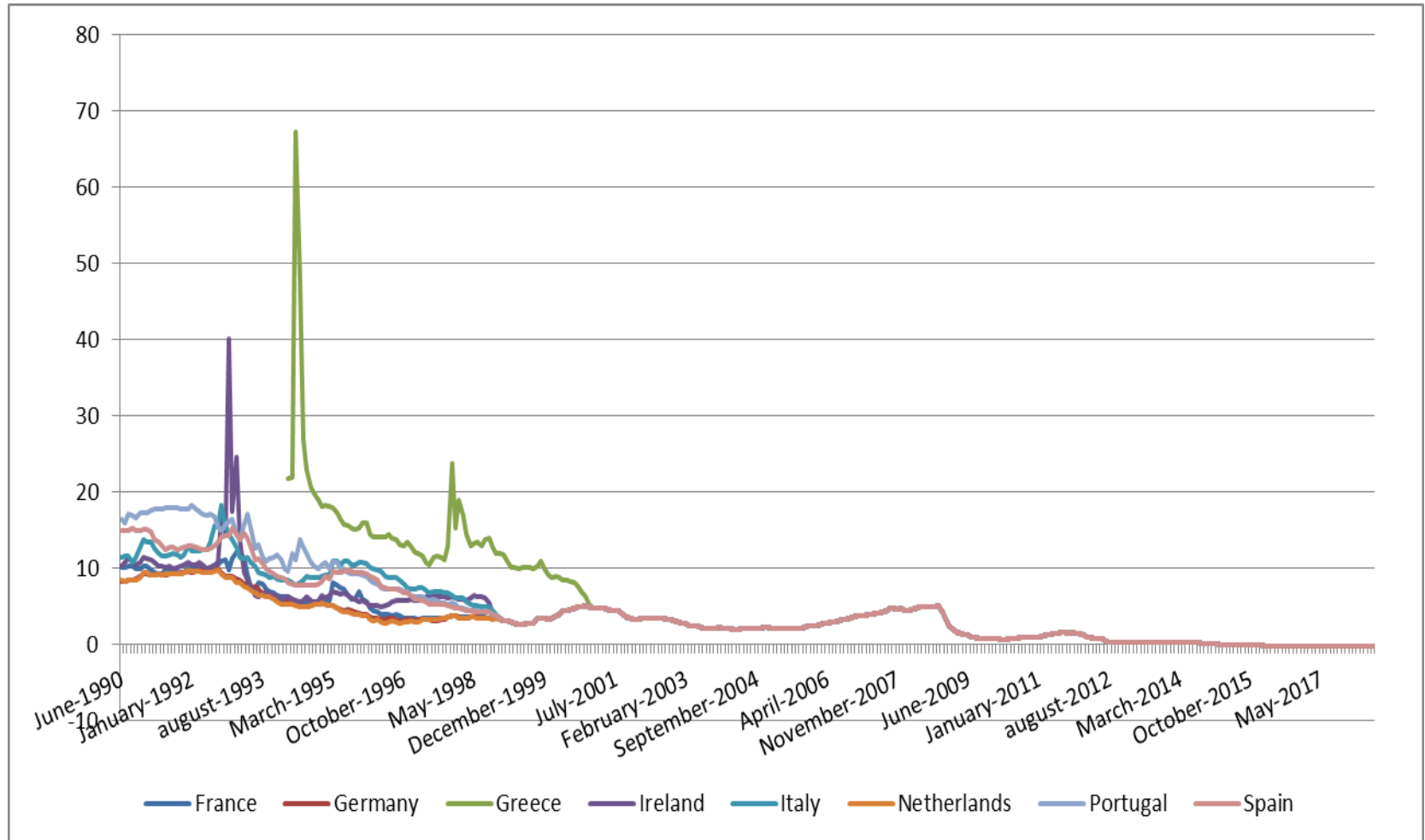
4 October 2018

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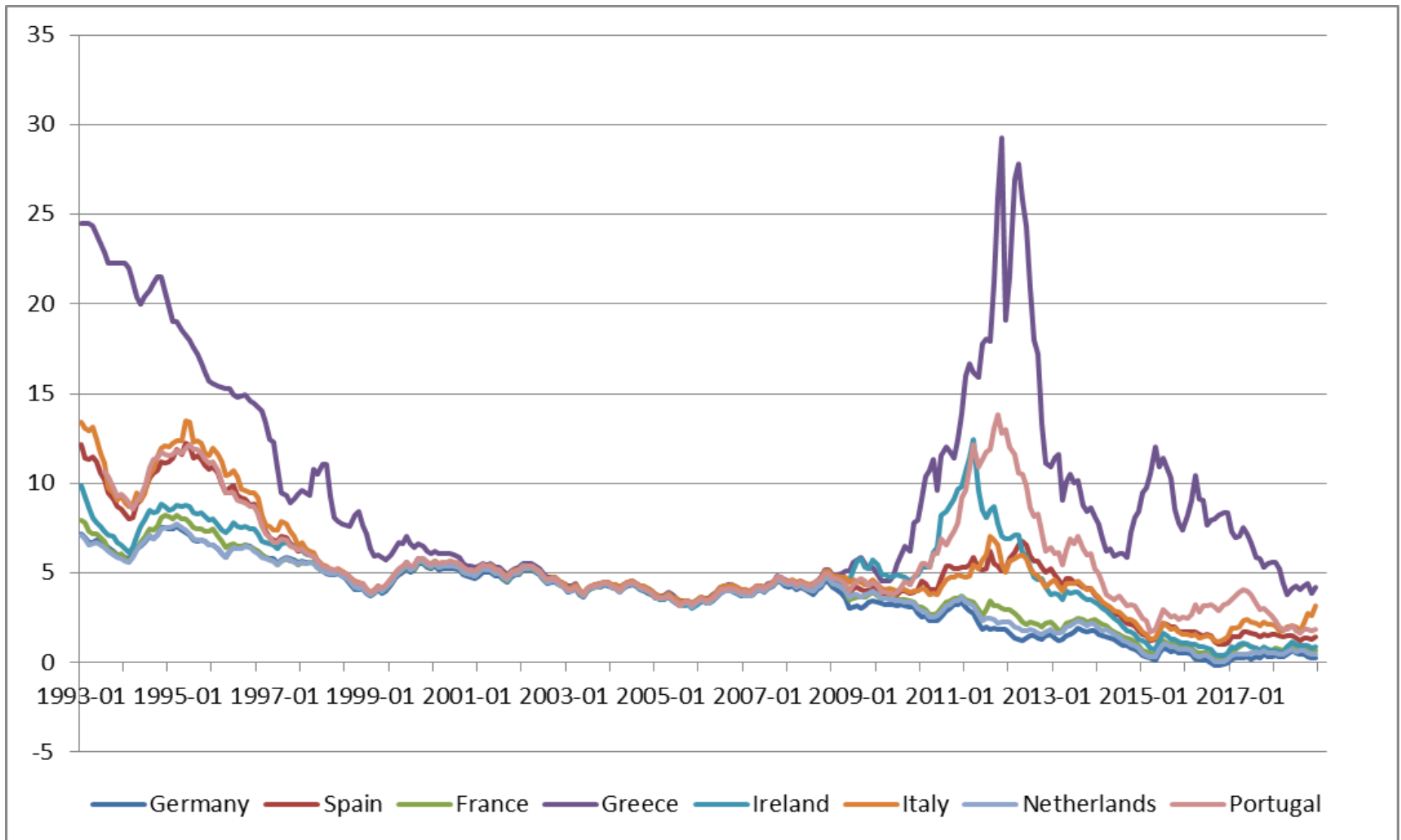
Introduction

- **In (continental) Europe, the economic activity is mostly financed by banks (80% bank based – 20% market based)**
- **Market based finance mostly consists in debt issuance rather than capital**
- **As a consequence, financial market conditions are primarily determined by interest rates in continental Europe**

Nominal convergence at play: Short-term nominal interest rates

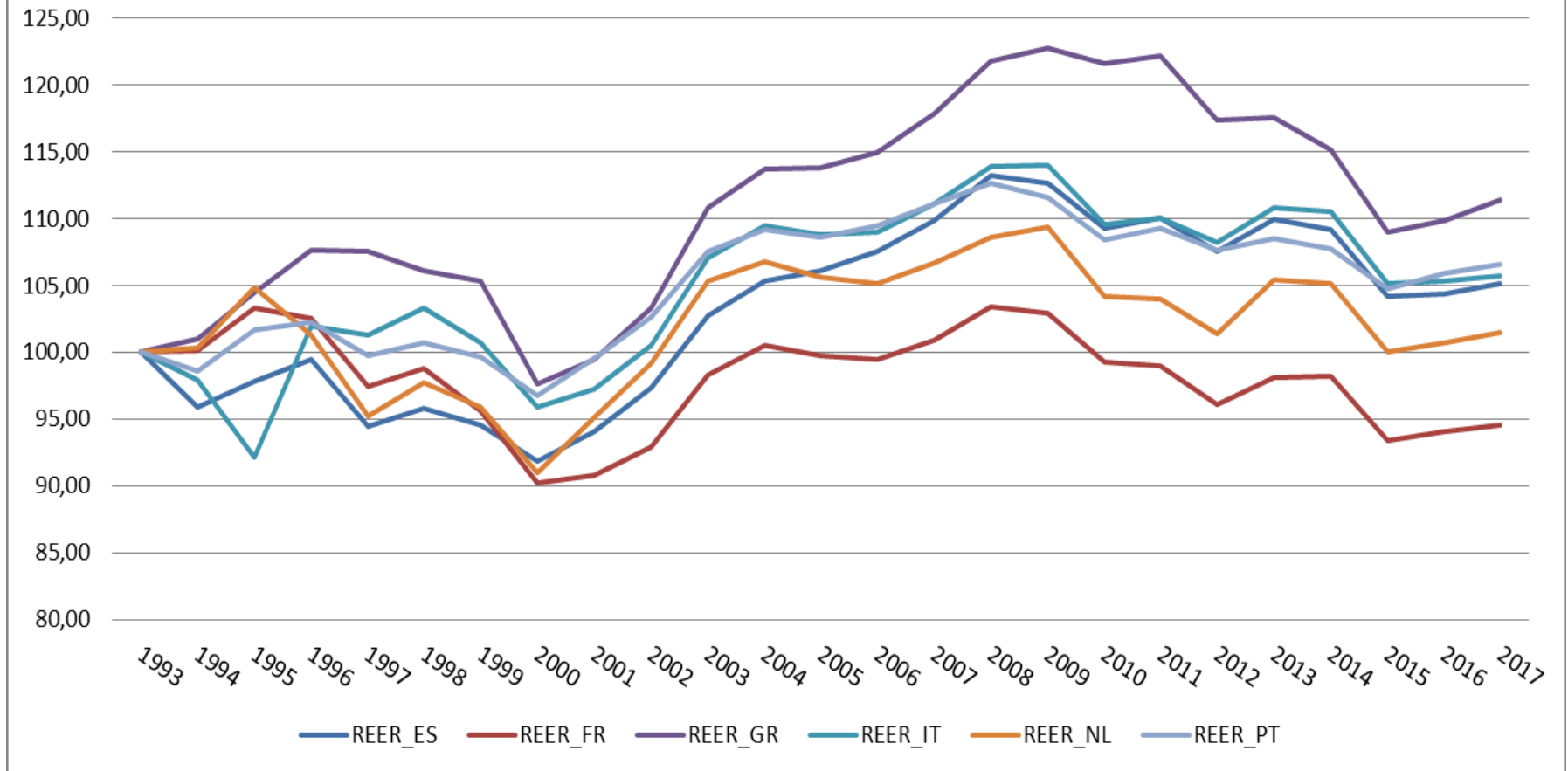


Nominal convergence at play: Long-term nominal interest rates



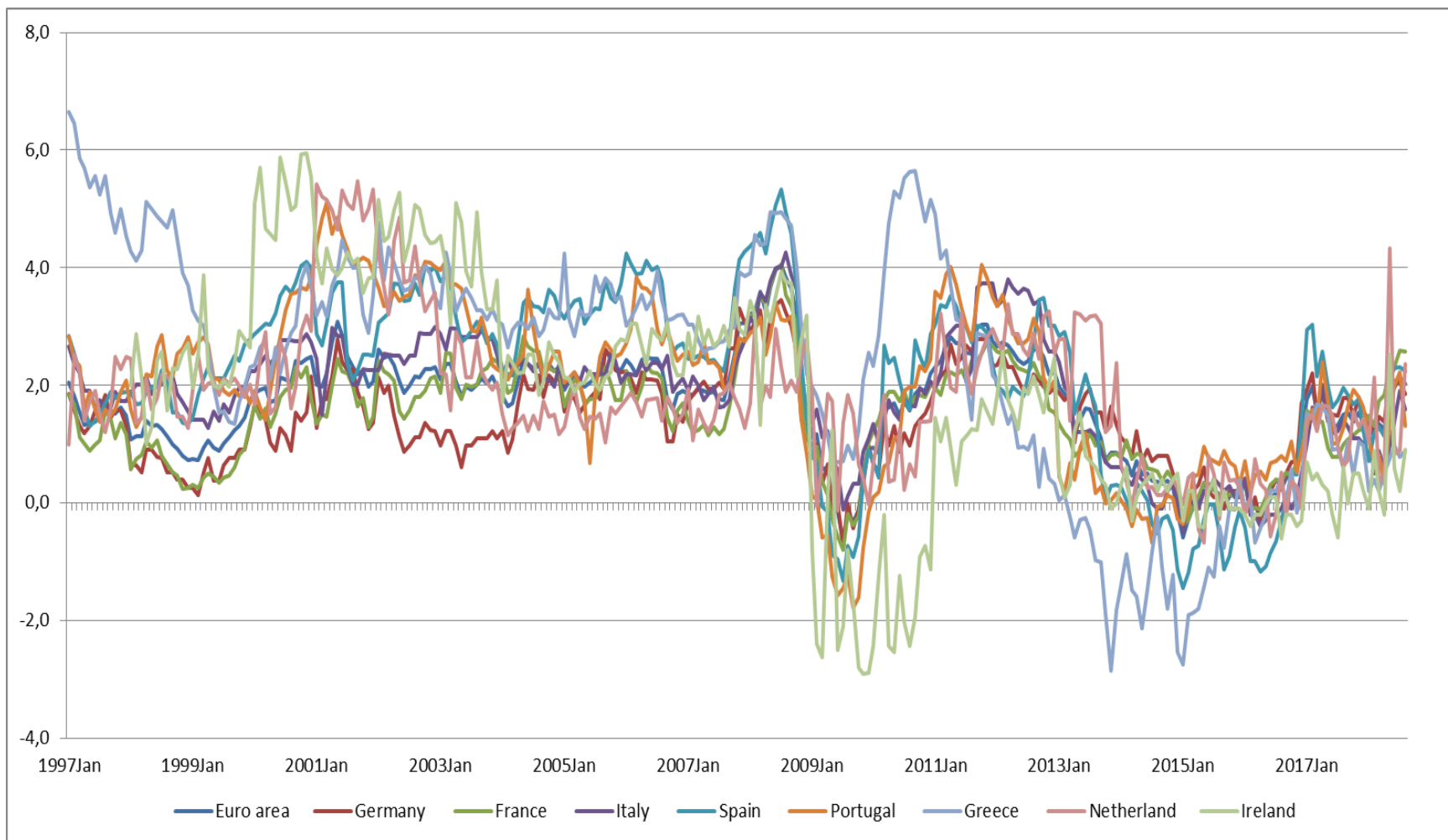
but a lack of real convergence

Real Effective Exchange Rates

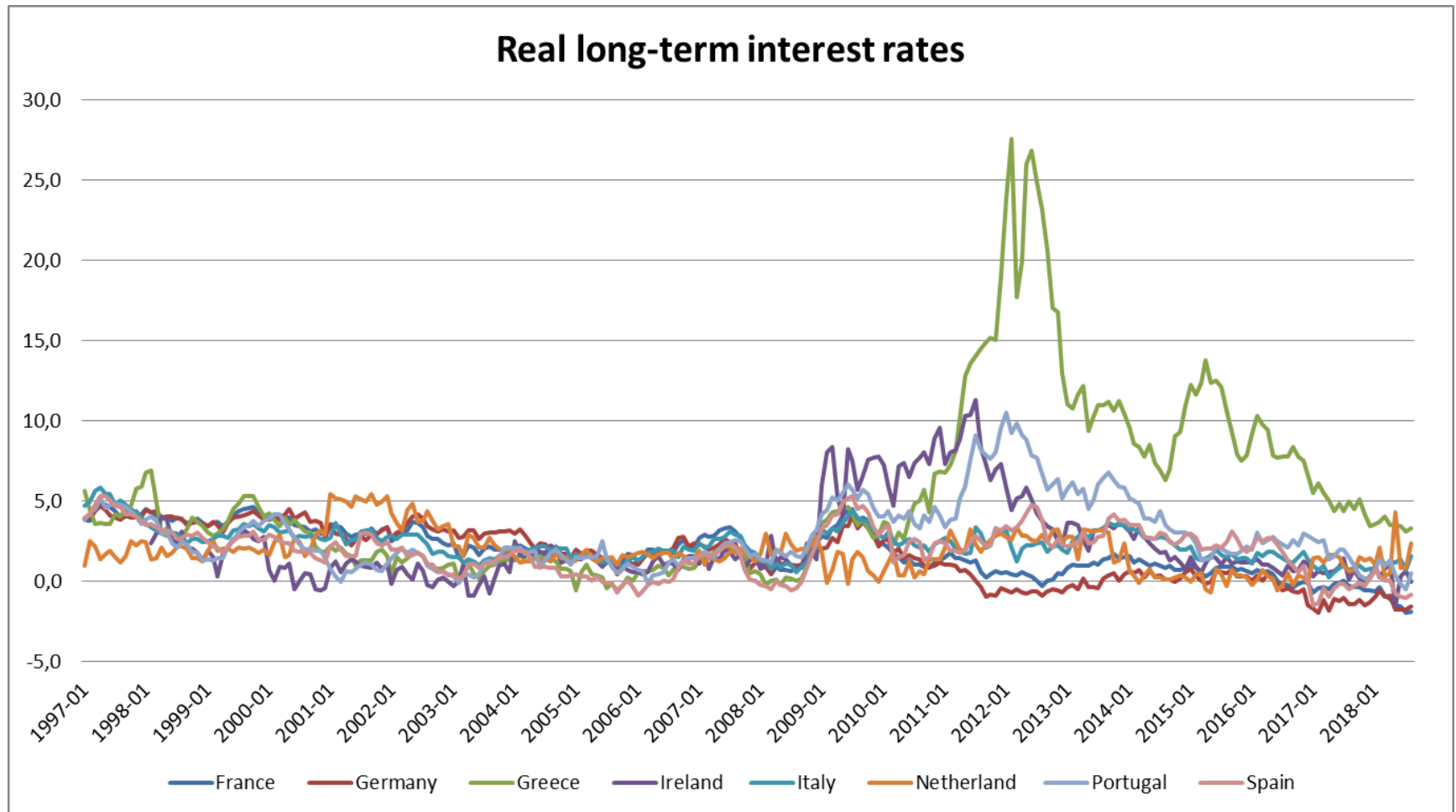


Persistent inflation differentials

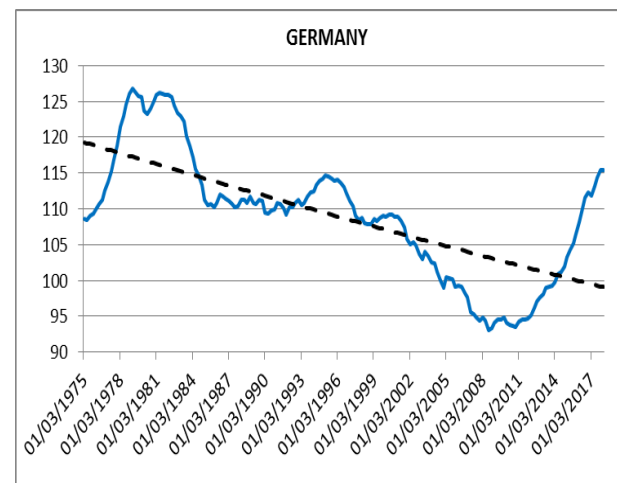
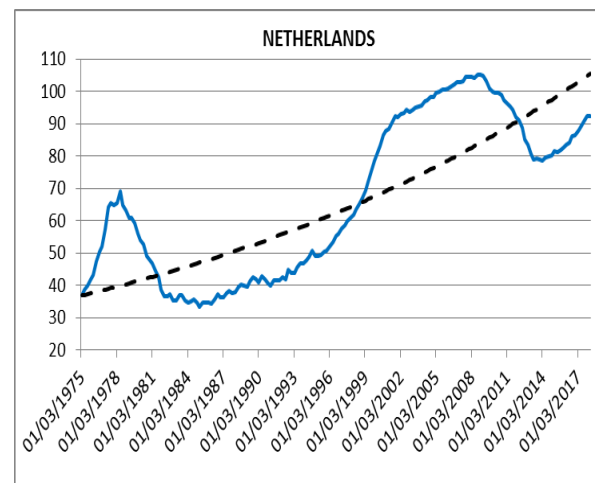
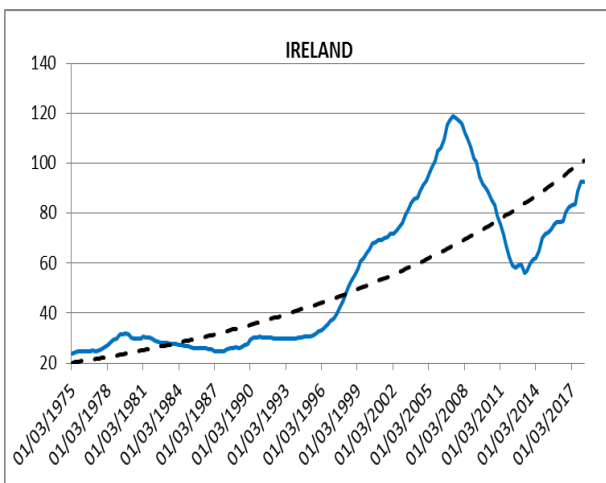
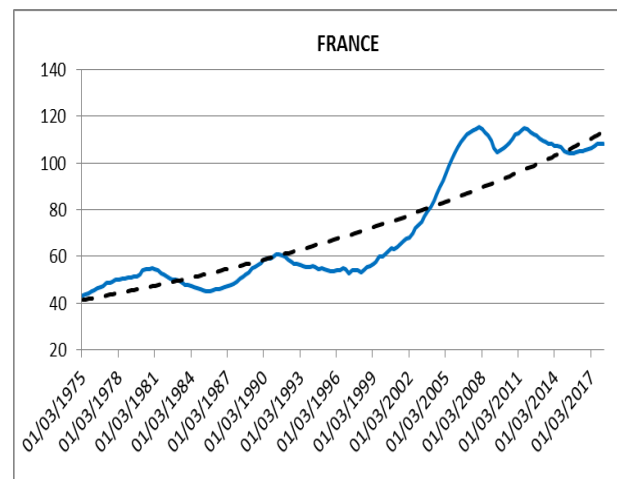
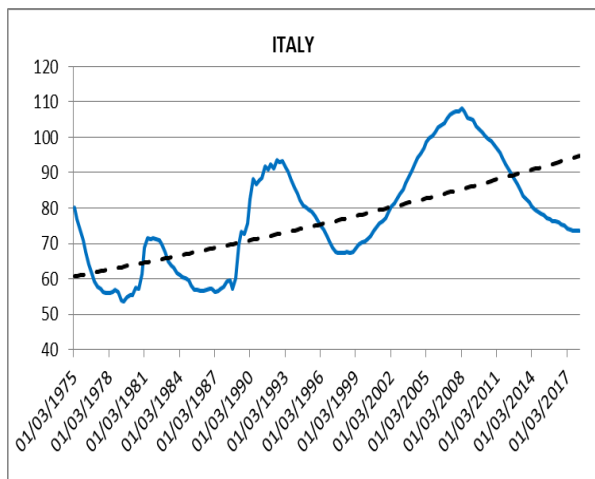
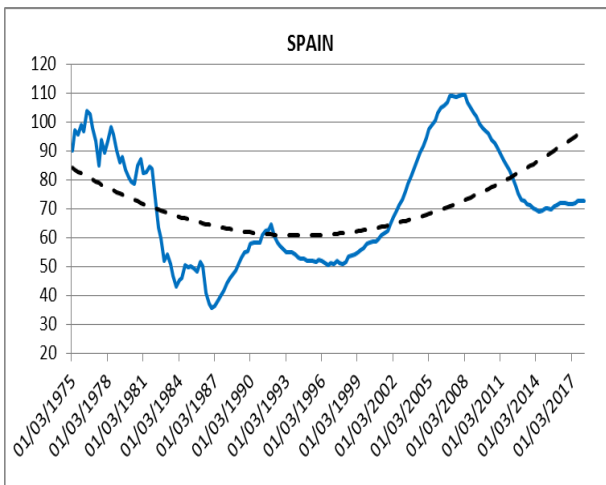
(HICP inflation, y-o-y,%)



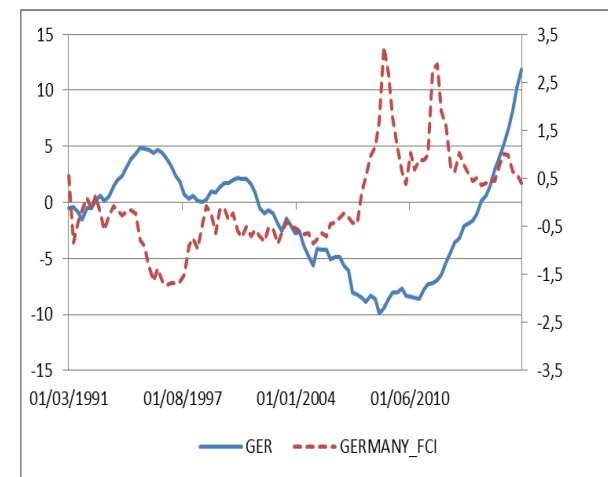
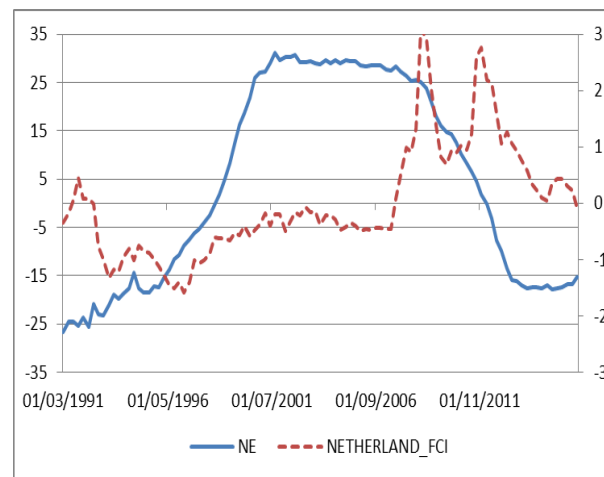
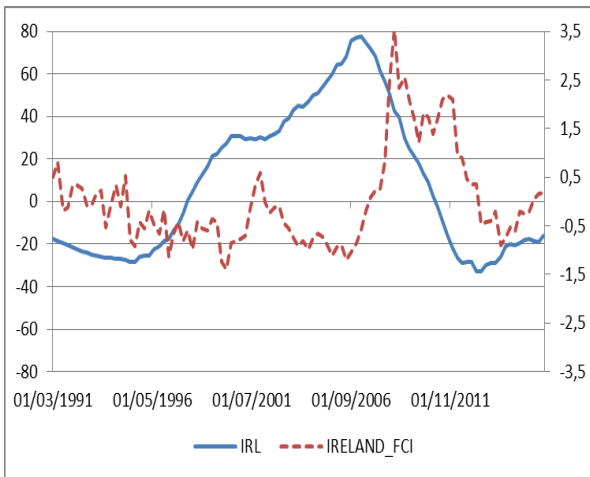
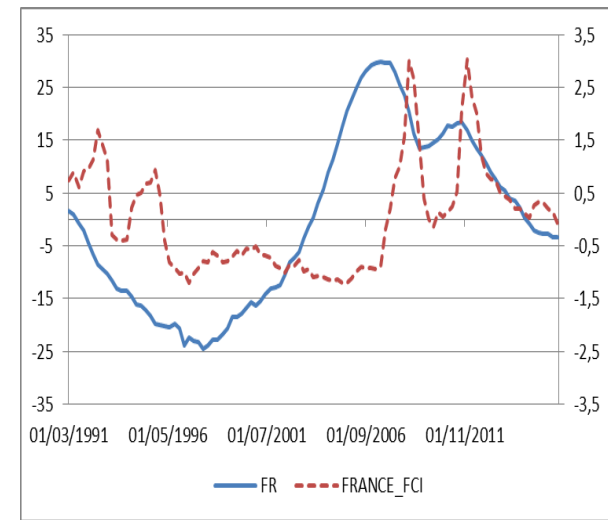
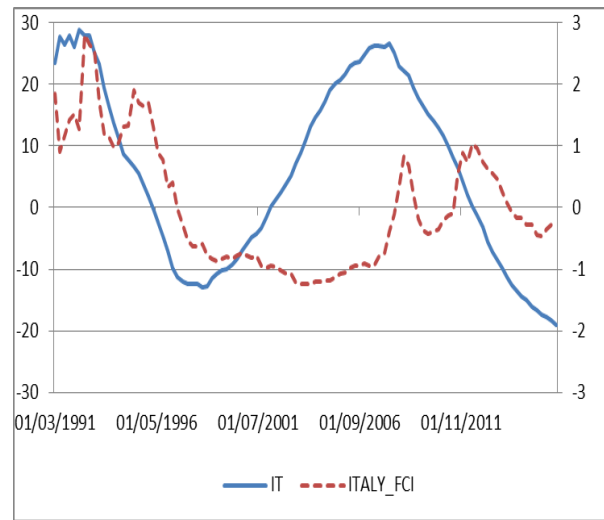
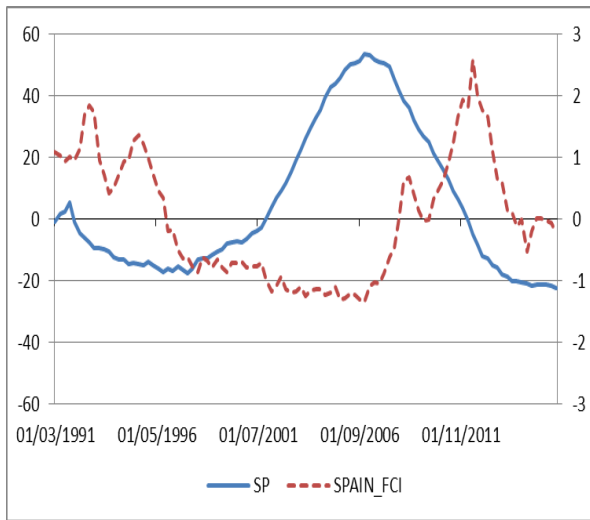
Heterogeneous real financial conditions



Built-up of financial imbalances on housing markets



Too easy FCI have usually been linked with the built-up of financial imbalances



Conclusion

As experienced in the past, the current situation is characterized by:

- **too easy for some but too tight for others financial market conditions**
- **Still the absence of real convergence and the lack of fiscal discipline**

By contrast, now, some macroprudential instruments exist and can be activated to prevent the built-up of some imbalances

- **But may have not been activated yet**
- **May not be effective to address:**
 - Resurgence of tensions and redenomination risks
 - Political uncertainty
 - Risk of reappraisal in risk premia