

## 6. Banking

Two issues that emerge are terms of access to the interbank clearing system associated with the introduction of the euro, and the outlook for bank mergers and consolidation in Europe.

A difference of opinion exists between the Bank of England and several other European central banks over access to the new TARGET system for interbank clearing in euros. The Bank of England wants access for itself on the same basis as other central banks, while other Europeans want to restrict the terms of access<sup>10</sup> for non-EMU participants. These arrangements may have the potential to influence the competitive positions of London, Paris, and Frankfurt as financial centres. The issue also has the potential to delay some technical preparations for EMU and harden attitudes, particularly in UK banking and official circles, against EMU. The Governor of the Bank of England has expressed his displeasure with the idea of singling out the UK this way. However if London-based clearing in euros was permitted and London retained its competitive advantage in financial services but the UK stayed out of EMU, one might see a significant part of the euro money market being cleared "offshore" in London.

The successful implementation of EMU will bring into sharper focus the differing regulatory regimes for banks as well as securities markets in Europe. The area is ripe for bank mergers and consolidations, which have already taken place in London (eg. Deutsche Bank's purchase of Morgan Grenfell). The removal of restrictions on U.S. interstate banking led to a wave of consolidations and mergers there. In Europe, two developments will foster financial sector consolidation: a Europe-wide approach to bank regulation, and withdrawal of the state from bank ownership, particularly in France and Italy.

### 4.4 Implications for Macroeconomic Co-ordination

EMU will have important implications for international monetary co-ordination. As a major new EU policy-making institution with clear independence from governments, the ECB could quickly become a powerful spokesman for European monetary and financial interests.

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<sup>10</sup>The controversy is about access to intra-day liquidity. The Bank of England is setting up facilities to clear euros on its books whether or not the UK participates in EMU. Part of the euro interbank market will reside therefore in London. There will be times when with real time settlement within the day, the Bank of England will want clearing banks to cover a euro overdraft position with funds from elsewhere in the clearing system. Since the Bank of England will not be an issuer of euros, it cannot provide overdraft coverage in euros through its own balance sheet, as a central bank can do with its own currency. It is access to this liquidity which is the issue - French and German central banks reportedly are insisting that, while all EU central banks can have access to the clearing, that liquidity within the day should be provided only to EMU participants to preserve monetary control. The Bank of England argues that monetary control is not significantly jeopardized and that safeguards against systemic risks to the system will be enhanced through its (and other non-EMU central banks') participation.