

Brexit & the European Financial System

Nicolas Véron
March 23, 2017



Baseline Scenario

- UK exit 2019, from EU & single market
- Orderly transition with withdrawal agreement
- Firms relocate client-facing functions to EU27
- EU insists on some critical functions onshore
- City decline in relative & absolute terms
- No single substitute in the EU27

Where Will City Financiers Go?



Based on early indications (public & not)

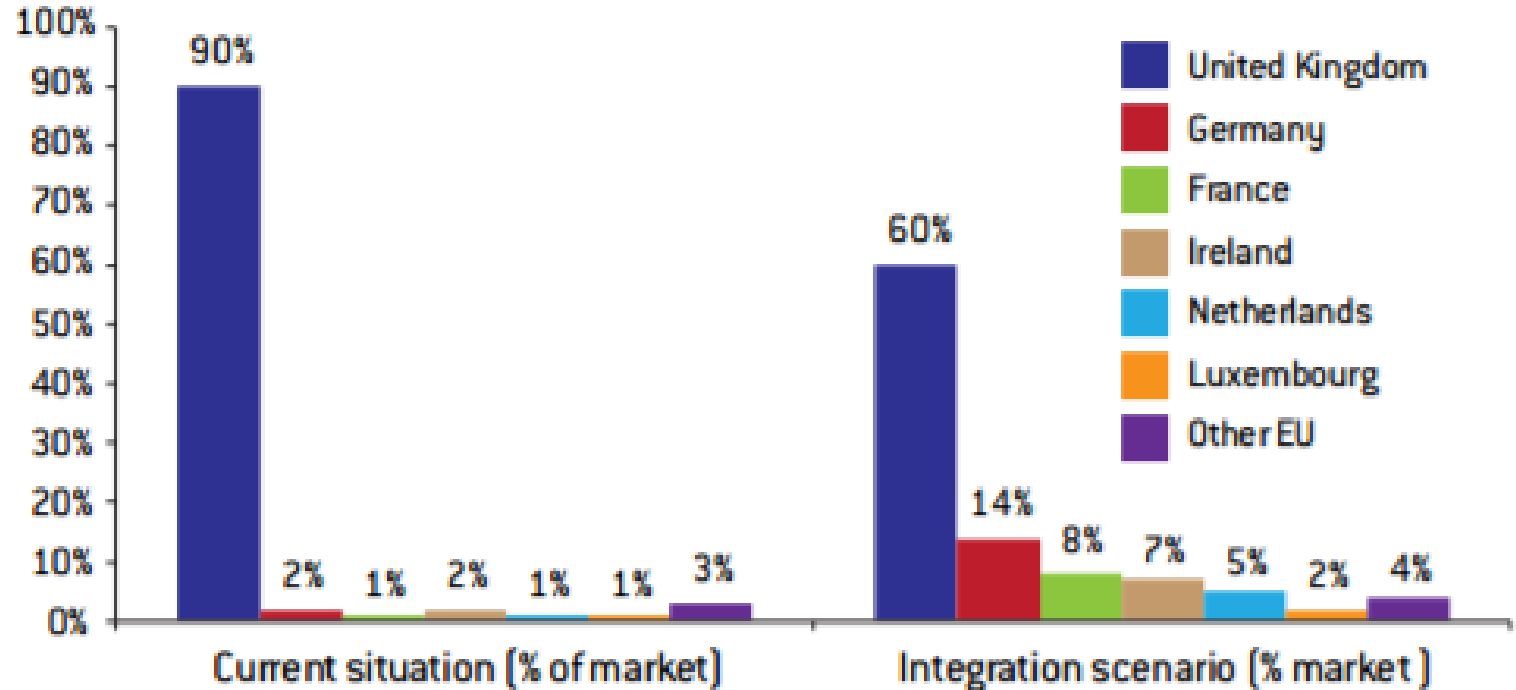
- Best placed: Frankfurt, Dublin, Luxembourg
- Below potential: Paris, Brussels, Amsterdam
- Peripheral: Madrid, Milan, Vienna, Nordics

Possibly patterns will evolve over time



One Plausible Future

POTENTIAL MIGRATION OF WHOLESALE MARKETS FROM LONDON TO EU27



Source: Sapir, Schoenmaker & Véron (2017)



Policy Challenges for EU27

- EU27 non-bank/capital market integration
 - “Capital Markets Union 2.0”
 - Role, governance, and funding of ESMA
- A more complete banking union
- Openness to third countries, including UK
 - Key test on financial infrastructure



International Clearing Houses

- Made critical by G20 derivatives reform
- UK-based CCPs serve EU27 and US
- US has direct supervisory access
- EU “equivalence” approach unsuited

- “Location policy” costly, partly mercantilist
- Direct access by EU authorities preferable
- Requires changes in EU legislation + UK



Global Engagement

- EU was champion of global financial standards during “Great Moderation”
 - Alignment between EU and global aims
- Its incentives have changed since
 - EU institutional integration, Brexit, broadening of global bodies’ membership
- But EU interest remains in global standards
 - Need for EU leadership if US disengagement
 - Compliance + streamlining of representation