A Concept For
An EBRD-World Bank Joint-Venture
With EU and Italy's Support

Bucharest, Governors' Club
May 23, 2003

Convergence

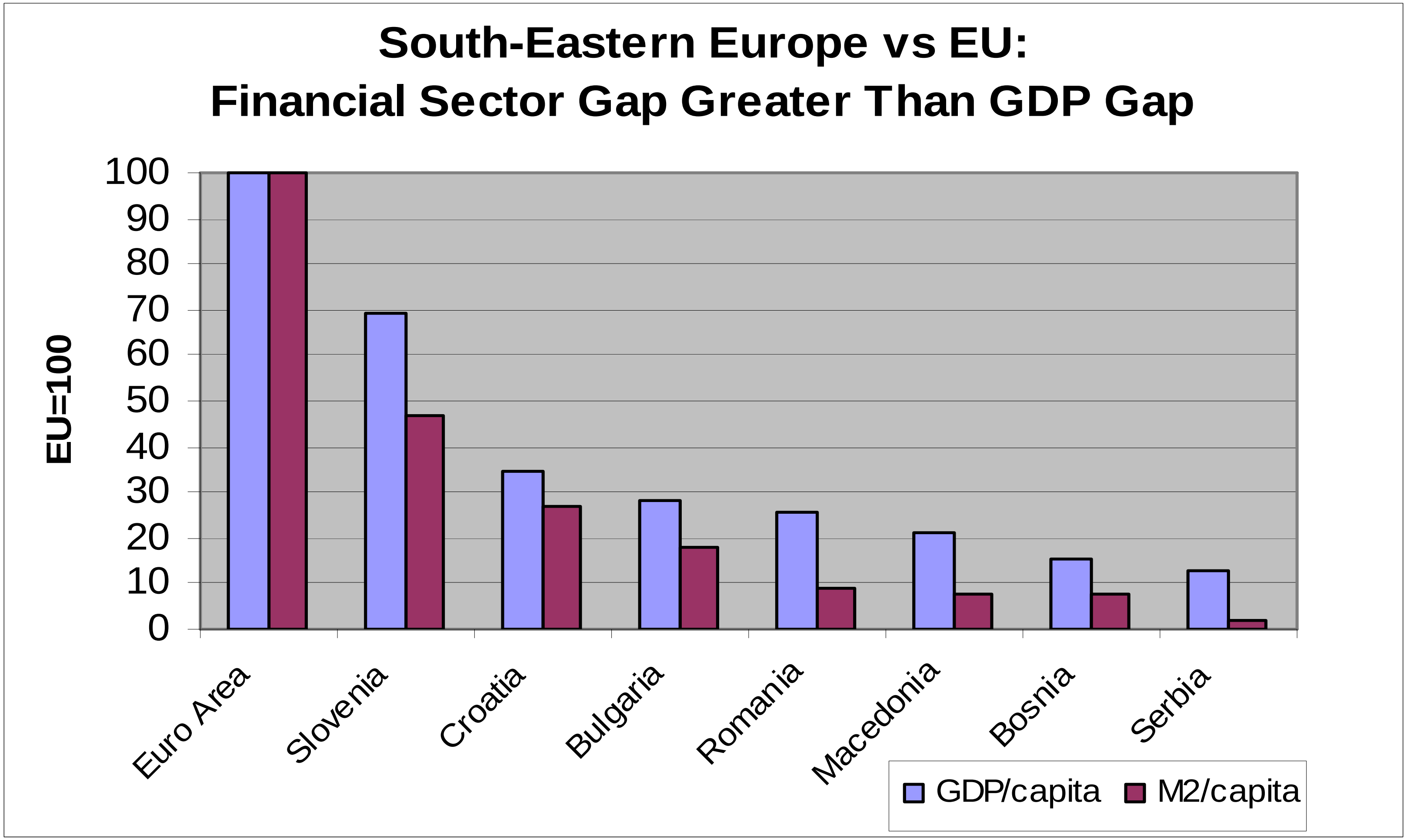
An initiative to strengthen the financial sector through a structured public-private dialogue

South-Eastern Europe

Bulgaria, Romania

Albania, Bosnia-H, Croatia, Macedonia, Moldova, Serbia and Montenegro

The Context



Financial sector is key contributor to economic growth

The Issue

- Financial sectors have been overhauled in the region
  - Right incentives now: privatization, foreign entry and improving prudential framework

•But, large "fine-tuning" reform agenda still outstanding

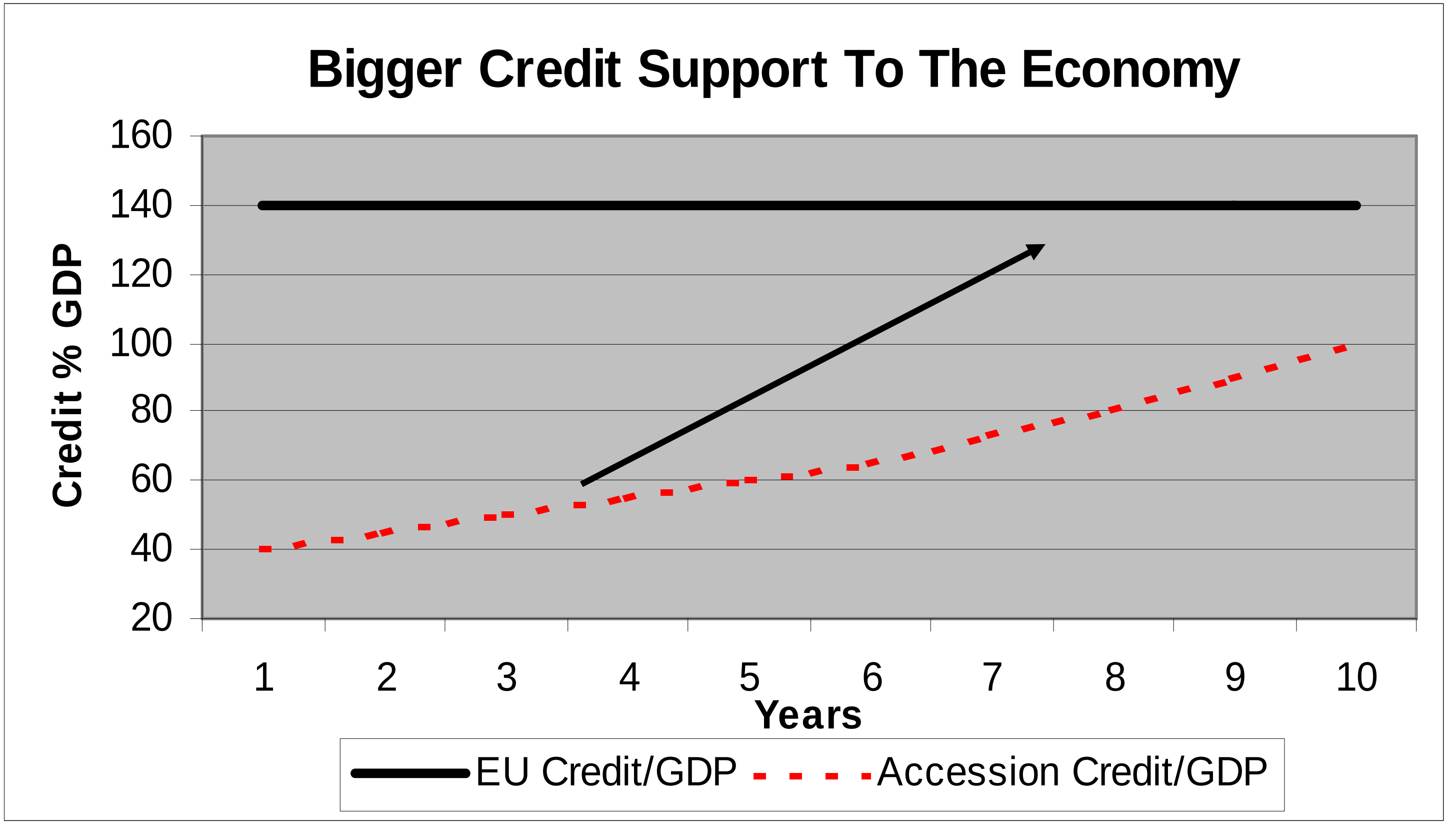
(incl. adoption of EU regulatory framework for several countries)

- Legal infrastructure
- Banking efficiency and safety
- Capital market development

•Indeed, "It is the last mile that counts"

- …And the trickiest to complete…
- But also with large potential benefits (few powerful incumbents)
- This is where *Convergence* fits…

The Vision



"The traditional role of the financial sector in underpinning investment and realizing growth potential through its intermediation and governance functions is still very limited in most EU accession countries". **Eugenio Domingo Solans, ECB Executive Board Member**

The Obstacles

- World Bank/IMF FSAPs and EBRD discussions with market participants highlight several "teething" problems:
  - Collateral registration and foreclosure procedures
  - Credit bureaux
  - "Business-unfriendly" bank supervision regulations
  - Deposit insurance arrangements
  - VAT issues
  - Ineffective securities market regulations
  - Interface between bank and securities market regulations
  - Harmonization of EU accession requirements in local legislation

Result: Finance Does Not Flow Efficiently – Especially to SMEs

A Useful Benchmark:
EU Single Financial Market Development

Vision	"The EU has no divine right to the benefits of an integrated financial market. It has to capture those benefits. The primary beneficiaries will be European SMEs. All actors, governments, regulators, market participants and consumers will need to adapt their positions in order to move forward". – *Alexandre Lamfalussy*
Method	"Consult, beforehand, in an open, transparent and systematic way with market participants and end-users (issuers and consumers). Where necessary, open hearings should be held. A summary of the consultation process undertaken should be made available when the final proposal is made". – *The Lamfalussy Wise Men Report*
Instrument	"The EU Commission establishes an independent advisory group, CESR, for the preparation of draft implementing measures. Before transmitting its opinion to the Commission, CESR shall consult extensively and at an early stage with market participants, consumers and end-users in an open and transparent matter." - *EU Commission Decision on Lamfalussy Process*

Why Public-Private Cooperation?
The Conceptual Framework

- "It is crucial to be aware that market-led progress does require co-operation among economic (public and private) agents. The driver of co-operation should be, as much as possible, moved by the private sector, i.e. by an enlightened perception of the private interest. But we cannot be blind to the fact that the necessary co-operation among private market participants does not materialize unless public authorities play an important role in promoting it".

Tommaso Padoa-Schioppa, Executive Board Member, European Central Bank

- "Where public policy issues were involved, we established a tradition of extensive consultation right across the relevant sections of the market. We recognized early on that where intervention was judged to be necessary – in the interest of market transparency or of prudential or behavioral conduct – it needed to be informed by those who properly understood the subtleties of the market if we were to reduce the risk of unforeseen consequences which could either frustrate the purpose of the intervention or unnecessarily obstruct market innovation. In some instances this approach involved encouraging the market itself to address the particular issue in question as a preferable alternative to official action." **Sir Edward George, Governor, Bank of England**

EBRD and World Bank Can Help Authorities Engage With Market Participants

International Institutions

Convergence

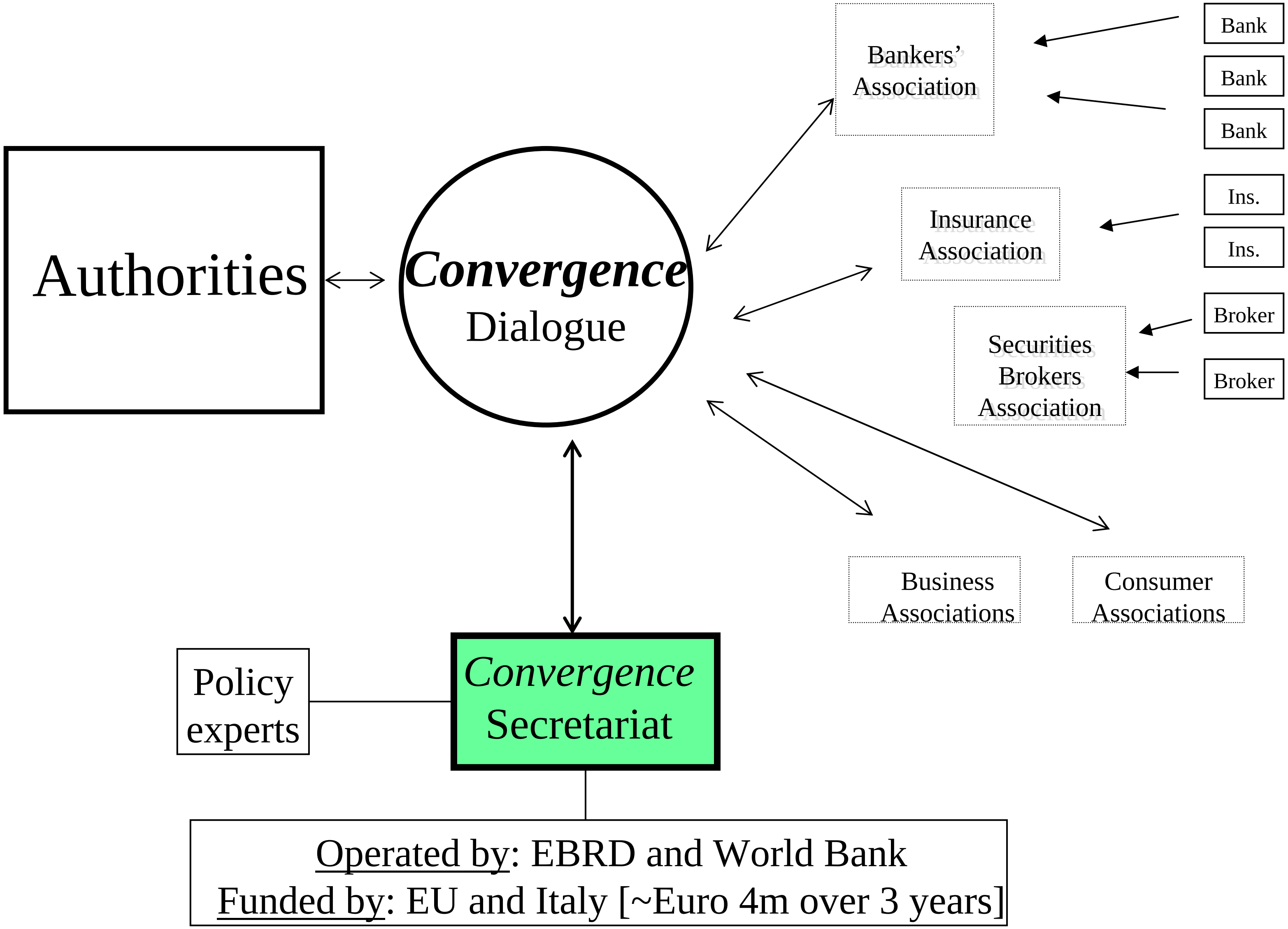
- To help national authorities organize private sector dialogue
  - Creating appropriate space and comfort
- To provide strategic perspectives
- To support dialogue with policy analysis, knowledge sharing and training resources
  - Helping consensus-building among market participants and with authorities
- To act as an honest broker between the parties when necessary
  - Providing independent technical opinions

Private Sector

Market Participants

- To identify issues of concern
  - Biggest market growth impact
  - Likely to lead to early government action
  - Building consensus among members
- To organize working groups
  - Strategic result orientation
- To engage with authorities constructively
  - With a public good focus

Convergence



What Will *Convergence* Do?

A Country-by-Country Approach

1^{st} Step	2nd Step	3rd Step
It will identify residual reform needs through a public-private brainstorming on financial sector development issues	It will prepare background studies on reform options ➢ In full and open consultations with authorities, market participants and users' associations	It will deliver final recommendation to authorities ➢Goal: To prepare reform measures at sustained pace and ready for smooth implementation

By using experts and organizing workshops

Convergence

Expected Benefits

Governments

- The system may grow faster by drawing on the energy and building on the incentives of market participants
  - *Convergence* will help authorities to include market participants' views on policy options under consideration as well as assess their reactions to reform suggestions
- The system may also become more stable, as market participants may align more accurately their incentives to the goals of national authorities
- The system may grow more harmoniously as *Convergence* will help various financial sector authorities coordinate their policy actions with financial sector, business and consumer associations

Market Participants

- They may be able to accelerate their business expansion plans
  - The authorities' long–term plans are clearer to them
  - They have greater comfort that their regulatory risk concerns may be taken into constructive account going forward
- They may operate within a more efficient financial infrastructure
  - Achieved more quickly through effective co-operation among themselves and with authorities
- New entrants may join with new products and in new segments
  - A result of a good investment climate in the financial sector

Beyond Advice -- *Convergence* Will Help Authorities Implement Concrete Reforms

Conclusion

Convergence will help the countries (authorities and citizens) reap the public good benefits of the new ownership incentives that have changed the financial sector landscape in South-Eastern Europe.

If properly harnessed, these incentives will have a powerful effect on the pace and depth of financial sector development, accelerating economic growth and personal income convergence with the EU.

Convergence will catalyze these positive forces for quicker results and a lasting impact on societies.