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Editorial

While Building Europe ...

„And the Goat shall bear upon him all their iniquities unto a Land not inhabited.“ (Leviticus 16:22). In this manner, the goat that departs – the (e)scape goat – is blamed and punished for the crimes or sufferings of others. The usefulness of such an animal should not escape a reformer bent on changing the French economy but expecting some unavoidable suffering along the way. Thus, it is easy to understand that French presidential candidates Ségolène Royal and Nicolas Sarkozy repeatedly pointed fingers at the European Central Bank's "euro fort" policy during the electoral campaign.

More recently, President Sarkozy has refrained from further calls for changing the ECB's policy mandate. The reactions of other European government officials, such as the German, Dutch and Austrian finance ministers, made clear that allies for such an initiative would be hard to find. Similarly, the lack of a reaction in foreign exchange markets emphasized market participants' belief that the ECB's independence will remain undisputed for now.

Central bankers taking a longer-term perspective, however, should not relax just yet. Any time a Euro area head of government will be faced with severe economic recession, the temptation will be there to blame overly restrictive interest rates set by the ECB and to call for changing its mandate. Of course, as long as other Euro area economies are performing satisfactorily and remain supportive of the ECB's independence, Euro area central bankers may easily brush this criticism aside. But what if the economic business cycle in the Euro area becomes more synchronized? Ironically, this is a long-held wish by central bankers who hope that the task of designing a common monetary policy would become easier in such an environment. However, synchronization would also bring along stronger political pressure on the ECB in bad economic times.

The Scapegoat by William Holman Hunt (1854)

To carry the thought experiment further let us think of a scenario such as the 1970s, when several adverse oil shocks lead to the Great Inflation in the United States, the United Kingdom and many other countries. Of course, the Great Inflation was no must. Germany, for example, was able to avoid the sustained rise in inflation. The Bundesbank was independent, determined to fight inflation, had a strategy, and, importantly, she could always rely on the inflation aversion of the German public.

While the ECB is similarly independent and committed by treaty to fight inflation, she cannot count on a single national public to stand behind it. As a supra-national institution she conducts monetary policy for a large number of nations whose people identify with the ECB's goal of price stability to very different degrees.

As Chancellor Merkel and President Sarkozy sit down to discuss how to ensure the long-term success of the European Union they may be well advised to guard against long-term vulnerabilities of its youngest institution.

Volker Wieland
CFS Director

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Comparing Market Quality Across Exchanges

February 2007

by CFS Program Director Erik Theissen (University of Bonn) and Maria Kasch-Haroutounian (University of Bonn)[1]

Exchanges around the world are facing massive structural change. Mergers (like the one between Euronext and the NYSE), attempted takeovers, acquisitions of minority stakes, and co-operations are rapidly changing the face of the industry. As more and more exchanges are organized in the form of for-profit firms (rather than as mutualized non-profit organizations), both the objectives of exchanges and the nature of competition are changing. At the same time, banks and institutional investors are putting pressure on exchange officials to decrease transaction costs. Recently a group of large investment banks has published plans to establish a pan-European trading platform for stocks. Such a move would obviously increase the pressure on exchanges to strive for efficiency.

Given that merging exchanges typically have different trading systems, after a merger the new entity will have to decide which trading system to adopt (or whether to retain both, which is likely to reduce the attainable cost reductions). Similarly, an independent exchange seeking cooperation with a partner should consider the quality of the trading system when choosing between potential partners. Finally, potential new entrants need to assess the quality of incumbent exchanges' trading systems before deciding to incur the fixed cost of entering the market.

Against this background, it is important to measure the quality of a trading system and to compare different trading systems. Liquidity is usually considered to be the most important measure of market quality, and the bid-ask spread is the most widely used measure of liquidity. In the present article, we use this established measure of market quality in order to address the issue of how to compare different trading systems.

A cross-exchange comparison of the bid-ask spread is complicated by the fact that the firms listed on different exchanges are not identical. As firm characteristics have a significant impact on liquidity, it is important to control for differing characteristics. There are two principal approaches to achieving this. The first is to analyze identical stocks traded in both markets, e.g. US stocks, which are also traded on Xetra, or German stocks, which are cross-listed on the New York Stock Exchange. Although this approach has been used in several empirical studies, it has a serious shortcoming. Liquidity is positively related to trading volume that, in turn, tends to be higher in a stock's home market. Thus, comparing the liquidity of a stock in its home market with liquidity in another market will most likely yield the result that liquidity is higher in the home market.

The second approach is the *matched samples* procedure which has been used extensively in the market microstructure literature, e.g. in order to compare the liquidity of the New York Stock Exchange to the liquidity of NASDAQ (e.g. Huang and Stoll 1996[2]). It is well known that the liquidity of a stock depends on characteristics such as its market capitalization, the trading volume, the volatility of the stock's return, and the price level of the stock. The matched sample procedure selects pairs of stocks from both markets in question such that the stocks are as similar as possible with respect to these matching criteria.

The idea is simple. If the matching procedure is successful (i.e., if the paired stocks are indeed similar with respect to the criteria used, and if the criteria capture all stock-specific characteristics that systematically affect liquidity), then differences in liquidity may indeed be traced back to the trading system.

An application: Xetra versus Euronext

The trading systems

In Continental Europe, there are currently two major players: Euronext group and Deutsche Börse. Euronext was formed in 2000 by a merger between the French Stock Exchange and the exchanges in Amsterdam and Brussels. Euronext has been operating a common trading platform since 2001. In 2002, the exchange in Lisbon and the London-based derivatives exchange LIFFE joined the Euronext group. In 2006, a merger between the New York Stock Exchange and Euronext was negotiated and approved by the shareholders' meetings of both exchanges.

Deutsche Börse AG operates the trading system Xetra that has also been adopted by the exchanges in Austria and Ireland. It has attempted mergers with both the London Stock Exchange and Euronext, but both attempts failed. Interestingly, during the negotiations with Euronext, Deutsche Börse offered to adopt Euronext's trading platform for the merged entity.

The two trading systems share many similarities. Most importantly, they are both anonymous electronic open limit order books, and both have liquidity providers (designated market makers referred to as animateurs as well as designated sponsors in Euronext and Xetra, respectively) for less liquid stocks. However, closer inspection reveals that there are a number of potentially important differences between the trading platforms. These concern, among other things, trading hours, the existence of intra-daily call auctions, and the rules for cross and block trades. Another potentially important point is that Xetra faces competition by the Frankfurt Stock Exchange and several small regional exchanges, whereas no such competition exists in France. Further, there are many more designated sponsors in Xetra than there are liquidity providers in Euronext. Finally, the minimum tick size is different between the two markets. It is always € 0.01 in Xetra (for stocks trading at prices above € 0.10). In Euronext, on the other hand, it is € 0.01 only for stocks trading at prices below € 50. It increases to € 0.05 for stocks with prices above € 50, to € 0.1 for stocks with prices above € 100, and to € 0.5 for stocks with prices above € 500.

Sample and Results

Both Deutsche Börse AG and Euronext provide CD-ROMs containing time-stamped data on bid and ask prices, transaction prices and trading volumes.

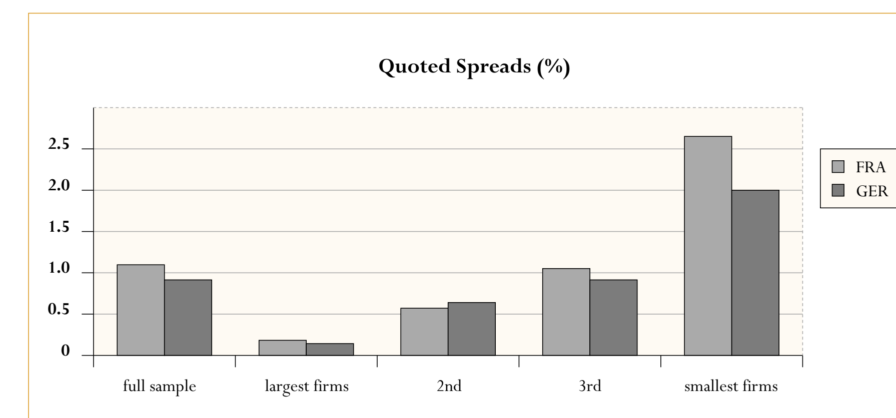

Figure 1

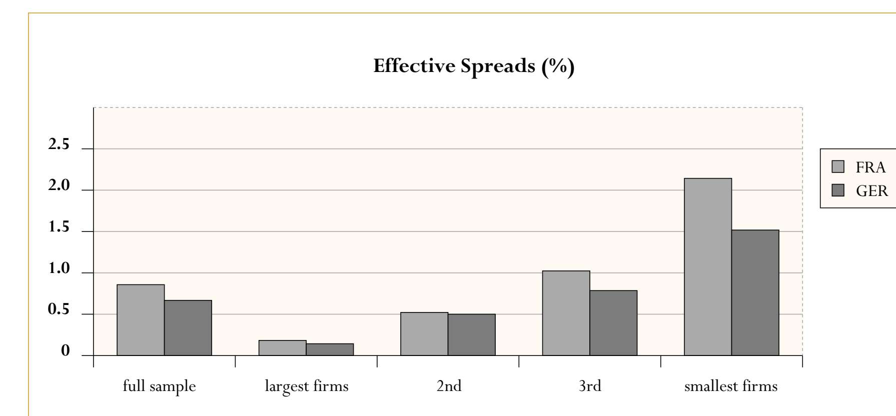

Figure 2

Since 2000, Erik Theissen has been Professor of Business Administration at the Department of Economics of the University of Bonn.

We use three months (65 trading days) of data (May, June and July 2002). During our sample period trading hours in Xetra were longer than those in Euronext. We restrict the analysis to those hours during which both markets are open.

We create matched samples of 40 pairs of stocks where each pair consists of one French stock traded on Euronext Paris and one German stock traded in Xetra. The matching criteria we use are market capitalization, price level, and volatility.

We use two measures of market quality: the percentage quoted spread and the percentage effective spread. The percentage quoted spread is simply the difference between the best ask and the best bid, expressed as a percentage of the quote midpoint. It changes whenever either the best bid or the best ask

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[2] Huang, R. and H. Stoll (1996): Dealer versus Auction Markets: A Paired Comparison of Execution Costs on NASDAQ and the NYSE', Journal of Financial Economics, Vol. 41, pp. 313-357.

changes. We record all quoted spreads and calculate weighted averages, where the weight is the time the spread was valid.

The percentage effective spread can only be measured when a transaction occurs. It is the absolute value of the difference between the transaction price and the quote midpoint, expressed as a percentage of the latter. The effective spread is obviously identical to the quoted spread at the time the transaction occurs. Average effective spreads, however, are typically smaller than average quoted spreads because transactions tend to be executed when the spread is low.

We report results for the full sample and for four groups of stocks sorted by market capitalization. Results for the quoted spread are shown in figure 1. The average quoted spread in Euronext is larger in the full sample and in three out of the four groups. The differences are statistically significant for the full sample and for groups 1, 3 and 4. The results thus indicate that quoted spreads in Xetra are, on average, lower than those in Euronext. Considering effective spreads rather than quoted spreads confirms this finding. Average effective spreads are lower in Xetra for the full sample and for all four groups of stocks, and with only one exception (group 2) the differences are statistically significant. Our analysis has shown that bid-ask spreads for comparable stocks are lower in Xetra than in Euronext. This result is robust to a variety of alternative specifications[3]. An important issue for future research would be to analyze which specific features of the trading systems actually cause these differences.

Erik Theissen's research and teaching interests are in the area of Market Microstructure, Experimental Economics and Empirical Finance. In 2006, he became CFS Program Director of the newly started Program Area "Economics of Exchanges" (XEcon). The purpose of the program is to advocate research in the area of trading and exchanges. This includes the analysis of market participants and their behavior, the analysis of market design and trading protocols, the analysis of "downstream services" like clearing and settlement, and the industrial economics of exchanges.

The research activities in the program will involve academics as well as practitioners and representatives of the regulatory authorities. Conferences, workshops and roundtable discussion will be organized in order to present the research results. Results will be published as CFS Working Paper as well as in academic and applied journals.

Current research projects are:
- Iceberg Orders
- A Comparison of the Market Efficiency and Market Quality of the New York Stock Exchange and Xetra
- The Industrial Economics of Exchanges - Clearing and Settlement

Christian Schlag (University of Frankfurt) and Joachim Grammig (University of Tübingen) are involved in the Project as CFS Fellows. Further collaborators to the Project are: Maria Kasch-Haroutounian (University of Bonn) and Oliver Wünsche (University of Tübingen).

[3]See Kasch-Haroutounian, M. and E. Theissen (2007): Competition Between Exchanges: Euronext versus Xetra, CFS Working Paper, forthcoming in European Financial Management

Accounting Systems and Financial Stability

by Franklin Allen (University of Pennsylvania and CFS)
Elena Carletti (Center for Financial Studies)

There has been an extensive debate in recent years on the advantages and disadvantages of moving towards a full mark-to-market accounting system for financial institutions such as banks and insurance companies. This debate was initiated with the move of the International Accounting Standards Board (IASB) and the US Financial Accounting Standards Board (FASB) to make changes in this direction as part of an attempt to standardize accounting standards across countries.

The debate has two opposing views. On the one hand, mark-to-market accounting has the advantage of reflecting the true (and relevant) value of the balance sheets of financial institutions and therefore of allowing investors and policy makers to better assess the risk profile of financial institutions. On the other hand, mark-to-market accounting is thought to lead to excessive and artificial volatility. As a consequence, under this accounting system the value of the balance sheets of financial institutions may be driven by short-term fluctuations in the market that do not reflect the value of the fundamentals and the long-term value of assets and liabilities.

The debate is complex as it features many different aspects. In our paper entitled "Mark-to-Market Accounting and Liquidity Pricing" we analyze the effects of using mark-to-market accounting when financial markets are illiquid. The main insight is that valuing the assets of financial institutions using market prices may not be beneficial in these circumstances. In times of financial crisis the interaction of institutions and markets can lead to situations where prices in illiquid markets do not reflect future payoffs but rather reflect the amount of cash available to buyers in the market. If mark-to-market accounting is used, then the volatility of asset prices directly affects the value of bank's assets. This can lead to contagion and force banks into insolvency even though they would be fully able to cover their commitments if they were allowed to continue until the assets mature. In contrast, if historic cost accounting is in use, this problem does not compromise the solvency of banks as it does not affect the accounting value of their assets. Thus, historical cost accounting may prevent crises which would occur under mark-to-market accounting.

The issue is illustrated by the case of the Long Term Capital Management (LTCM).

Franklin Allen

The Federal Reserve Bank of New York justified its action of facilitating a private sector bailout of LTCM by arguing that if the fund had been liquidated many prices in illiquid markets would have fallen and this would have caused further liquidations and so on in a downward spiral. Similarly, the results of our analysis illustrate how using accounting values based on market prices can significantly exacerbate the problem of contagion when markets are illiquid. The notion that market prices cannot be trusted to value assets in times of crisis also resembles the suggestion in Bagehot (1873) that in response to crises central banks should value bank collateral weighting panic and pre-panic prices as market prices are not accurate measure of values in those circumstances.

Elena Carletti: a Staff Portrait on page 29

Elena Carletti

The result that mark-to-market accounting can be distortionary and generate "artificial" contagion is obtained in a model with a banking sector and an insurance sector. Banks obtain funds from depositors who can withdraw on demand, and can invest in loans, short and long term assets. Insurance companies insure firms against the possibility of their machines being damaged, collect premiums and invest in short or long term assets to fund the costs of repairing the firm's machines.

In such a framework mark-to-market accounting generates contagion when three elements are present. First, there must be a source of systemic risk. For simplicity, we focus on the case where only the insurance sector faces such risk. In particular, the insurance companies find it optimal to insure firms when only a limited number of machines are damaged, and go bankrupt when a large number of machines are damaged. Second, there must be a source of contagion through market prices. This means that the banking and the insurance companies must hold at least one type of asset in common that is liquidated on a secondary market. We analyze the case where both the banks and the insurance companies hold the long term asset. Third, the market where the "common" asset is sold must be characterized by liquidity problems in that some investors must be provided with incentives to hold liquidity and liquidity pricing occurs. This implies that prices do not always represent the future value of the assets.

When the bad state of the economy is realized, the insurance companies go bankrupt and need to liquidate the long term asset. Market participants need to be given incentives to hold liquidity and purchase the assets. This means there must be states in which asset prices are „low“ so the participants can make a profit and cover the opportunity cost of holding

the short asset in the other states. The low prices are determined by the endogenous amount of liquidity in the market rather than the future earning power of the asset. If accounting values are based on historic cost, the low market prices do not lead to contagion. Banks are not affected by the low prices. They remain solvent and can continue operating until their assets mature.

In contrast, when assets are priced according to market values, low prices can cause a problem of contagion from the insurance sector to the banking sector. Even if banks would be solvent if they were allowed to continue, the current market value of their assets can be lower than the value of their liabilities. Banks are then declared insolvent by regulators and are forced to sell their long term assets. This worsens the illiquidity problem in the market and reduces prices even further. The overall effect of this contagion is to lower welfare compared to what would happen with accounting values based on historic costs. In some cases banks will structure their portfolios and deposit contracts to remain solvent so that contagion is avoided. However, even in this case there is a distortion.

This analysis has important implications for the debate on the optimal accounting system. In particular, it stresses the potential problems arising from the use of mark-to-market for securities traded in markets with scarce liquidity. Also, the analysis has important implications in the light of the recent accounting standards SFAS 157 and IAS 39. According to these standards, prices should be used to value assets if there is an active market with continuously available prices. Our analysis suggests that it is also necessary that the market be liquid in the sense that it can absorb abnormal volume without significant changes in prices.

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CFS*colloquium series*

Unternehmensverfassung im Wandel/ Corporate Governance in Transition

Corporate Governance in Unternehmen – Die wachsende Rolle institutioneller Anleger/ Corporate Governance in Companies – The Growing Role of Institutional Investors

In his speech at the CFScolloquium on 11 October 2006, Wolfgang Mansfeld, a member of the Managing Board of Union Asset Management Holding AG, presented his views on the topic "Corporate Governance in Companies – The Growing Role of Institutional Investors". In his opinion, this topic is important for two reasons. Firstly, active institutional investors make capital markets more efficient. And secondly, more active behavior may contribute to an increase in private investors' wealth. In this context, it has to be clarified what role institutional investors should play as shareholders and how they should exercise their shareholder rights.

Wolfgang Mansfeld

Mansfeld stated that a structural change has taken place on the capital markets over the last 15 years. The share of investors in a position to play an active role in the corporate government of the target company, in particular the share of institutional investors, has been growing rapidly. Today institutional investors hold a majority in many DAX-listed companies and can exert influence and defend their interests by exercising their voting rights in the shareholder meetings. According to Mansfeld, good corporate governance is primarily about shareholder value. Investors are interested in high returns on their investments and, therefore, good corporate governance exists when a company works in such a way that it serves the interests of its shareholders. This implies that there should be no room for a broad concept of stakeholder interests. He cited the notion of "Deutschland AG", arguing that in Germany both the self-interests of management and the influence exerted through workers' participation play too big a role.

While presenting his definition of good corporate governance, he spoke about a recent initiative by a leading stock exchange index provider, who intends to set up a corporate governance rating based on five criteria: the compensation system of the executive and non-executive directors, the quality of the stock option programs for the managers, shareholder rights and how they may be exercised, the structure of the board, and the audit process. Although this project is at an early stage, it nevertheless gives some indication of what constitutes good corporate governance.

In summary, it can be said that the influence of institutional investors has been growing and good corporate governance should primarily take the interests of shareholders into account. Having established this point, Mansfeld proceeded to focus on how institutional investors could influence corporate governance. In the past, they have played a mostly passive role by purchasing shares they regarded as promising and selling those deemed otherwise. Nowadays, their role has changed and institutional investors see themselves as shareholders who want to improve the company performance. Two mechanisms are used for this purpose. One way to exert influence is the so-called "one-to-one" or direct cooperation approach. Through a direct dialog, the management can present the company and the company's strategy and offer investors the opportunity to express their opinions and doubts. Mansfeld regards this method of cooperation to be of growing importance. A second, and more official approach, is to exercise share voting rights. The exercising of these rights derives from two distinct motives: On the one hand, institutional investors should attend shareholder meetings to exercise their voting rights in compliance with government regulation and self-regulation and, on the other hand, they should do so in order to fulfill their role as trustees of their clients' money.

Mansfeld supports the view that institutional investors should exercise their voting rights and that active shareholders contribute to more efficient capital markets. He also explicitly supports self-regulation, which is also the basis for the rules of conduct of the BVI - Bundesverband (Federal Association of) Investment und Asset Management e.V. However, institutional investors should verify carefully whether it is worth influencing the corporate governance of companies. Shareholder activism has to be conducted in accordance with the fiduciary obligations as regards clients, but should not be a goal in itself. He warns that a more active role on the part of institutional investors might be postulated by different interest groups. Institutional investors should be wary of becoming instruments for an array of socio-politically motivated engagement. Although important for society as a whole, efforts put into projects such as the Carbon Disclosure Project (an initiative to enforce companies to publish their pollutant emission) have to be justified in terms of higher returns for their clients, the private investors. At this point, Mansfeld cited research that shows that companies with a high corporate governance rating do not necessarily offer a better performance. Furthermore, limits have legally been set to determine the extent to which an investor may intervene in the actual management of a company. The EU Investment Directive serves as a formal framework in this respect.

Mansfeld presented the policy of Union Investment as an example of how these principles may be implemented in a concrete policy context. Since time and resource constraints make it impossible for Union Investment to exercise its voting rights at the shareholder meetings of every single company in which it has invested, the investment company picks the 200 largest companies in its portfolio. However, when it comes to the actual decision-making process, Union prefers to act in accordance with a catalog of general guidelines, rather than to make decisions case by case. This is a common approach to structuring the decision-making process among investment companies. The catalog contains the following principles. Firstly, it includes the principle of "one share one vote", voting against any proposals aimed at introducing different classes of shares. Secondly, the positions of Chief Executive and Chairman of the Board should be split. Furthermore, members of the Board of Directors should be free of conflicts of interest, particularly those that may lead to disadvantages for the shareholders. And finally, Union Investment demands transparent management remunerations based on long-run performance.

Concluding his presentation, Mansfeld called attention to the Corporate Governance Action Plan and associated work that is being done at the European level. Many of the concepts in the Action Plan are fully supported by Mansfeld. However, some of the legislative proposals, such as the disclosure of shareholder voting and the promotion of independent directors, do not meet with his approval. He also spoke about the commitments of unregulated funds, i.e. hedge funds, as institutional investors. Rules of conduct for hedge funds are currently non-existent but are badly needed. This would enhance the transparency of their strategies as shareholders and would reduce possible conflicts of interest.

In summary, it may be said that Mansfeld's answer to the question whether institutional investors should use their growing importance to influence corporate governance of companies suggests that ultimately the performance of the company is of foremost importance to the investor and that corporate governance has to be in line with this issue.

Tim Oliver Berg and Lut De Moor (CFS staff)

Joint Lunchtime Seminars

The Joint Lunchtime Seminars are a series of weekly research lectures inviting academics from other institutions to present their research in the fields of Monetary Economics, Macroeconomics, Finance and Econometrics. The speakers comprise both well-established senior researchers as well as those at the assistant and associate level from all over Europe and the United States.

Originally started in January 2001, the weekly presentations have become a fixed entry in the diary of many members of research institutions and central banks located in Frankfurt. As a result, seminars are usually accompanied by lively debates and subsequent discussions.

The Joint Lunchtime Seminars are organized by Klaus Adam (European Central Bank), Heinz Herrmann/Sandra Eickmeier (Deutsche Bundesbank) and Volker Wieland (Frankfurt University and CFS)/ Günter Beck (Frankfurt University).

30 May 2007 — **Dynamic Factor and Factor Augmented Error Correction Models**
Anindya Banerjee (European University Institute)

23 May 2007 — **Market Liquidity and Funding Liquidity**
Marcus Brunnermeier (Princeton University)

16 May 2007 — **Consumer Confidence and Elections**
Gikas Hardouvelis (Eurobank)

8 May 2007 — **A Century of Work and Leisure**
Valerie Ramey (University of California, San Diego)

2 May 2007 — **Competition, Risk-Shifting, and Public Bail-Out Policies**
Isabel Schnabel (Max Planck Institute for Research on Collective Goods)

25 Apr. 2007 — **Exchange Rate Models are Better than You Think**
Charles Engel (University of Wisconsin)

18 Apr. 2007 — **Idiosyncratic Uncertainty, Inflation, and Welfare**
Miguel Molico (Bank of Canada)

11 Apr. 2007 — **Assessing Estimates of the Exchange Rate Pass-through**
Ida Wolden Bache (Norges Bank)

4 Apr. 2007 — **Changes in Predictive Ability with Mixed Frequency Data**
Ana Beatriz Galvao (University of London)

28 Mar. 2007 — **Five Facts About Prices: A Reevaluation of Menu Cost Models**
Emi Nakamura (Harvard University)

21 Mar. 2007 — **Learning from Public and Private Observation of Other's Action**
Pierre Olivier Weill (New York University)

14 Mar. 2007 — **Informed Lending: Foundations and Applications to Corporate and Consumer Finance**
Roman Inderst (Frankfurt University)

7 Mar. 2007 — **New Keynesian Models, Durable Goods, and Collateral Constraints**
Tommaso Monacelli (Bocconi University)

28 Feb. 2007 — **News shocks with Limited Enforcement**
Karl Walentin (Sveriges Riksbank)

21 Feb. 2007 — **Household Need for Liquidity and the Credit Card Debt Puzzle**
Irina Telyukova (University of California, San Diego)

14 Feb. 2007 — **Learning, Macroeconomic Dynamics and the Term Structure: A Bayesian Analysis**
Hans Dewachter (KU Leuven)

7 Feb. 2007 — **Are Valuation Effects Desirable from a Global Perspective?**
Pierpaolo Benigno (LUISS - Free University for International Studies in Social Science, Rome)

24 Jan. 2007 — **The Role of Housing Collateral in an Estimated Two-Sector Model of the U.S. Economy**
Stefano Neri (Bank of Italy)

17 Jan. 2007 — **Financial Innovation and the Transactions Demand for Cash**
Francesco Lippi (University of Sassari)

19 Dec. 2006 — **Restructuring the Sovereign Debt Restructuring Mechanism**
Mark L. Wright (University of California, Los Angeles)

12 Dec. 2006 — **Risk Sharing in Private Information Models with Asset Accumulation: Explaining the Excess Smoothness of Consumption**
Nicola Pavoni (University College London)

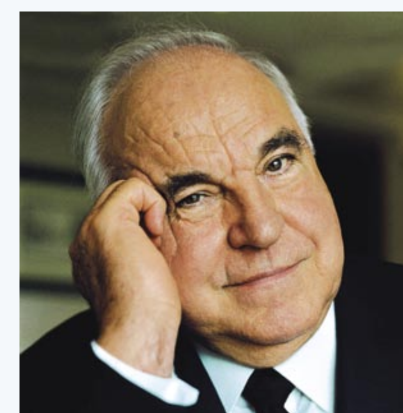
5 Dec. 2006 — **Banks' Choice of Liquidity: The Role of Fire Sales and Entry**
Tanju Yorulmazer (Bank of England)

CFS*luncheon*

The Center for Financial Studies organized a lunch-time lecture under the new heading "CFS Luncheon". The first event was held on 19 April 2007 with a talk by Professor Martin Weber (University of Mannheim) on the topic of "Active versus Passive Portfolio Management". Udo Rosendahl (DWS Investment GmbH) acted as discussant and Dieter Kuckelkorn (Börsen-Zeitung) as moderator of the discussion. The lecture and discussion were held in German. This first CFS Luncheon was well received and the attendance was above all expectations. Around 150 participants, mainly from the banking sector, have attended the event. Jan Pieter Krahnen (CFS Director and Organizer of the event) said that similar events are under consideration for the future.

CFS*presidential lectures*

"Die Zukunft Europas" (The Future of Europe) Dr. Helmut Kohl, 21 June 2007



Dr. Helmut Kohl was born in 1930 and studied Law, Political Science and History at the Universities of Frankfurt and Heidelberg. In 1958, he received the degree of Dr. phil. He joined the Christian Democratic Union (CDU) in 1947 and was the federal chairman of the CDU party from 1973 to 1998.

His 16 year tenure as Chancellor of Germany (Bundesrepublik Deutschland) was the longest in post-war German history: he held the office from 1982 till 1998. During this time, Helmut Kohl played a crucial role in many important historic changes that took place in Europe, such as the German Reunification and the signing of the Maastricht Treaty, which led to the creation of the European Union. He became a greatly respected European statesman.

His visions to "Overcome the division of Germany and Europe" and to bring forward the French-German reconciliation and European integration were vital in this respect.

Helmut Kohl received many awards and prizes throughout his career. To name a few, he was awarded the "Großkreuz des Verdienstordens der BRD in besonderer Ausführung" (Grand Cross of the Order of Merit of the Federal Republic of Germany), was made honorary citizen of Europe and received the "Presidential Medal of Freedom" from U.S. President Clinton.

Among his publications are: Helmut Kohl. Erinnerungen (1982-1990 and 1930-1982).

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CFS Presidential Lecture Series on European Integration

In everyday life "Europe" widely stands for "Bureaucracy from Brussels", disputes about finances and national interests. Beyond these quarrels, the track record of the European Integration is endangered to fall into oblivion. After two terrible world wars in the first half of the 20th century, the European Union today unites more than 490 million Europeans from 27 countries in freedom and peace. Thirteen of these member states, of which many did not know a solid currency for decades, now share a common stable currency, the Euro. Particularly younger generations are at risk to lose knowledge about the importance of the European Integration.

The Center for Financial Studies (CFS), beyond its engagement in questions of financial markets and monetary problems, would like to contribute with this lecture series to the awareness of the importance and achievements of the European Integration. For this purpose, the CFS has invited prominent speakers with expert knowledge in questions of European Integration.

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The lecture series will be opened by the former chancellor Dr. Kohl with the speech "Die Zukunft Europas" ("The Future of Europe") on 21 June 2007. The speech will be held in German. Cardinal Lehmann will make a speech on the topic "Über die Chancen des biblisch-christlichen Leitbildes für die europäische Integration" ("On the Opportunities of the Biblical Christian Overall Concept for the European Integration") on 5 September 2007. The speech will be held in German. Mario Draghi (Governor of the Bank of Italy) will give a speech on 22 November 2007. In addition Mario Monti (10 years member of the European Commision), Lord Dahrendorf (House of Lords) and Professor di Fabio (German Federal Constitutional Court) have accepted to contribute to future lectures.

CFS*research conferences*

CFS Summer School 2007
12 – 19 August 2007

Training Center of the Deutsche Bundesbank Eltville (near Frankfurt am Main), Germany

"Corporate Governance and Capital Markets" Jointly organized by CFS and ECGTN

The CFS-ECGTN Summer School 2007 on "Corporate Governance and Capital Markets" is organized by the Center for Financial Studies and the European Corporate Governance Training Network (ECGTN). The topics of this year's summer school are: the role of mergers, acquisitions, restructurings; venture capital and private equity; corporate governance and shareholder value.

The lectures will be given by:
- **Yakov Amihud** (Stern School of Business, New York University) on "Mergers, acquisitions, and restructurings"
- **Francesca Cornelli** (London Business School) on "Venture capital and private equity"
- **David Yermack** (Stern School of Business, New York University) on "Corporate governance and shareholder value"

The school is intended for doctoral and post-doctoral students in economics, finance, law and political science. Participation is compulsory for Early Stage Researchers of ECGTN.

The Summer School will be held at the Training Center of the Deutsche Bundesbank, situated 30 miles west of Frankfurt at the riverside of the Rhine and in the midst of one of the most famous wine growing areas in Germany.

The program will start on Monday morning and is scheduled to end on Saturday evening. Meals and lodging will be provided from Sunday evening (12 August) until Sunday morning (19 August). Social events will also be organized. Participants will be charged EUR 1,350.- covering registration, full board at the Training Center and background material.

Further information about the Summer School 2007 can be found on the CFS website.

International Conference on Public versus Private Ownership of Financial Institutions

The conference jointly organized by the Center for Financial Studies, the Deutsche Bundesbank, and the Wharton Financial Institutions Center was held at the Deutsche Bundesbank, Frankfurt on 17-18 November 2006. The focus of the conference was to address the implications of the ownership structure of financial institutions for performance, growth, credit availability, and stability of the financial sector.

Reinhard Schmidt and Edgar Meister,
Photograph: René Zimmer ©

The opening speech was held by **Edgar Meister** (Member of the Executive Board, Deutsche Bundesbank). He started with a brief review of the characteristics of the German banking system and its three-pillar structure, emphasizing the reasons for the existence of public banks in the economy. Meister compared the system in Germany with those of other European countries that have faced a privatization trend in the last years. He argued that further research is required before the positive consequences of privatization in a banking sector can be satisfactorily analyzed.

The first session on "The Role of Government" was chaired by **Beatrice Weder** (University of Mainz and CFS). **Julan Du** (Chinese University of Hong Kong) presented the first paper in the session, "Government-Business Relationship and Financial System Structure". This paper shows that government intervention plays an important role in shaping the structure of a financial system. A higher degree of state intervention tends to lead to a more bank-based financial system and government ownership of banks, since

Beatrice Weder-di Mauro, Photograph: René Zimmer ©

bank financing is less sensitive to the negative effects of state intervention when compared with equity financing. The paper was discussed by **Giovanni Dell' Ariccia** (International Monetary Fund), who focused on the characteristics of the sample and suggested that additional controls in the empirical analysis and more theoretical background would provide a better motivation to the paper.

Elias Papaioannou (European Central Bank) presented the next paper entitled "Financial Development and Intersectoral Investment: New Estimates and Evidence", in which he examines whether greater levels of financial development lead to greater investment in growing sectors. His study links institutional features with the intersectoral investment responsiveness through financial development and finds strong evidence for an association between financial development and the intersectoral investment responsiveness measure. Moreover, he finds that state ownership of banks is strongly related to capital market size and intersectoral investment responsiveness. The discussant of the paper, **Uwe Walz** (Goethe University Frankfurt and CFS), argued against the underlying theoretical considerations of the two stage approach of the model and recommended examining reversals in the country ranking of investment responsiveness and in financial development ranking due to the relatively longer sample period.

The second session, chaired by **Thilo Liebig** (Deutsche Bundesbank), addressed "Bank Ownership and Financial Stability" and began with a presentation by **Gianni De Nicolo** (International Monetary Fund) on "Bank Ownership, Market Structure and Risk" (joint work with Elena Loukoianova, International Monetary Fund). This paper models the impact of market structure, bank monitoring and bankruptcy costs on banks' risk of failure by focusing on the heterogeneity of banks, and it also empirically tests the predictions derived using data for non-industrialized countries. The findings may be summarized as follows: first, the positive relationship between bank concentration and risk of failure is stronger when bank ownership is taken into account, and the relationship is strongest if the state-owned banks' market share is larger. Second, foreign banks are riskier than private domestic banks. Third, there are negative "external" effects on private domestic banks from state-owned and foreign banks' larger market shares. **Isabel Schnabel** (Max Planck Institute for Research on Collective Goods, Bonn) started the discussion of the paper by looking at the definitions used in the paper for "competition" and "public/ foreign banks". She compared the paper with the work by Gropp/Hakenes/ Schnabel (2006) and concluded that findings on externalities owing to state-owned banks and highly concentrated banking sectors are robust to different data and different methodologies.

Heiko Hesse (World Bank and University of Oxford) presented the next paper in the second session, "Cooperative Banks and Financial Stability" (co-authored by Martin Cihák, International Monetary Fund). This study finds that due

Thilo Liebig, Photograph: René Zimmer ©

to lower volatility in returns, cooperative banks are more stable than commercial banks. Moreover, commercial banks are less stable if they are in a system with a higher presence of cooperative banks. **Ralf Elsas** (University of Munich) discussed the paper by focusing on sample characteristics and the methodological issues. In particular, he suggested controlling for mergers since distress mergers might have an impact on the financial status of banks.

Isabel Schnabel, Photograph: René Zimmer ©

The keynote speech, moderated by **Franklin Allen** (University of Pennsylvania), was held by **Ross Levine** (Brown University). Levine provided a review of the recent literature on government ownership of banks and compared different views related to the topic. The studies discussed cover both developed and undeveloped countries and investigate the economic impact of government-owned banks as well as the links to politics. Levine concluded his speech with a summary of findings that government-owned banks frequently slow economic growth and that their lending is based on political criteria.

The third session chaired by **Jan Pieter Krahnen** (University of Frankfurt and CFS) focused on "SME Financing and Relationship Lending: Evidence from Asia". **Wako Watanabe** (Tohoku University) presented the paper entitled "Do Governmental Financial Institutions Help Startups Grow? Evidence from Japan" (co-authored by Hikaru Fukanuma, National Life Finance Corporation and Tadanobu Nemoto, Chuo University). Based on a survey of small and medium enterprises (SMEs), the paper finds that government financial institutions (GFIs) lend to firms with limited credit availability, and firms that borrow from GFIs grow faster than firms that borrow from private banks. The paper was discussed by **João A.C. Santos**, (Federal Reserve Bank of New York), who argued that the authors need to explore other performance measures of firms and to control for additional firm characteristics such as capitalization.

Jan Pieter Krahnen, Photograph: René Zimmer ©

Maria Soledad Martinez Peria (World Bank) presented the final paper of the day, "Bank Ownership Type and Banking Relationships" (co-authored by Allen N. Berger, Board of Governors of the Federal Reserve System and Wharton FIC; Leora F. Klapper, World Bank and Rida Zaidi, University of Cambridge). Investigating the impact of bank ownership type on banking relationships for Indian firms, the authors find that firms with relationships to foreign banks are more likely than other firms to be transparent, to have multiple relationships, and to diversify across bank ownership types. But firms that have relationships with state-owned banks are less likely to maintain multiple banking relationships and to diversify across ownership types compared to other firms. **Todd Gormley** (Washington University in St. Louis) expressed his concern about the direction of causality for the impact of foreign banks when discussing the paper. He suggested the use of more controls in the model and the investigation of within-district variation for foreign banks.

The second day of the conference started with the session on "The Experience in European countries" chaired by **Elena Carletti** (CFS). The first speaker, **Miguel A. García-Cestona** (Universitat Autònoma de Barcelona) held a talk on "Multiple Goals and Ownership Structure: Effects on The Performance of Spanish Savings Banks" (co-authored by Jordi Surroca, Universidad Carlos III). This paper shows how the ownership structure of savings banks affects their performance level and their goal priorities. The findings suggest that insider-controlled savings banks favor different goals such as profit maximization and perform better, compared with those controlled by public administrators. The discussant, **Lucy White** (Harvard Business School and University of Lausanne), argued that studying only savings banks does not answer all questions related to efficiency. In particular, she suggested that the authors should use input-output analysis to measure efficiency.

The final paper of the session and the conference was presented by **Elisabetta Fiorentino** (Dresden University of Technology) entitled "Productivity Change, Consolidation, and Privatization in Italian and German Banking Markets" (co-authored by Alessio De Vincenzo, Bank of Italy; Frank Heid, Deutsche Bundesbank; Alexander Karmann, Dresden University of Technology and Michael Koetter, University of Groningen). The authors find that both countries' banking systems have experienced productivity growth owing to the improvement of technology in the period 1995-2004. Moreover, Italian banks' productivity growth, positively affected by privatization, has been higher than that of German banks. Cost efficiency changes have contributed little to growth. **Steven Ongena** (Tilburg University) discussed the paper, and suggested exploring the timing of the effects of ownership changes and controlling for other factors in order to show that privatization really affects productivity growth.

The conference concluded with a panel discussion moderated by **Gertrude Tumpel-Gugerell** (Member of the Executive Board, European Central Bank). The first speaker, **Luis Rodriguez** (Head of the Technical Secretariat, Associate Directorate General of Supervision, Bank of Spain), gave a summary of the Spanish experience, focusing on the structure of savings banks. **Paolo Marullo Reedtz** (Deputy Head, Banking Supervision Department, Bank of Italy) gave a brief review of the Italian banking system before 1980. He compared the figures for public and private banks and pointed to the limited profitability and low capital endowments of savings banks. He said that for private banks there are legal barriers to acquiring a public bank. **Martin Hellwig** (Director, Max Planck Institute for Research on Collective

Goods and Former President of the German Monopoly Commission), on the other hand, questioned the objectives of Basel II. He also argued that the presence of public banks increases competition in the industry and that the UK should not serve as a model with regard to the profitability of banks since there is limited competition in the industry. **Hans-Helmut Kotz** (Member of the Executive Board, Deutsche Bundesbank) asked if a bank should be shareholder-oriented or stakeholder-oriented as many people use arguments on profitability. **Tumpel-Gugerell** responded by emphasizing that capital requirements are not equal for each type of bank and this prevents the industry from being a legal playing field. All discussions showed that the debate on bank ownership still continue, especially with respect to Germany.

Günseli Tümer-Alkan (CFS research staff)

The complete conference program including papers and presentations can be found at: www.ifk-cfs.de

ECB-CFS Research Network on “Capital Markets and Financial Integration in Europe”

The ECB-CFS Research Network on “Capital Markets and Financial Integration in Europe” is currently in its second phase until the end of 2007. The Internal Steering Committee consists of the following members: Gertrude Tumpel-Gugerell (ECB), Michael Binder (University of Frankfurt), Philipp Hartmann (ECB), Jan Pieter Krahnen (CFS and University of Frankfurt). The ECB-CFS network organizes two conferences per year on topics related to its priorities. In 2006, the conferences were held in Berlin and Madrid.

7th ECB-CFS Research Network conference, hosted by Deutsche Bundesbank 28 – 29 September 2006 “Financial System Modernisation and Economic Growth in Europe”

Financial integration and financial system modernization are recognized to be key issues in fostering competition and economic growth in Europe. But what are the exact mechanisms behind the interaction of finance and growth? Does financial development indeed cause economic growth, or is it the other way round? And, how far have European countries progressed in modernizing their financial systems?

Leading-edge research addressing these and related questions was presented and discussed at the seventh ECB-CFS Research Network conference ‘Financial System Modernization and Economic Growth in Europe’ at Harnack Haus in Berlin.

In her opening remarks, **Gertrude Tumpel-Gugerell** (Member of the Executive Board of the ECB) emphasized the strong ties between financial development and economic growth. As the benefits of European financial market modernization have not always been fully perceived by European citizens, raising general awareness of these benefits would be essential.

Gertrude Tumpel-Gugerell

The first session revisited the financial development-growth nexus. It was generally agreed that financial development drives economic growth - although reverse causality exits. Drawing from the results of two technically demanding papers, **Elias Papaionnou** (ECB) showed that financial development is vital in channeling capital into the most productive industries, and that countries with larger capital markets were faster to adapt to technological change. **Jean Imbs** (HEC Lausanne) looked at US State-level banking sector deregulation between 1972 and 1995. Applying portfolio theory to the literature on finance and growth, he presented evidence of deregulation having a positive effect on capital efficiency. **Alain de Serres** (OECD) exploited cross-country as well as industry variation, to demonstrate that competition-friendly regulation has a positive effect on productivity and output growth.

Jean Imbs

The second session focused on the relationship between lenders and borrowers in corporate and household financing. **Charles Grant** (University of Reading) showed that debt repayment behavior of households differs significantly across European countries. The way households deal with adverse events that restrain ability to pay largely depends on the institutional setting and the cost of default. Using a novel data set which includes information from accepted and rejected loan applications, **Robert Hauswald** (Kogod School of Business, American University) reconfirmed that geographic distance between banks and borrowers plays an important role in determining pricing and availability of credit. He noted, however, that it is not distance per se but rather informational deficiencies that drive the results. Mainly addressing developing countries, **Xiaoyun Yu** (Kelly School of Business, Indiana University) provided a theoretical explanation for favoritism leading to the efficient allocation of capital.

In his keynote lecture, **Philippe Aghion** (Harvard University) revisited the finance-growth debate, focusing on potential interaction effects between the two. Aghion presented evidence that catching up was easier for countries with a high level either of financial or technological development, whereas less endowed countries were likely to fall back. He went on to argue that a more counter-cyclical budgetary policy was more growth enhancing in countries with lower levels of financial development. Presenting his arguments with verve, he concluded that for the EU it would be advisable to have a more pro-cyclical budgetary policy. These remarks sparked a lively discussion, as did his claim that EU countries chiefly should foster financial market development and not labor market reform, since the latter was costly and not as responsive.

Avanidhar Subrahmanyam

According to work presented by **Avanidhar Subrahmanyam** (UCLA) in the third session, high CEOs salaries can be explained by larger shares of unsophisticated retail investors. In contrast to institutional investors, retail investors may be unable to decipher true CEO compensation from disclosures. **Kaspar Meisner Nielsen** (Copenhagen Business School and CEPR) showed that publicly traded corporations in Europe that adhere to the “principle of proportional ownership” have on average higher firm value.

The first day ended with a superb view over Berlin city from the top of the “Reichstag” building. In his dinner speech,

Thomas Mayer (Chief Economist Europe of Deutsche Bank AG) pleaded for monetary policy makers to pay closer attention to financial markets change in risk appetite and the way financial markets price risk.

The second conference day started with two parallel sessions: one focusing on the interrelation between transparency, finance and growth, the other looking at startup financing. **Vladimir Atanasov** (Mason School of Business) claimed that restricting the possibilities of financial tunneling proved beneficial to the stock market development in Bulgaria. **Ari Hyytinen** (Bank of Finland) presented evidence for Finland, indicating that mandatory disclosure requirements may have a positive impact on small businesses financing costs. Within the parallel session, **Marco Da Rin** (Tilburg University and Università di Torino) analyzed the effects of trust on investment and economic growth, while **Luísa Farinha** (Bank of Portugal) assessed whether initial financing conditions matter for the survival of start-up firms.

Thorsten Beck

Thorsten Beck (The World Bank) pointed out that breadth and outreach of financial sectors in cross-country comparison and over time were not well researched, largely owing to a lack of consistent data. Therefore, the World Bank has taken first steps to develop a new database that comprises the number of loans and deposits in a given country as well as the number of ATM machines. A first analysis suggests that these indicators can be useful when measuring access to and use of financial services, yielding complementary information to standard indicators of financial depth. Challenging the seminal paper of Rajan and Zingales (1998), **George von Fuerstenberg** (Indiana University) proposed an alternative measure of external finance dependence that is not related to technological factors. He argued that differences in dependence on external finance as in Rajan and Zingales, might merely reflect differences in technology across different manufacturing sectors.

Philipp Hartmann (ECB) presented a number of indicators that can be used to measure financial development as opposed to financial integration in the EU. The numbers considered suggest that Greece, Italy and Portugal need further financial system improvements, while France and Germany offer a somewhat mixed picture. Finland, the Netherlands and Sweden are front-runners regarding their financial systems. Not surprisingly, the UK, and to a lesser extent the US, somewhat stand out as performing better than the Euro area countries according to a number of measures. The interpretation of the numbers stimulated large interest from the audience. It was generally welcomed that the indicators focus on quality rather than size of the financial systems and that the results be made public, although in some cases, such as competition and liquidity, more sophisticated yardsticks would be required.

Heinz Herrmann, Axel Weber

Axel Weber (President of Deutsche Bundesbank) chaired the panel discussion on "How to Reconcile Global Capitalism with Local Stakeholders?". **Karl-Peter Schackmann-Fallis** from the German savings banks association (DSGV) was convinced that "all business is local" and that the institutions he represents would be able to "substitute the merger of enterprises by the consolidation of processes". **Hanns Ostmeier** (The Blackstone Group) pointed out that private equity - as opposed to public listings - would be more patient, and thus benefit the targeted companies. He also noted that London was used as a hub for financial services by the hedge fund and private equity industry, as Frankfurt was not able to offer the required expertise. **Angel Ubide** (Tudor Investment) believed that future hedge fund regulation might become necessary, more because of consumer protection issues than for financial stability reasons. He also lobbied for a reformed and integrated mortgage market in which consumers would be able "to take their mortgages to other banks".

In his closing remarks, **Axel Weber** resumed that financial integration and modernization do matter for economic growth, but were first and foremost market driven processes. He also pointed to the role of policy makers, who should be committed to providing an effective legislative and regulatory framework.

Christian Weistroffer (CFS and Deutsche Bank AG)
With thanks to the ECB staff who provided the Conference Summary

The complete conference program and downloadable papers can be found at: http://www.eu-financial-system.org/Berlin2006_programhtm.html

8th ECB-CFS Research Network conference, hosted by Banco de España 30 November – 1 December 2006 "Financial Integration and Stability in Europe"

The 8th Conference of the ECB-CFS Research Network was hosted by the Bank of Spain in Madrid on 30 November and 1 December 2006. The topic "Financial Integration and Stability in Europe" addressed one of the Network's new priorities introduced after the start of the second phase. The conference combined research paper presentations with a policy panel discussion.

In his opening remarks, Governor **Miguel Fernández Ordóñez** (Bank of Spain) noted that financial integration in Europe was advancing along different paths in different markets and that progress had been fairly limited in certain markets. Ordóñez reviewed the main aspects of the relationship between financial integration and financial stability and identified a number of challenges that supervisory authorities face. To meet these challenges, he said, cooperation among supervisors needs to be reinforced. He noted that the recently implemented Lamfalussy approach provided a sound basis in this direction.

The first session on "Relationships between Financial Integration and Stability" started with a presentation by **Iftekhar Hasan** (Rensselaer Polytechnic Institute and Bank of Finland) who spoke about his empirical research concerning the impact of cross-border bank mergers and acquisitions (M&As) on bank risk. **Gianni De Nicoló** (IMF) presented empirical research on the evolution of synchronization between real activity and financial market integration and the implications for financial stability in Western Europe. The results suggest that the integration process does not necessarily signify an unambiguously positive effect on financial stability. **Philipp Hartmann** (ECB) presented the third paper "Financial Integration, Specialization and Systemic Risk". The main results of this paper demonstrate that increased inter-bank integration fosters banks specialization, thereby increasing both the actual benefits from diversification as well as the risk of contagion.

The second session focused on "International Financial Flows, Political Links, and Financial Fragility". **Jerry Parwada** (University of New South Wales) examined whether market co-movements affect international portfolio investment and presented evidence of increased investment opportunities

when co-movements increase. **Giuseppe Vulpes** (UniCredit Group) spoke about his research into measuring co-movements in EU banks' risk using a dynamic factor model, from which a bank fragility indicator is derived. Co-movements in the fragility indicator across EU banks appear to have increased significantly since 1999. **Xiaoyun Yu** (Indiana University) investigated the causal relation between bilateral political relations and economic trade flows for the US and showed that a change in political relations do indeed affect investment strategies.

The third session consisted of two parallel sessions, the first one of which focussed on "The Effects of Financial Modernization and Development on Retail Financing". **Oren Sussman** (University of Oxford) talked about the effects of corporate insolvency law harmonization in the EU on bankruptcy costs and raised the concern that the 2002 legislation had not achieved its goal. **Rocco Huang** (World Bank) spoke about the effects of branching deregulation on economic growth. **Martin Brown** (Swiss National Bank) presented the third paper in this session about information sharing and credit market performance. He provided evidence that information sharing is associated with improved availability and lower cost of credit to firms. The parallel third session looked at "Cross-Border Banking and Retail Integration" with presentations by **Giovanni Dell'Ariccia** (IMF) on the risk and organization of bank foreign affiliates, **Iman van Lelyveld** (De Nederlandsche Bank) on internal capital markets and the lending by multinational bank subsidiaries and **Massimiliano Affinito** (Bank of Italy) on wether the Law of One Price holds in the euro area.

The first day was concluded by two parallel sessions, one chaired by **Christian Laux** (CFS and University of Frankfurt) on "Market Discipline and Bank Risk" and the other chaired by **Stefan Mittnik** (CFS and University of Munich) on "Bank mergers, competition policy, and efficiency". **Xavier Freixas** (University Pompeu Fabra) examined different accounting rules using a theorical model and argued that intertemporal smoothing matters in the choice of the accounting system. **Alfred Lehar** (University of Calgary) focused on the third pillar "Market Discipline" of Basel II and analyzed the theoretical foundation of market-based bank regulation. In the parallel session, **Ignacio Hernando** (Bank of Spain) presented a paper about the reaction of industry insiders to the announcement of M&As in the European financial industry. The results would seem to suggest that domestic merger deals have led to a reduction in the level of competition. **Steven Ongena** (University of Tilburg) spoke about the impact of legislative changes that strengthen competition policy on stock market valuations of banks and non-financial firms. The findings were that legislative changes aimed at strengthening competition policy decrease the valuation of firms but increase the market valuation of banks. Furthermore, he argued that supervisory control, although not bad per se, might not be helpful for efficiency and value-enhancing decisions owing to its greater focus on stability issues.

The second day started with a session on "Policy Issues in European Banking". **David Mayes** (Bank of Finland) presented a paper on making the system of prompt corrective action (PCA) more effective for cross-border banking groups in the EU. He pointed out that effective implementation of PCA would require that EU supervisors have the same authority to take corrective measures. When a bank that is part of an integrated cross-border banking group reaches the point where PCA mandates resolution, the resolution could have implications for a number of Member States. The second paper was presented by **Dirk Schoenmaker** (Vrije Universiteit Amsterdam and the Dutch Ministry of Finance). The aim of the paper is to explore mechanisms for fiscal burden sharing in a banking crisis in Europe. Schoenmakers clarified his preference for private sector solutions to solving a bank failure. He spoke about different mechanisms for ex ante burden sharing and argued that fiscal and supervisory arrangements should be made in tandem. In a study presented by **Klaus Schaeck** (University of Southampton), the effect of competitive conduct by financial institutions on the banking system fragility is analyzed empirically in a cross-country setting. The findings did not support theoretical studies on the link between competition and fragility.

The subsequent policy panel on "Financial Integration and Stability in Europe" was chaired by **Alexandre Lamfalussy** (former President of the European Monetary Institute), who called attention to the absence of systematic crises over the last 7 or 8 years. In his view, this was due to a number of factors including the actions of central banks and the behavior of private banks. He also emphasized the greater opaqueness of the financial system as a result of financial innovations.

Charles Goodhart (London School of Economics) focused on various issues relating to financial crises and argued that more linkages between financial institutions brought greater strength in response to small and medium shocks, but could widen the scale and scope of big shocks. He also stressed that the greater robustness of an integrated financial system might be tested by the greater pro-cyclicality of Basel II. The other members of the panel included **George Kaufman** (Loyola University Chicago), who discussed issues relating to bank insolvency and an efficient resolution strategy, **Matías Rodríguez-Inciarte** (Santander Group) who highlighted the advantages of stress tests for measuring risk, **Peter Nyberg** (Finnish Ministry on Finance) who focused on the management of cross-border systemic crises and on how to proceed in the future in order to improve the handling of cross-border systemic problems and finally **Henk Brouwer** (De Nederlandsche Bank), who presented an overview of the EU institutional framework for supervision and crisis management. In his opinion, the supervisory framework was working with respect to crisis prevention, but had not yet been seriously tested for crisis management.

In her closing remarks, **Gertrude Tumpel-Gugerell** (ECB) commented that the current level of financial integration in Europe is not very high. She concluded that effective and efficient banking supervision is essential both to promote financial integration and to safeguard financial stability. The introduction of the Euro, the single monetary policy, the existence of a single payment area, and the growing process of European financial and banking integration are good reasons for an enhanced common European approach to prudential supervision and financial stability.

The text is based on the Conference Summary, which has been kindly provided to us by ECB staff

THE DEUTSCHE BANK PRIZE IN FINANCIAL ECONOMICS 2007

Michael Woodford to receive Deutsche Bank Prize in Financial Economics 2007

Michael Woodford

Michael Woodford, the John Bates Clark Professor of Political Economy at Columbia University in New York, is to be awarded the Deutsche Bank Prize in Financial Economics 2007. This prize, presented by the Center for Financial Studies (CFS) in coopera-tion with the University of Frankfurt, carries an endowment of 50.000 Euro and is sponsored by the Deutsche Bank Donation Fund.

Michael Woodford is one of the inter-nationally most highly acclaimed researchers in the field of monetary economics. Woodford is to be awarded the Deutsche Bank Prize in Financial Economics 2007 for his fundamental contributions to the theory and practical analysis of monetary policy.

Woodford advocates that central banks adhere to systematic and transparent rules in the design of monetary policy. The effects of monetary policy depend critically upon what market participants expect about future policy and the course of the economy. Thus, interest rates should be set according to systematic rules and central banks need to communicate information about how they intend to conduct policy in the future. The best way for central banks to communicate the future course of policy, according to Woodford, is to be explicit about the rules that guide policymaking decisions. Good rules require explicitly stated targets for policy, such as inflation, and clear

Volker Wieland (Chairman of the jury 2007):

"Michael Woodford has developed a theory of monetary macroeconomics that holds widespread appeal to academic researchers owing to its rigorous microeconomic foundations. Woodford has proved the immense practical value of his theory by analyzing the central role played by expectations and communication in the implementation of monetary policy.

Woodford's work, summarized in his influential monograph "Interest and Prices: Foundations of a Theory of Monetary Policy", has quickly become the standard reference for monetary theory and analysis among academic economists and their colleagues at central banks."

explanations stating how an interest rate level consistent with the policy target is to be achieved. Woodford argues in favor of direct inflation targeting rather than using intermediate targets or reference values for money and credit aggregates.

Michael Woodford studied at the University of Chicago as well as Yale Law School, and wrote his thesis at the Massachusetts Institute of Technology (MIT). His first appointment to a professorship was in 1984 at Columbia University in New York. After further teaching and research positions at the University of Chicago and Princeton University, he returned to Columbia University in 2004 to take up a Chair in Political Economy. During the course of his academic career, Woodford has taken on numerous visiting professorships and consultancy briefs. Thus, for example, he has been an advisor to the central bank of Brazil and the U.S. Federal Reserve as well as the European Central Bank.

The recipient of the Deutsche Bank Prize in Financial Economics 2007 has been selected by an international jury of leading economic researchers and practitioners from the world of finance. This time the jury comprises **Günter Franke** (University of Constance), **Michael Haliassos** (CFS Program Director and Frankfurt University), **Otmar Issing** (President of CFS), **Jan P. Krahnen** (CFS Director and Frankfurt University), **Patrick Lane** (The Economist), **Lucrezia Reichlin** (Director General of Research at the ECB), **Reinhard H. Schmidt** (Frankfurt University), **Lars E.O. Svensson** (Princeton University), **Norbert Walter** (Managing Director of Deutsche Bank Research and Chief Economist of Deutsche Bank Group), and **Volker Wieland** (Chairman of the jury, CFS Director and Frankfurt University).

The Deutsche Bank Prize in Financial Economics is awarded to honor internationally renowned economists, whose

Lars E.O. Svensson (Princeton University):

"The ideal DB Prize recipient is a person who has made outstanding scientific contributions in the area of finance, money, and macroeconomics that are of great relevance and importance for policy or market practice. Nobody fulfils these criteria better than Michael Woodford. He has made a series of outstanding scientific contributions. For many years he has worked on improving the microfoundations for monetary macroeconomics and during this work developed and refined the theory of the so-called New Keynesian model and provide the first empirical estimates of its parameters. His work is summarized in his monumental monograph, Interest and Prices: Foundations of a Theory of Monetary Policy, which is already immensely influential and will be of lasting value. Furthermore, his research is of great practical importance for policymakers. It has provided the foundations for the latest generation of empirical dynamic stochastic general equilibrium models that are now being developed by the most advanced central banks for policy simulations and forecasting. It has also provided central bankers with a practical framework of how to think about policy and the transmission mechanism of monetary policy, in particular the fundamental role of expectations and transparency in implementing monetary policy. His research is now influencing the conduct of monetary policy in many different ways all over the world."

Patrick Lane (The Economist):

"Michael Woodford is a worthy winner of this year's Deutsche Bank Prize in Financial Economics. His work on monetary policy has become highly influential. The emphasis he lays on the importance of expectations to the conduct of policy is especially notable. The same is true of his work on central banks' transparency and communication—a topic of increasing interest not only to central banks themselves but also to those who watch them in financial markets and the media."

work has both decisively influenced research in the fields of finance and money and macroeconomics and delivered important results for economic policy and practice. The prize is awarded on a two yearly basis. The first prize winner was Eugene F. Fama, Professor of Finance at the University of Chicago, who in 2005 was honored for his theory of efficient markets.

This year the prize will be presented to Michael Woodford by Josef Ackermann, Chairman of the Management Board and the Group Executive Committee of Deutsche Bank AG, at an award ceremony taking place in Frankfurt on **4 October, 2007**. The award ceremony will be preceded by a scientific symposium on **"The Theory and Practice of Monetary Policy Today"**.

Norbert Walter (Deutsche Bank Group):

"Michael Woodford combines theory and practice in a very particular way: Not only are his excellent results of research important for science – they are also of concrete use in monetary policy around the globe. I know no other person in this field of research, whose findings were more crucial for discussions on monetary policy in the past decade. Many central banks are keen on winning him for cooperations to improve their analyses in monetary policy. In addition, his findings also have the potential to be adapted to other political fields. The Deutsche Bank Prize in Financial Economics will provide an important contribution towards making Michael Woodford more popular – even beyond the circle of experts."

MANY NEWSPAPERS HAVE REPORTED ON THE NOMINATION OF MICHAEL WOODFORD AS PRIZE WINNER OF THIS YEAR'S AWARD. IN JANUARY, THE GERMAN NEWSPAPER *HANDELSBLATT* PUBLISHED AN INTERESTING ARTICLE ABOUT THE IDEAS THAT WOODFORD REPRESENTS AND THE MOTIVATION BEHIND THE CHOICE OF THE JURY TO SELECT HIM AS PRIZE WINNER. THE ARTICLE ON PAGE 24 IS BASED ON AN INTERVIEW BY NORBERT HÄRING WITH MICHAEL WOODFORD AND VOLKER WIELAND.

At this occasion, the jury would like to thank the nominators for their immense support during the nomination procedure. More than 2,700 university teachers and researchers from 24 countries had the opportunity to submit a suggestion for the nomination.

Michael Woodford awarded generously endowed Deutsche Bank Prize in Financial Economics (*)

by Norbert Häring (Handelsblatt)

A prominent critic of the monetary policy strategy of the ECB, the U.S. economist Michael Woodford, has been awarded the € 50,000 Deutsche Bank Prize in Financial Economics. Since 2005, the prize has been awarded jointly every two years by the Frankfurt-based Center for Financial Studies (CFS) and the Deutsche bank Donation Fund.

In explaining the motivation behind the choice of prize winner, CFS Director Volker Wieland mentioned in particular that Woodford has developed a theory of the monetary policy transmission mechanism that is consistently derived from the decision processes of individual households and businesses.

An important implication of Woodford's work is the significant impact of expectations on monetary policy. From this he infers that central banks should do everything in their power to allow the public to be able to accurately assess the central bank's reaction to specific situations in the economy. For this reason Woodford is a proponent of the strategy of inflation targeting, which in essence rests on the notion that the central bank should announce an inflation target and adjust its interest rate according to whether there is a shortfall or overshooting of this target.

"I would recommend that both the ECB and the US Federal Reserve take a close look at how the central banks of England, Sweden and Norway make and communicate their decisions", Woodford told the Handelsblatt. These central banks currently represent the vanguard with respect to clear communication and predictability of policy. The Norwegian and Swedish central banks nowadays even forecast publicly what decisions regarding their interest rate targets they are likely to take in the future, given today's information.

The European central bank pursues a strategy similar to that of inflation targeting. However it makes a point of not naming it as such. Under its two-pillar policy strategy, the ECB observes not only inflation but also the money supply and credit aggregates and accords these indicators greater significance.

Very open

Woodford, who advises the ECB as well as other central banks, makes no bones about the fact that he strongly disapproves of the degree of importance given to the money supply. In his opinion, a rational justification for this no longer exists. Rather, this approach requires an unnecessary use of resources and makes it difficult for the ECB to explain its decisions in a coherent fashion.

In November 2006, at the invitation of the ECB, Woodford presented his theories to an academic forum and was greeted with widespread approval from the top-level audience. "I was impressed by the openness with which the ECB faces its critics", Woodford commented.

This openness was also apparent in the award to Woodford. The jury includes Otmar Issing, who is the father of the two-pillar strategy so heavily criticized by Woodford, and who was until recently the chief economist of the ECB.

What Woodford represents

Top researcher

Together with Lars Svensson and the Chairman of the US Federal Reserve, Ben Bernanke, Woodford is currently regarded as one the world's three leading monetary policy theorists.

New-Keynesianism

His treatise "Interest and Prices: Foundations of a Theory of Monetary Policy" is akin to a bible for monetary economists of a new-Keynesian orientation. This currently dominant direction of research assumes that interest-rate policy has a short-term effect on production and employment. Neoclassical economists such as Edward Prescott have disagreed with this proposition.

Career

Woodford currently teaches at Columbia University. Previously he has held positions at the most important elite universities. He was born in Massachusetts in 1955.

(*) The text is a translation of an article by N. Häring. The article was published in Handelsblatt on 26-28 January 2007 and has kindly been made available to CFS by Handelsblatt GmbH, Wirtschafts- und Finanzzeitung – © All rights Reserved

The ECB and Its Watchers IX
Frankfurt, 7 September 2007

The 9th meeting of the CFS trademark conference series "The ECB and Its Watchers" will be held on 7 September 2007. This conference series was initiated in 1999 by Otmar Issing and Axel Weber (then Director of CFS). The invitation-only event is regularly attended by many influential professionals from the financial community, central banks and academia and is well known for an informal and spirited exchange of views between ECB officials and academic and market experts. This way of interaction with the monetary authorities can rightly be called a formula of success. General interest in the "The ECB and Its Watchers" conference as a forum of discussion has been rising over the years.

This year's conference will be the first one without Otmar Issing on the ECB side of the debate. However, the ECB's unwavering commitment to face its critics in this public forum is revealed in this year's cast of speakers. ECB President **Jean-Claude Trichet**, Vice-President **Lucas Papademos** and ECB Board Member **Jürgen Stark** will speak to and debate with the ECB's watchers. They will be joined by President **Axel Weber** from the ECB's Governing Council, **Pervenche Berès** who chairs the European Parliament's Committee on Economic and Monetary Affairs and **Ignazio Angeloni** from the Italian Treasury. Academic and private sector ECB watchers speaking at the conference include **Charles Wyplosz**, **Stephen Cecchetti**, **Joachim Fels**, **Paul de Grauwe**, **Wolfgang Münchau** and **Jan Hatzius**.

At CFS we are proud of the continued success of this conference series. We are particularly pleased to see that a similar initiative has recently been started in the United States by Professors **Stephen Cecchetti** (Brandeis University) and **Anil Kashyap** (University of Chicago) in cooperation with the Board of Governors of the Federal Reserve. In an article published on 17 January 2007, the Wall Street Journal reported on the U.S. Monetary Policy Forum (MPF) quoting **Peter Hooper** (Chief U.S. economist at Deutsche Bank), stating that the new US event is modeled after the CFS conference "The ECB and Its Watchers". The first meeting of this new forum "US Monetary Policy Forum (MPF)" was held in March 2007. We asked Peter Hooper to write us his impressions of this new initiative (See the article "The New Fedwatchers Conference" on page 26).

As usual, the 9th "ECB and Its Watchers" conference is by invitation only. We expect about 200 participants and media representatives. The next CFS Newsletter will report extensively on the event.

Lut De Moor and Volker Wieland

The complete conference program will be made available soon on the CFS website www.ifk-cfs.de

The New Fedwatchers Conference

by Peter Hooper (Chief Economist and Managing Director of Deutsche Bank Securities Inc., New York)

Peter Hooper

The US Monetary Policy Forum (MPF), held on March 9 this year in Washington DC, brought together academic economists, financial market participants, and senior officials of the Federal Reserve system. The forum was organized by Professors Stephen Cecchetti and Anil Kashyap of the Brandeis International Business School and the University of Chicago Graduate School of Business, respectively, in collaboration with an advisory panel of academic and Wall Street economists and in consultation with senior Fed officials. It featured presentation and discussion of a report, "Understanding the Evolving Inflation Process," a panel discussing "Liquidity and monetary policy," and a speech on Fed communication and transparency by a former Fed vice chairman.

This year, the MPF, which its organizers hope to make an annual event, involved one of the larger public gatherings of Fed officials outside the Jackson Hole conference. It differs from the Jackson Hole conference and many other Fed conferences (which typically deal with broad academic topics) in its more central focus on issues of direct interest to monetary policy, as well as in its broader involvement of the private financial sector. The MPF is more closely patterned after the successful CFS conference *"The ECB and Its Watchers"* held annually in Europe, soon entering its ninth year. Like the *ECB Watchers conference*, the MPF stresses involvement of the investor community as well as academia, the central bank, and the press. In both cases, policy makers are involved directly in panel presentations and discussions. The focus is on issues of immediate interest to current monetary policy. Its intent is to help the academic and business communities and the central bank to learn from each other and in so doing, to enhance the transparency of monetary policy.

There are also some differences between the MPF and the *ECB Watchers conference*. One is in size and scope. The first MPF was half as long in time, and had roughly half as many presenters and participants as the most recent *ECB Watchers conference* held in Frankfurt last May. From its more modest beginning in 1999, the *ECB Watchers conference*, of course, has expanded to be a full day conference with some 22 presenters and 250 participants, a tribute to its success over the years. Other differences are more subtle. A central (but not sole) focus of the MPF was on a report written and presented in an unusual collaborative effort by a group of academic and business economists and then discussed specifically by two policy makers, Fed Vice Chairman Kohn and Richmond Fed President Lacker.

The ECB Watchers conference has typically had more individual papers and panel presentations, but policy makers' reactions/responses have been held to the end in the form of general comments and reactions to the entire proceedings by Chief Economist Issing. Another difference is that whereas the *ECB Watchers conference* has involved papers and presentations by ECB staff researchers, an important ingredient to its success, the MPF did not do so this year, perhaps reflecting the relative brevity of the conference.

As to the substance of the MPF this year, former Fed vice Chairman Alan Blinder kicked things off with a speech on Fed communication. He noted that the Fed has made much progress in the direction of transparency and predictability, but he also said that much remains to be done. He suggested the need for more internally consistent FOMC forecasts, and he recommended that the Fed publish a Taylor-rule type indicator of what its forecast implies for the possible future course of the fed funds rate. In ensuing discussion, the proposal received mixed reviews from both Fed participants and investors.

The next session of the Forum focused on an issue of central importance to monetary policy makers: what caused inflation to rise in the past, and could it happen again?[1]

In addressing this issue, the report analyzed the great inflation and the stabilization of inflation that occurred in the US and many other countries over the past four decades. The report reviewed and tested many of the explanations for this behaviour of inflation and concluded that shifts in monetary policy were most important. The report found that central banks' success in stabilizing inflation and inflation expectations at relatively low levels has reduced the statistical reliability of various measures of inflation expectations as predictors of inflation. In their comments, Kohn and Lacker stressed the importance of keeping inflation expectations low or reducing them further, and Kohn was hopeful that the history of the great inflation would not repeat itself because policy makers and the economics profession more generally has learned much from that experience.

In the closing session, several academic, Wall Street, and Fed panellists (including Governor Kroszner and President Stern) wrestled somewhat inconclusively with how to define and measure liquidity and how to gauge its implications for the markets. One point of consensus appeared to be a strong preference for price measures (rates, spreads, and premiums) over quantity measures (money and credit stocks and flows).

Overall, the MPF seems to be off to a good start; many participants considered it to be a very useful way to facilitate communication between the Fed and the markets and to help further clarify Fed views on key issues. The organizers look forward to building on this success in years to come, and the *ECB Watchers conference's* experience in this regard undoubtedly gives them reason to be optimistic.

[1] "Understanding the Evolving Inflation Process," by Stephen G. Cecchetti, Peter Hooper, Bruce C. Kasman, Kermit L. Schoenholz, and Mark W. Watson. Available at: http://research.chicagogsb.edu/gfm/events/confrences/2007-usmonetaryforum.aspx

CFS Financial Center Index
New Sentiment Index for Germany as a Financial Center

Project Team: Stephan H. Späthe & Christian Knoll (CFS)

With its GDP share of 16% the financial sector is of considerable economic significance for both Germany in general and the Rhine-Main area in particular. A closer look reveals that there have been very few surveys specifically related to this economic sector, as areas of financial business, leasing and insurance are frequently omitted from many of the usual business surveys. With its new research project, the CFS Financial Center Index, CFS aims to fill this gap. In quarterly intervals the index provides information about the evaluation of financial market agents regarding the development of Germany as a financial center.

The CFS Financial Center Index is a new type of instrument for analyzing the performance of the financial community of Frankfurt in particular and Germany in general. It is based on a management survey started in February 2007 and conducted at quarterly intervals of over 300 leading executives from the Frankfurt financial community. The survey sample will be extended to include the whole of Germany in the near future. The CFS Financial Center Index summarizes current evaluations and expectations about the future with respect to specific business parameters and thus reflects a representative picture of the current business sentiment.

Financial Center Monitoring

The CFS Financial Center Index is part of a larger project conducted by the State of Hesse that aims to measure the competitiveness of Germany as a financial center in comparison to the rest of Europe. The Helaba Landesbank Hessen-Thüringen as a partner in this project already published in summer 2006 the initial study "Finanzplatz Frankfurt – Ein Standort bewegt sich" ("Financial Center Frankfurt – a location in action"). The Frankfurt School of Finance & Management is the project's third partner providing a database of historical financial center indicators.

Index Calculation

In order to calculate the index, a standard catalogue of questions requests information about the participant's view on four business parameters: 1) transaction/sales volume, 2) profit, 3) employment and 4) investments. The answers to the questions may be given as "positive", "neutral", or "negative" and a response is requested for the previous and the current quarter. All participants are allocated to branch-specific groups. Within each group, a balance of the share of positive and negative responses is evaluated and transformed into performance data. These performance

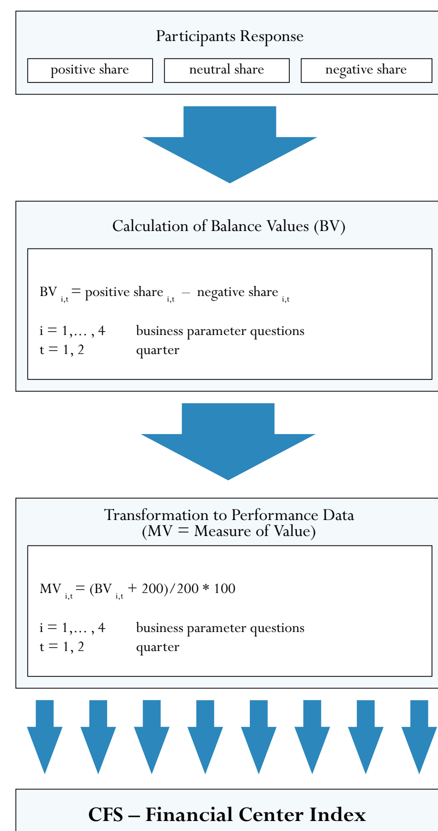

Figure 1

data are then collated to constitute the CFS Financial Center Index.

This first set of questions, that is used to calculate the index, is supplemented by further sets of questions. The second set deals with questions regarding the expansion plans as well as the relocation plans of business activities. The final third block of questions deals with current issues in the financial sector, thus enabling short-term, representative opinion polls. These two additional blocks of questions do not enter the index calculation directly but provide important additional information about the financial center's situation.

Sub-indices

The CFS Financial Center Index is currently compiled from three dimensions. First, there is the temporal dimension (evaluation of the current situation and expectations for the near future), second, there is a branch-specific dimension (cf. Business Sample - Groups 1 to 4 below), and third, there is a performance related dimension (transaction/sales volume and value added). The evaluation with respect to the value added is calculated as the weighted average of the answers to the questions related to profit, employment, and investments.

When the survey is extended to cover Germany as a whole, then a fourth spatial dimension will be added. Taken together, these individual sub-indices allow a detailed structural analysis of the financial center, whereby it is the changes from one quarter to the next that are of main interest.

Business Sample

The businesses and institutions that take part in the CFS Financial Center Index survey are not only chosen from the financial sector but also from other sectors that directly profit from the financial sector. The underlying definition of a financial center is deliberately chosen to be very extensive and the sample of businesses is compiled of four groups as shown in Figure 3 on page 29.

Results

The evaluation of the first survey resulted in an initial index value of 126.2. This indicated a very positive sentiment in the financial sector and its connected enterprises, since by construction the maximum attainable index value is 150 and the minimum 50. A value of 100 signals a neutral prevailing mood. The expectations of the first quarter 2007 even exceeded the good results obtained for the last quarter of 2006. This upward movement resulted from an expected rise in employment, particularly among the financial center-oriented services such as accountants, lawyers and rating agencies. Profit expectations whilst at a high level were, on the other hand, slightly declining.

The second survey that took place between 16 and 27 April 2007 resulted in an index value of 125.0. Compared to the initial value of 126.2, this can be interpreted as a flattening on a high level.

In principle the survey shows that the business representatives are cautiously optimistic about the future development of Frankfurt as a financial center. In the first survey, it was the financial center service providers, whose expectations turned out to be distinctly more positive than those of the traditional financial institutions, i.e. the banks, insurances, investment trusts, and the stock exchange. The second round showed a slight decline in the optimistic trend of the service providers.

On the contrary, the expectations of the traditional financial institutions and brokerage firms were higher in the second round and thus reached the same high level as the expectations of the service providers.

The international stock exchange consolidation is currently not perceived to be a threat to Frankfurt as financial center. In the long run, a Deutsche Börse that operates alone is not in any way expected to lead to the marginalization of Frankfurt as a stock exchange location.

The impending implementation of the European Markets in Financial Instruments Directive (MiFID) that should lead to greater transparency in the securities business is reflected in the expectation that there will be a redistribution in profits from financial institutions towards service providers.

The special additional survey in the second round dealt with specific legal regulations in Germany (such as the REIT-law and tax regulations) and their impact on the competitiveness of Germany.

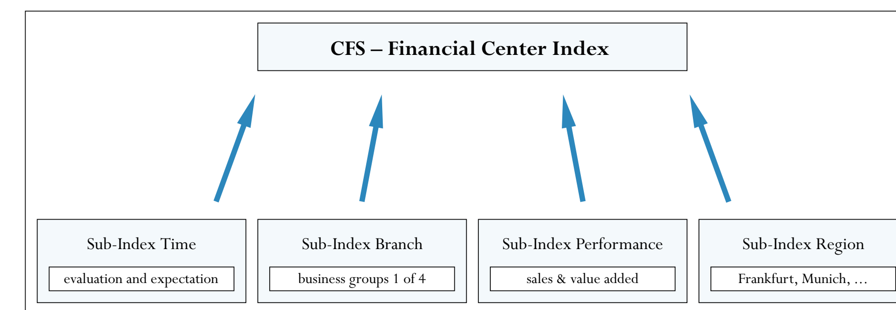

Figure 2

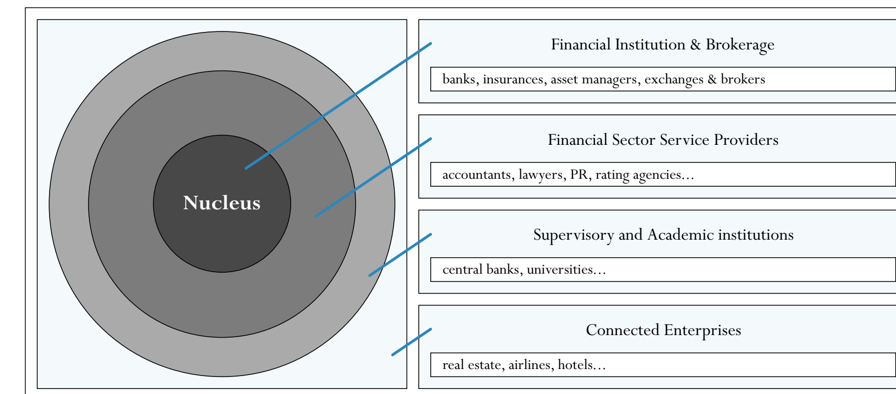

Figure 3

The number of participants in the survey has doubled from 149 participants in the first stage to 338 in the second one. This will continue to rise.

Future Outlook

The third survey for the CFS Financial Center Index will take place in the first week of July. The extension of the survey to cover the financial sector in Germany as a whole is anticipated to start in the fall of 2007. Interested companies from the financial sector that have not yet participated in the survey are welcome to contact CFS for additional information.

Further details can be found at www.finanzplatzindex.de.

Staff Portrait

Elena Carletti joined the CFS in April 2004 as a post-doctoral researcher in the area of "Credit Management and Credit Markets". Her previous positions include that of assistant professor at the Chair of Prof. Martin Hellwig at the University of Mannheim, and that of Tutorial Fellow in Finance at the London School of Economics. She holds a Ph.D. in Economics from the London School of Economics, a Doctorate in Economics from the University of Bologna, and a Master in Economics from Bocconi University in Milan. Elena is expected to complete her Habilitation in Economics this fall at the University of Mannheim.

Elena's research interests are in the areas of financial intermediation, financial regulation, corporate finance and competition policy. Recently, she has been working with Franklin Allen on a number of papers concerned with financial institutions and corporate finance. Part of this work has been published or is forthcoming in refereed journals such as the Journal of Monetary Economics and the Journal of Accounting and Economics. Her work is also published in other refereed journals, such as the Journal of Financial Intermediation and the Journal of Money, Credit and Banking.

Elena Carletti has also been active as co-organizer of a number of conferences at the Center for Financial Studies, like the CFS-IMF "Open Forum on Germany's Banking System" in 2005 and the conference on "Private versus Public Ownership of Financial Institutions" jointly organized by the Center for Financial Studies, the Deutsche Bundesbank and the Wharton Financial Institutions Center in 2006. In 2005 and 2006, she took on the Secretariat work for the ECB-CFS Research Network on "Capital Markets and Financial Integration in Europe" and helped organize various conferences and shape the research agenda of the network.

Next to her position at the CFS, Elena Carletti is affiliated with the Max Planck Institute for Research on Collective Goods in Bonn, and is a research fellow of the Financial Institutions Center at the Wharton School of the University of Pennsylvania.

Elena Carletti has been awarded several grants throughout her career. In 2004, she received the Grant of FDIC's Center for Financial Research (CFR) for a project on competition policy and bank merger control (joint with Philipp Hartmann and Steven Ongena). In 2002, she was awarded the CEPR/European Summer Institute Prize for the Best Central Bank Research Paper (with Philipp Hartmann).

Frankfurt University in top 10 of Uniranking 2007

Universitäten

Volkswirtschaftslehre	Jura	Wirtschafts-ingenieurwesen	Betriebswirtschaftslehre
1. Uni zu Köln	1. Uni Heidelberg	1. RWTH Aachen	1. Uni Mannheim
2. Uni Mannheim	2. Bucerius Law School Hamburg	2. Uni Karlsruhe (TH)	2. Uni zu Köln
3. LMU München	3. Uni Bonn	3. TU Darmstadt	3. EBS Oestrich-Winkel
4. Uni Heidelberg	4. LMU München	4. TU Berlin	4. Uni Münster
5. Uni Bonn	5. Uni Freiburg	5. TU München	5. LMU München
6. Uni Freiburg	6. Uni Münster	6. TU Kaiserslautern	6. KU Eichstätt-Ingolstadt
7. Uni Frankfurt a.M.	7. HU Berlin	7. TU Dresden	7. Uni Frankfurt a.M.
8. Uni Hohenheim	7. Uni Passau	8. TU Braunschweig	8. Uni Hohenheim
9. Uni Regensburg	9. Uni zu Köln	9. Uni Stuttgart	9. Uni Erlangen-Nürnberg
9. Uni Tübingen	10. Uni Tübingen	10. Uni Bochum	10. Frankfurt School of Finance & Management*
			10. Uni St. Gallen
			12. WHU Vallendar
			13. Uni Bayreuth
			14. Uni Augsburg
			15. HHL Leipzig

Die Favoriten der Personalchefs
Welche Hochschulen in der Wirtschaft den besten Ruf genießen

Elektrotechnik	Maschinenbau	Wirtschaftsinformatik	Informatik
1. RWTH Aachen	1. RWTH Aachen	1. TU Darmstadt	1. Uni Karlsruhe (TH)
2. Uni Karlsruhe (TH)	2. Uni Karlsruhe (TH)	2. RWTH Aachen	2 TU Darmstadt
3. TU Darmstadt	3. TU Darmstadt	2. TU Ilmenau	3 TU München
4. TU München	4. TU München	2. Uni Mannheim	4 TU Ilmenau
5. Uni Stuttgart	5. Uni Stuttgart	2. TU München	5 RWTH Aachen
6. TU Dresden	6. TU Berlin	2. Uni Stuttgart	6 Uni Dortmund
7. Uni Erlangen-Nürnberg	7. TU Dresden	7. Uni Erlangen-Nürnberg	7 TU Berlin
8. TU Berlin	8. TU Braunschweig	7. Uni Karlsruhe (TH)	8 TU Kaiserslautern
9. TU Kaiserslautern	9. TU Kaiserslautern		9 Uni Stuttgart
10. TU Braunschweig	10. Uni Hannover		10. Uni Mannheim

Fachhochschulen

Betriebswirtschafts-lehre	Wirtschafts-ingenieurwesen	Elektrotechnik	Maschinenbau
1. ESB Reutlingen	1. FH München	1. FH Karlsruhe (HTW)	1. FH Karlsruhe (HTW)
2. FH Pforzheim	2. FH Karlsruhe (HTW)	2. Hochschule Esslingen	2. FH Aachen
3. FH Münster	3. FH Darmstadt	3. FH Darmstadt	3. FH Darmstadt
4. FH München	4. FH Aachen	4. FH München	4. FH München
5. FH Furtwangen	5. FH Mannheim	5. FH Aachen	5. Hochschule Esslingen

The German weekly magazine, WirtschaftsWoche, published its annual ranking of German Universities in March. This ranking, "Uniranking 2007", relates to the universities' economics, law, engineering, and computer science faculties. It is compiled in co-operation with two firms from the recruiting and consulting branch and is based on the evaluation of more than 1000 personnel managers from large German companies. The Faculty of Economics and Business Administration at the University of Frankfurt has been awarded its best ranking to date and now rates among the top 10 Germany universities. Both the Macroeconomics Department (VWL) and the Department for Business Administration (BWL) have moved up to 7th place. WirtschaftsWoche called this a change of symbolic significance.

News from the House of Finance: Goethe Business School expands its Graduate Program with the "Executive Master of Finance and Accounting"

The program will be conducted in English and German and is directed towards practitioners. On 5 July 2007, the Goethe Business School will present the new program to human resource managers and other corporate representatives (Location: Campus Westend, Room 1.314, Time: 11:00-13:00).
To register or for further information, please consult EMFA@gbs.uni-frankfurt.de or contact M. Pruessner (Tel. +49-69-905-50-37-60)

CFS*colloquium series 2006*

"Funktionswandel von Banken und Börsen: Die neue Herausforderung?"
"Banks and Exchanges in Flux: The next great Challenge"
All Lectures will be held in German

4 July 2007 — **Dr. Reto Francioni** (Deutsche Börse AG)
Wachstum durch Innovation: Das Entwicklungspotenzial von Börsen

12 Sep. 2007 — **Hermann-Josef Lamberti** (Deutsche Bank AG)
Clearing, Settlement und die Kosten des internationalen Wertpapiergeschäfts

17 Oct. 2007 — **Prof. Dr. Ernst-Moritz Lipp**
(Odewald & Compagnie Gesellschaft für Beteiligungen mbH)
Private Equity: Chancen und Risiken des neuen Kapitalmarktes

7 Nov. 2007 — **Susanne Klöß** (Accenture GmbH)
Die Bedeutung von IT für die Entwicklung der europäischen Börsen

Admission to the lectures of the CFScolloquium is only possible after registration. Interested parties who do not receive Email information regularly may contact Isabelle Panther, Tel. +49 (0)69-798 30053 or Email: panther@ifk-cfs.de

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