

“Single Market Trails Home Bias”

By Juan Delgado

Brussels, October 9, 2006

At a Press Briefing on Monday, October 9 at 10:30am Bruegel published the **Bruegel Policy Brief 2006/05 “Single Market Trails Home Bias”** by Juan Delgado, Research Fellow at Bruegel. The paper is the result of original research at Bruegel into the degree of “home bias” in the goods and services markets and in equity investment.

The home bias is the tendency to spend on goods and services produced in one’s home country and to invest in the equity of national companies. A typical European country’s demand is composed of 83% of domestic products and its equity portfolio contains 65% of domestic equity. Juan Delgado relies on two benchmarks (a Frictionless Economy and an Integrated Economy) to measure it in the different markets and to determine whether the single market programme has had an observable impact on reducing home bias in Europe.

According to these benchmarks, the most integrated economies within the EU are Belgium and Austria while Spain and Greece are at the bottom of the list.

Whilst the degree of home bias varies significantly from country to country, it remains very high in the EU. The Single Market notwithstanding, Europeans still buy locally, and also invest locally. Overall, the home bias in product markets has not changed substantially over the past few years but it has decreased in equity markets.

The brief draws policy conclusions from the finding that the integration of product markets through the Single Market programme is showing signs of exhaustion in the EU:

- Internal market policies should adapt to the new economic environment and focus on favouring entry and competition, facilitating innovation and the further integration of value chains across Europe.
- Within the euro area, countries need to make more progress towards integration in order to make sure that monetary policy responds effectively to the needs of the economy. A single currency cannot be sustained over the long term without a single market.
- Markets for goods, services, and capital are interdependent, and this can not be ignored when engaging in reform. Progress on only one could be frustrated by lack of progress on other fronts.

In the new Member States of the EU, stock markets have grown rapidly, but their importance is still much lower than the rest of EU. Hungary and the Czech Republic, for example, have integrated their product markets rapidly but their investments still remain very national. This could leave them vulnerable to shocks in their product markets.

The brief concludes “in order to fully exploit the synergies between financial, product and labour market reforms, such reforms need to take into account the links between markets without expecting that reform in one market will leverage to other markets.”

The full policy brief will be available at www.bruegel.org after the press briefing, about 11:15.

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