lunchtalk@bruegel

Development through financial integration? Lessons from Emerging Europe

with

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and

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Financial integration - in the form of large debt and foreign direct investment flows, and an increasing presence of foreign banks - has been an integral part of the "development model" of emerging Europe over the last decade. The region's slide into deep recession has raised questions about this model.

The presentation will argue three points. First, the role of financial channels in the transmission of the crisis to emerging Europe is more subtle than it appears at first. While financial contagion obviously played a role, foreign bank ownership mitigated the capital flow reversal and the output decline. Second, unlike other emerging market regions, both macroeconomic and sector-level evidence shows that financial integration has boosted long-term growth in emerging Europe. Third, the process of financial integration - particularly large inflows of foreign financing - contributed to credit booms, excess leverage, and foreign currency lending that made the region vulnerable. Going forward, the challenge will be to embrace financial integration while better managing its risks.

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