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Foreign bank ownership and business cycle synchronization in the European Union

Data for 28 EU member states from 1998 to 2016 are used to assess the effects of foreign bank ownership on synchronization of business cycles between euro area and EU countries. Economies with higher share of assets owned by foreign banks are more synchronized with the euro area. Greater foreign bank presence leads to stronger co-movement in output being chiefly the result of greater alignment in investment cycles. It suggests that foreign banks present in EU member states treat host countries as an extension of domestic market and their lending behavior in home and host countries is similar. Our results show that greater foreign bank ownership reduces costs of monetary integration. Common monetary policy is likely to be more adequate for EU countries with higher foreign bank ownership than for those who stick to domestic (including government) ownership.

Keywords: bank ownership, optimum currency area, business cycle synchronization

JEL: E32, E44, F36, G32, F45