Speech By John Bruton Ambassador of the European Union to the United States of America at the Irish Financial Services Association Annual Dinner Four Seasons Hotel Dublin, Ireland 1st September 2005, at 8:00 pm

I am delighted to speak here tonight because of the vital importance of your industry.

Financial services are at the heart of modern economic development. Financial service providers act as the lubricating oil in the economy. They link consumers who want to invest their savings for a good return with companies who want to borrow on best terms for expansion. To achieve this, they need to maximise choice and information and spread risks as widely as possible. This is why it is so critical that we continue the hard work of integrating our financial markets across the European Union and why European financial market integration is central to the Lisbon agenda. When markets integrate, there are huge gains for investors, companies and employment.

But our system of regulation must keep up with this. If it fails to keep up, it will hold back economic expansion. We need financial market regulation that works at national and European level. The Transatlantic economy is at the heart of it. If the EU and the US can cooperate successfully on regulating financial markets, everyone else will follow.

But before I get into that, I would like to say something about the broader strategic context in which your industry will operate.

The economy is not an abstraction. The economy consists of people, and it will only grow if people feel secure and are reasonably free.

The world economy faces four critical problems, which I would place in descending order of importance as follows:

- the possible proliferation of nuclear weapons to terrorist organisations.
- A possible global epidemic such as avian flu.
- Social turmoil in western countries because of inability to accept the costs and loss of dynamism initially associated with ageing and the low birth rate.
- An increase in oil prices so sharp that the financial system cannot adapt to it.

All these four problems require action by politicians as well as by the market.

The time horizon may be too long for sole reliance on market solutions – but perhaps the inventiveness of the financial services industry will prove me wrong that point!

Proliferation of nuclear weapons to terrorist organisations is far more dangerous than proliferation of nuclear weapons to states, even states like North Korea. States can be deterred by the fear of retaliation; non-state organisations cannot by deterred at all. Inventorizing, controlling and reducing the stock of nuclear weapons in the world is the number one security priority for the world and, as such, it is the number one economic priority. One cannot have economic growth without security. A terrorist nuclear detonation in a western city would destroy all economic confidence. Non-proliferation will only work if all states are willing to cooperate, and that will only happen if all feel they are being treated fairly. It is not viable for one country to demand a right to increase and upgrade its nuclear weapons capabilities while asking others to eliminate theirs.

A global epidemic would be almost as destructive. When one bears in mind that the flu epidemic of 1919 killed more people than the First World War, and when one then compares the extent to which we commemorate and write about the 1914-1918 war as against the 1919 flu, one perceives an almost willful forgetfulness about what epidemics can do.

Preventive medicine, whether in regard to flu or malaria, does not offer the prospect of the profits that encourage R&D by pharmaceutical companies. Governments should come together to put money into research on epidemics and chronic medical conditions affecting the poor. This would be enlightened self-interest and economic good sense.

Advanced countries are becoming older and older. People are living longer, and better. But, in the case of most countries since around 1960 and in the case of Ireland since 1980, birth rates have been falling.

Far more people are reaching retirement age each year than are graduating from schools and universities. People have also been retiring earlier and staying in college longer.

When the present pension system was designed, the average person lived for five or ten years in retirement on a pension; now the average person could spend thirty years or more in retirement on a pension. The financing problem that this creates is different for different countries.

In the United States, the financing problem is worst in respect of the healthcare needs of the burgeoning retired population. Social Security, though it is getting most political attention in the US, is the lesser problem.

In most European countries, on the other hand, the problem is with financing of pensions or Social Security.

These financing problems on both sides of the Atlantic could lead to a painful clash between a diminishing number of younger people at work, who are forced to pay higher taxes and insurance contributions, and an increasing number of retired people demanding their "rights."

As the average age of the work force rises, willingness to innovate, to move house or to take risks will diminish too.

All of this will slow economic growth, but worse still, it is liable to be exploited by populist politicians who will put forward "solutions" that will make the problem worse.

The point about the problem caused by the ageing of our societies is that it is a problem that will eventually solve itself--either because the retired eventually die, the birth rate increases or both happen together. It is preferable, I suggest, to raise the birth rate.

An increase in Europe's birth rate today would begin to rejuvenate the workforce within twenty years or less. The present low birth rate is, in part, a result of the design of the welfare state, and if that design is changed, so might the birth rate.

Economic incentives play a major part in human behaviour, and we should not be so idealistic or politically correct as to ignore the effect some of the incentives presently built into European Social Model are having in artificially depressing European birth rates.

The present design of the welfare state in most European countries is one which gives much larger taxpayer support to the financial and other needs of dependent retired adults than it does to dependant children and young adults. The living costs of children and young adults come to about two-thirds of those of a retired adult, but state or collective support for children and young adults comes to nowhere near two-thirds the level of support given at the older end of the age spectrum. Today's children and young adults may not have votes yet, but they are tomorrow's taxpayers and tomorrow's pension contributors, and there is little equity as between present tax, welfare and pension treatment of households containing children and young adults and the treatment of households without them. This is being recognised in France where there are proposals to alleviate the pension contributions required of adult members of households with children.

I now come to the last of the four problems for the world economy I identified earlier – **rising oil prices**. The increase in oil prices now taking place is hardly surprising, in light of the increase in demand relative to supply and the limited nature of this resource. Oil prices would have to be $80 a barrel just to reach 1974 levels in real terms. The wonder is that oil prices have been so low for the last thirty years! A global problem will arise only if oil-consuming countries fail to adjust properly to the new higher price level. Global labour, capital and product markets are much freer now than they were in 1974 and this makes it easier to adjust appropriately, and thus suffer only once-off losses.

This is, however, a very strong case for European countries to invest heavily in research on renewable energy. Ireland, in particular, with its abundance of fertile land should investigate the possibility of refining biomass to produce a substitute for oil. We should not forget that, whereas 75% of the world's energy comes from oil, 95% of the world's industrial chemicals come from oil! We should not leave strategic research on alternatives to oil to the oil industry itself.

Nuclear power, on its own, cannot be a substitute for oil. It now meets only 6% of the world's energy needs and none of its industrial chemical needs. For nuclear power to supply just 17% of the world's energy needs would require the building of 7,000 new nuclear reactors. I am not sure that public opinion is ready for that. It also has spin-off security risks to which I referred earlier.

The financial services industry will have a crucial role in solving these four problems. You can devise the instruments to spread and share risks in a way that matches long-term and short-term considerations. You can find new ways to harness the profit motive to public welfare.

As EU Ambassador to the United States, one of my priorities is to ensure that EU and US regulations on financial markets enable you to do that job well, on both sides of the Atlantic.

In a global marketplace, no one lives in isolation anymore. No one can make his laws in isolation either. Be it accounting, corporate governance, banking, securities or insurance: the laws and rules we pass will affect not just us, but also our trading partners around the globe. Cooperation between regulators and supervisors is not only necessary, it is essential. We aim not at harmonisation, but at fundamental equivalence and at mutual recognition.

There are two main challenges on our international financial services regulatory cooperation agenda:

(i) to remove the inefficiencies and reduce the frictions caused by differing regulation in different jurisdictions.
(ii) to protect our markets from instability, fraud and financial crimes.

First, reducing frictions
In 2002 the EU and the United States set up what has come to be known as the Financial Markets Regulatory Dialogue. It was a response to US concerns about effects of our Conglomerates Directive on US companies. But it then became an essential tool to find a constructive way through the difficulties caused for European companies by the Sarbanes-Oxley Act.

Since then we established a pattern of regular meetings and have built trust and mutual understanding based on informal and low key cooperation.

Let me give an example of where we need to cooperate: up to now, European companies listed in the US have had to reconcile their IFRS (International Financial Reporting Standards)-accounts to US-GAAP (Generally Accepted Accounting Principles).

In a world where two sets of acceptable standards exists, this is unsatisfactory. Companies which are already publishing their accounts to one high-class standard have then to reconcile them expensively to another equally high-class, but different, standard. For some European companies raising capital in the United States, this cost has been estimated at between US $5 and $10 million per annum.

The IASB (International Accounting Standards Board) and the FASB (Financial Accounting Standards Board) are engaged in a process of converging the two standards over time. And the European Commission and the SEC (US Securities and Exchange Commission) are working with these two institutions to ensure that convergence programme has a clear timetable, clear objectives and is transparent to all stakeholders. This is urgent.

Meanwhile, thanks to our dialogue, the US Securities and Exchange Commission has said that by 2009 it will drop the reconciliation requirements, which is hugely welcome. The European Commission is working on a reciprocal basis.

We also are working on further integration of clearing and settlement systems; on deregistration reform and on insurance issues. We are taking steps to help build the transatlantic venture capital market.

Finally, a few words on protecting our markets from fraud and financial crimes. All markets are founded on trust. Without trust, markets break down. Look at Enron, Worldcom, Parmalat or Ahold and the damage they did to market confidence. That is why we need to put up a united international front against corporate fraud, money laundering and also terrorism financing. The European Union and the US can tackle this together.