In case of imperfect financial markets, the financial structure of a given economy— that is, the administration comprising the country's entire financial system— plays an essential role in the processes of monetary transmission. The differences in the prevailing financial structures across the Member States which have signed up to Economic and Monetary Union (EMU) may hamper the implementation of a common European monetary policy. The book (based on the author's PhD thesis) examines the relation between financial structures and the transmission of a unified monetary policy throughout Europe, and, in particular, within the framework of EMU. The objective of the study is to bring to the fore the similarities and differences that exist among the national financial structures of countries belonging to the European Union and to discuss whether the revealed differences may have an impact on the strength and nature of monetary policy transmission.

De Bondt's book focuses on six European countries: Germany, France, Italy, the UK, Belgium, and the Netherlands. The four largest countries represent almost three-quarters of the EU in terms of gross domestic product, while the two smaller ones bring to the study important information concerning small and open economies with a relatively high concentration in the banking industry (the Netherlands was chosen because it is the author's home country). Detailed consideration of these countries enables us to take a closer look at whether cross-country differences in terms of financial structures are systematically related to differences in monetary transmission. The cross-country survey covers the period 1980–1995, a period of financial liberalization, deregulation (in accordance with the process of creating a single European financial market), and innovation.

The conclusions of the book are based on both theoretical and empirical findings. First, the author provides an extensive survey of theories and stylized facts related to one of the most important elements of the financial system, private sector credit. Five theories are examined in Chapter 1. The theory of financial intermediation explains the emergence of indirect credit markets, which
have proven far more important than the direct ones (particularly in Germany, Italy, Belgium, and the Netherlands, among the countries under consideration). Indirect credit markets exist because financial intermediaries exploit economies of scale and have a comparative advantage in the production of information. Banks have a cost advantage in crediting and monitoring, and also an information advantage because of their close and durable relationships with clients. Regulation as a further important element of the financial structure is regarded as both cause and outcome of the emergence and operation of specific categories of financial intermediation. The theory of capital structure shows that the tax structure, information asymmetries, and strategic interaction between firms and their competitors, customers and suppliers, all have an impact on the financial structure. According to the agency theory, debt mitigates potential conflicts of interest between managers and outside shareholders, and also increases potential conflicts between shareholders and debtors. Theoretical arguments based on contracting costs, signaling, and taxation explain the debt maturity structure. In all the countries considered, credit to firms has a shorter maturity than credit to households due to the fact that more and better information is available on them.

The empirical survey, based on the five theories, revealed that in all the investigated countries indirect credit markets played a far more pivotal role in granting credit than direct credit markets. The dominant market participants are banks having an information advantage. The most striking difference in terms of financial structures concerned debt maturity. This proved to be comparatively short in Italy and the UK, but if - as the author supposes - this difference relates to historical divergences in term spread (that is, in the deviations between long-term and short-term interest rates) and inflation trends, it will soon be reduced by the recent Europe-wide convergence in interest rates and price increases.

Chapter 2 gives an overview of the various channels of monetary transmission, with particular attention to credits and the asymmetric effects of monetary policy in Europe. Based on the decomposition of the accumulated impact of the diverse channels of monetary transmission, the author finds that, because European monetary policy is confronted by a wide spectrum of such channels, the design of a comprehensive monetary policy and the process of policy preparation should not focus exclusively on the direct forms of monetary transmission and interest rates, but should pay attention also to the other channels via asset prices, credits, the expectations of the various market actors, and the factor of uncertainty.

Another implication of de Bondt's findings on the shaping of monetary policy is that a change in monetary policy can be amplified through credit channels and that these channels have distributional consequences among borrowers and lenders. According to the theory of credit channels, any shock to the cost spread between self-financing and credit - called the external finance premium (EFP) - affects borrowers' decisions, and therefore influences their behavior. The EFP is affected by monetary policy in two ways: through the bank lending channel and through the balance sheet.