

Towards a Competitive and Future-Proof European Banking Sector

As part of its Communication on the Savings and Investment Union, the European Commission has announced to perform a comprehensive review of the competitiveness of the EU's banking system. The European Council of 23 October 2025 explicitly endorsed this idea and called on the Commission to identify additional potential for further simplification and strengthening competitiveness. On 12 December, the Economic and Financial Affairs Council approved the Council Conclusions on simplifying the Union's financial services regulation, further strengthening the call on the Commission and the European Supervisory Authorities to review and streamline the existing financial services framework. This paper sets out the expectations of the EPP's ECON Working Group for this process. The competitiveness review should not only assess the status quo, but lead to concrete legislative changes to improve the competitive position of the EU's banking sector. The necessary legislative proposals should be presented swiftly so that the European legislator can adopt them within the next eighteen months.

The EU's Banking Sector: Resilient, but falling behind:

While the European banking sector is resilient, it also faces severe risks: European banks are challenged by persistently lower profitability higher costs compared to international peers and a fragmented European market. The average return on equity for EU banks has lagged well behind US banks in recent years. This profitability gap constrains European banks' ability to compete effectively on an international level, limits their ability to invest in new technologies and to serve the European economy. These challenges are at least partially due to the EU's regulatory and supervisory approach and the high compliance cost with a Single Rulebook that has become increasingly more complex, sometimes compounded by diverging national interpretations.

In addition to domestic factors, international developments are widening the competitiveness gap. In the United States and the United Kingdom, regulators have begun to recalibrate post-crisis frameworks to encourage investment and innovation. Meanwhile, in Asia, financial centres such as Singapore and Hong Kong are expanding rapidly with lighter but robust regulatory regimes and strong digital infrastructure. European banks, by contrast, operate under a more fragmented regulatory and supervisory environment and face higher effective capital requirements and an overall more complex framework. Unless the EU adapts its rulebook with competitiveness and the promotion of stable economic growth in mind, there is a real risk that market share, profitability, and technological leadership will continue to shift toward jurisdictions that are more agile and proportionate in their regulatory approach. This, in turn, would negatively affect firms and households' capacity to access finance and financial services at a competitive price.

Ultimately, the EU banking sector's role is to serve the European citizens and companies. A more competitive banking sector will be able to improve economic outcomes for Europeans, will be more innovative and thus contribute to boosting economic growth.

48 Against this backdrop, the European Commission's upcoming review of the competitiveness
49 of the EU's banking sector is more than timely. This paper outlines some priority areas that
50 the European Commission should pay due attention to when conducting the review.

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52 At the same time, the financing needs of the European economy are evolving. Certain
53 investments, particularly those linked to innovation, digitalisation, and the green transition,
54 entail risk profiles that cannot be adequately met through bank credit financing. These
55 investments require deeper and more integrated capital markets, as well as easier access for
56 investors to investment opportunities, especially in start-ups and scale-ups, where market
57 fragmentation also plays a negative role. Therefore, the project to make European banks
58 more competitive must not be looked at in isolation, but must be accompanied by
59 complementary initiatives in the area of capital markets, payments, corporate law (28th
60 regime), financial literacy as well as technological security and resilience as an integral part of
61 the EU's financial sector.

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65 **Breaking down fragmentation: Building a truly European banking market**

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67 EU banks face a competitive disadvantage owing to the lack of scale that results from an
68 incomplete Single Market. Despite years of integration efforts, banks continue to operate
69 largely within national ecosystems, facing duplicated requirements, divergent supervisory
70 expectations and structural ring-fencing. This fragmentation raises costs, limits efficient
71 resource allocation at group level and may slow progress in cross-border consolidation,
72 contributing to European banks operating at a different scale compared with peers in more
73 integrated jurisdictions such as the United States or the United Kingdom.

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75 At the same time, national macroprudential buffer requirements and supervisory practices
76 reflect domestic risk assessments and financial stability considerations. Further integration
77 efforts must therefore strike the right balance between enhancing cross-border efficiency and
78 safeguarding host-country resilience.

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80 Against this backdrop, it would be appropriate to explore greater convergence in supervisory
81 procedures and to assess the functioning of intra-group capital and liquidity arrangements
82 within the Banking Union. In particular, a careful review of the use of liquidity waivers and
83 the conditions under which capital and liquidity can be reallocated within cross-border groups
84 could help identify areas where the Single Market can function more effectively without
85 undermining financial stability.

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87 Deeper integration must continue to safeguard financial stability. However, strengthening the
88 Single Market for banking should be seen not as a trade-off against stability, but as a means
89 to enhance it by fostering stronger, more diversified cross-border groups and a more resilient
90 European banking system overall.

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92 The completion of a better integrated European banking market would represent a major
93 step in reducing market fragmentation. **The Banking Union**, which is based on the three pillars

94 supervision, resolution and deposit insurance, **should therefore be further developed based**
95 **on a clear timeline and measurable milestones.**

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97 Consolidation of the EU banking sector, both within Member States and on a cross-border
98 basis, could be an effective way to improve banks' competitiveness and to give banks a bigger
99 role in contributing to EU growth. One way to support this is by looking at merger and
100 acquisition barriers for EU banks. At the same time, any consolidation efforts should be looked
101 at in the context of the post-2008 objective to end too-big-too-fail, meaning that appropriate
102 supervision is needed and that bigger banks should always have highly credible recovery and
103 resolution plans and authorities should have the right tools to be able to manage failures of
104 these larger banks. In this respect, there should also be an effective liquidity backstop at EU
105 level, possibly via the ESM common backstop.

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109 **Simplification: Keep going**

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111 The European Commission's recent steps toward simplification are welcome and overdue.
112 The decision to deprioritise non-essential Level 2 measures and the ongoing simplification
113 workstreams launched by the ECB's Single Supervisory Mechanism and the European Banking
114 Authority are important first moves. Their recommendations should now feed directly into
115 the Commission's forthcoming competitiveness review. Yet these efforts must go further and
116 have to be looked at in a wholistic manner.

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118 A **comprehensive streamlining of the EU financial rulebook** is needed. The Commission
119 should launch an omnibus legislative initiative to identify and remove obsolete, excessively
120 burdensome or overlapping provisions across the financial services acquis. This exercise
121 should go hand in hand with a **moratorium on non-essential new rules** and the systematic
122 elimination of redundant reporting or disclosure obligations. In line with the Commission's
123 broader target of reducing administrative burdens by 25 percent (and 35 percent for SMEs)
124 such a review should focus on eliminating duplication and avoiding multiple data requests for
125 the same information. The moratorium should also apply to files that are still in the pipeline,
126 but do not in their current forms contribute to administrative simplification, increase EU
127 competitiveness, adopt a market-led approach, meet existing demand, or enhance
128 opportunities for innovation in existing markets.

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130 Simplification must extend to supervisory processes themselves. European and national
131 authorities should intensify efforts to streamline and harmonise the **Supervisory Review and**
132 **Evaluation Process (SREP)**, which in its current form often results in duplicative data requests,
133 inconsistent timelines and limited transparency around risk assessments. A more coordinated
134 approach that is built on common templates, clearer expectations and better sequencing,
135 would reduce the administrative burden on banks while enabling supervisors to focus on
136 material risks rather than process-heavy exercises. Improving the efficiency of SREP is an
137 essential part of making the overall supervisory framework more predictable, proportionate
138 and aligned with the EU's competitiveness objectives.

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140 A further step in simplification should be the shift from today's reporting-heavy system to a
141 genuinely data-driven supervisory model. Instead of requiring banks to compile and submit
142 ever more complex templates, supervisors should be able to access granular, non-
143 standardised datasets directly through secure, harmonised infrastructures supported by
144 modern supervisory technology tools and the use of increasingly advanced technological
145 developments, in particular artificial intelligence, to overcome technical obstacles that have
146 traditionally prevented a pull model. **Moving from a "push" to a "pull" architecture** would
147 cut compliance costs, improve data quality and allow supervisors to focus on substantive risks
148 rather than on processing paperwork. Such an access-based approach would make
149 supervision faster, more consistent and more proportionate, freeing up resources that banks
150 can redirect toward lending, innovation and supporting the real economy.

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152 Simplification should also extend to the **sustainable finance framework**. While the
153 frameworks overarching goal should be maintained, the Commission needs to ensure greater
154 coherence, reduce duplicative provisions and better align obligations across financial services,
155 disclosure, and risk management rules. The proposals for the revised SFDR can only be the
156 starting point. Following the adoption of the Sustainability Omnibus package, prudential rules
157 and supervisory expectations must be adjusted to reflect the more limited scope of the CSRD
158 following the adoption of Omnibus 1. The same logic applies to the EU Taxonomy for
159 sustainable investments: a review is needed to ensure that its screening criteria are realistic
160 and proportionate across all economic activities. In particular, the "do no significant harm"
161 screening criteria should be critically reassessed to avoid excluding viable projects that
162 contribute to Europe's green transition.

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164 Simplification must become a standing priority of the current legislative cycle. Recognising
165 that a positive competitiveness agenda is the only way to start closing the gap with our
166 competitors, we call on the European Commission to prepare a **Financial Services Omnibus**
167 that systematically streamlines the entire EU financial services rulebook and adopt still in the
168 first half of 2026. Furthermore, all new legislation should be subject to a **binding**
169 **competitiveness assessment** in order to prevent the build-up of additional red tape.

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173 **Proportionality: One size does not fit all**

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175 European banking rules must be better **calibrated to the size, business model, complexity**
176 **and risk profile** of institutions. Smaller, regionally focused banks with simple balance sheets
177 and limited trading activity should not be subject to the same highly complex prudential and
178 supervisory requirements designed for large, internationally active groups. While the EU's
179 framework recognises this principle through the designation of small and non-complex
180 institutions (SNCIs), the current approach remains too narrow and too limited in scope. Unlike
181 other major jurisdictions (including the United States, the United Kingdom and Switzerland)
182 the EU has applied the full Basel framework to virtually all banks, irrespective of their risk
183 profile or cross-border activity. This comprehensive, "all-banks" approach goes well beyond
184 Basel's intended application to internationally active banks and creates a structural
185 competitiveness gap for smaller European institutions that face high compliance costs
186 without corresponding systemic relevance. Therefore, like other major jurisdictions, small,

187 non-internationally active banks should be able to opt into a significantly simpler set of rules
188 that is separate from, but coexists with, the current European banking rules, **a genuine small**
189 **banking regime** calibrated to the size, complexity, business model and risk profile of small
190 institutions.

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192 The upcoming review should therefore place strong emphasis on the exploration of this new
193 optional small-bank regulatory regime. Such a regime should be expressly designed for non-
194 internationally active banks with a domestic focus and with a non-systemic footprint. Eligible
195 banks would be able to opt in to a tailored prudential framework aligned with international
196 best practice for small-bank regimes. Under this model, the complex Pillar 1 risk-based capital
197 requirements and much of the qualitative Pillar 2 framework would be replaced by a single,
198 transparent leverage-based requirement set at a conservatively high level to ensure the
199 regime remains fully compatible with financial stability. A portion of this leverage
200 requirement could be structured as a releasable buffer, giving supervisors a simple but
201 effective macroprudential tool to manage procyclicality. Beyond capital requirements, a
202 dedicated small-bank regime should also provide targeted relief from other rules (such as the
203 NSFR and overly complex pillar 2 requirements). Banks would benefit from significantly
204 simplified reporting and disclosure obligations, reducing administrative costs and allowing
205 greater focus on core lending activities.

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207 Above all, **proportionality must become a guiding principle** across the entire regulatory
208 system, not a marginal adjustment. This includes periodically recalibrating thresholds -
209 reflecting inflation and structural changes - to ensure banks are not inadvertently pushed into
210 more burdensome regimes purely due to balance-sheet growth. A more balanced, risk-
211 sensitive approach will ensure that the entire biodiversity of Europe's banking landscape
212 remains strong, competitive and capable of supporting households, SMEs and local
213 economies across the Union.

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217 **Basel implementation: Rethink the scope of application**

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219 The standards emerging from the Basel Committee for Banking Supervision (BCBS) are at the
220 heart of the Union's prudential regime and are meant to preserve an international baseline
221 for banking rules.

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223 While the EU has taken an ambitious proposal to the implementation of the Basel III
224 finalisation package, both in scope and timeline, an **uneven Basel III implementation**
225 **timetable is emerging on international level**. The EU has started to apply the last set of Basel
226 standards from January 2025 (with some delays for the market risk), while other major
227 jurisdictions have not yet implemented or are postponing parts of these rules.

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229 Most of the additional capital charges for European banks are driven by the output floor,
230 which represents a hard lower bound for capital requirements derived from internal models
231 when compared to the standard approach. The output floor is phased-in over a number of
232 years, with additional transitional periods for certain categories (e.g. low risk immovable
233 property loans or loans to unrated corporates). However, this means that the impact of the

234 output floor gets bigger every year and the competitive gap to jurisdictions that have not
235 implemented Basel III grows every year. Against this background, the European Commission
236 should:

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238 • **Narrow the scope to large banks:** As mentioned in the previous chapter, the Basel III
239 framework - and in particular the output floor - should be applied on a consolidated basis
240 only to larger internationally active banks.

241 • Maintain the phase-in of the output floor only for those banks using internal models that
242 would stay under the revised scope of Basel III after applying the exclusions considered
243 under the proposed Small Banking Regime, but consider **extending or making permanent**
244 **the transitional allowances for certain low-risk exposures**, such as for mortgages, SME
245 loans, and unrated corporates.

246 • **Revisit the Market Risk Approach:** In light of an uneven international rollout of the new
247 market risk framework (the Fundamental Review of the Trading Book), the EU should
248 consider delaying or smoothing in its own market-risk capital rules to preserve
249 competitiveness. If other jurisdictions postpone the implementation of Basel's market risk
250 rules, the EU should likewise reconsider the effective date of its stricter requirements via
251 Level 1 legislation. Alternatively, European regulators can use the flexibility in Level 2 to
252 deliver a more level playing field, for example, by adopting less conservative calibration
253 factors ("multipliers") for EU banks' market risk models.

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257 **The capital stack: Simpler and more coherent**

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259 Over the past couple of years, increases in capital requirements for European banks have
260 been largely driven by supervisory discretion, while baseline capital requirements have stayed
261 the same. Those additional supervisory top-ups pose a competitiveness challenge for
262 European banks compared to their supervisory peers.

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264 A **genuine simplification of the capital stack is therefore needed**. The objective should be to
265 reduce the number of overlapping buffers and supervisory add-ons, creating a clearer, more
266 transparent hierarchy of capital requirements, including with regards to the differentiation of
267 going concerns and gone concerns. In particular, the systemic risk buffer (SyRB) should either
268 be removed or harmonised through a single EU-wide methodology aligned with the buffers
269 for systemically important institutions (G-SIIs and O-SIIs). The proposals made by the ECB's
270 Single Supervisory Mechanism in this regard should be built upon.

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272 Greater predictability and transparency in capital requirements would strengthen overall
273 stability and improve the usability of capital buffers. The simplification of the capital stack
274 should in aggregate **not lead to higher capital requirements** for the European banking sector.

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281 **Ensuring a favourable financing environment for small and medium-sized enterprises:**

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283 Small and medium-sized enterprises are the backbone of the European economy, and they
284 rely heavily on bank financing. It is therefore crucial that regulatory capital rules support,
285 rather than hinder, banks' ability to lend to SMEs. However, aspects of the new Basel III
286 framework could unintentionally make SME credit less accessible. In particular, the Basel
287 output floor will substantially raise the risk-weighted assets for any **exposures lacking an**
288 **external credit rating** once the current EU transitional provisions expire in 2032. If this were
289 to take effect unmitigated, many SMEs could face higher loan pricing or even credit rationing,
290 as banks would be forced to hold much **more capital against SME loans**. Such an outcome
291 would directly contradict the EU's policy goal of boosting investment and competitiveness,
292 especially given the high investment needs in digitalization, greening the economy, and
293 scaling up innovative firms. In order to avoid such an outcome, as part of the competitiveness
294 review, the Commission should present options, which preserve favourable financing
295 conditions in its banking competitiveness report. All significant recalibrations of the
296 prudential framework should be based on a careful assessment of their feasibility and
297 expected benefits and associated risks.

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299 To ensure a favourable financing environment for SMEs, the prudential framework must be
300 calibrated with a nuanced, risk-sensitive approach. The **SME Supporting Factor**, which allows
301 banks to hold less capital against loans to smaller firms, has been an effective tool and should
302 be enhanced going forward. In fact, there is a strong case to raise the threshold for qualifying
303 SME exposures to reflect the **updated definition of mid-cap companies** in the EU.

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307 **Reducing the number and complexity of Level 2 and Level 3 acts**

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309 Over the past decade, the volume of Level 2 and Level 3 rules in financial services regulation
310 has exploded, contributing to a regulatory ecosystem that is increasingly complex and difficult
311 to navigate. Level 1 legislation is now routinely followed by hundreds of pages of delegated
312 acts, regulatory technical standards, guidelines and Q&As. Not all of these acts are indeed
313 necessary and the Commission has wisely decided to de-prioritize about 115 of them as "non-
314 essential".

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316 Reducing the number and complexity of Level 2 and 3 acts is essential for a simpler, more
317 coherent regulatory framework. We support a **rigorous review of the existing stock of**
318 **technical standards and guidelines with an eye to eliminating overlaps, contradictions,**
319 **needless detail or overreach compared to the respective Level 1 texts**. Many reporting,
320 disclosure, and prudential requirements could be slimmed down without impairing the
321 objectives of resilience and soundness.

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323 We call on the European Commission to be more restrained when it comes to suggesting new
324 delegated acts. At the same time, any new empowerments for Level 2 acts should be tightly
325 scoped to prevent overreach, and the European Supervisory Authorities should be mindful of
326 the proportionality principle when drafting standards.

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328 **Making supervision work: Clarity, accountability, competitiveness**

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330 A competitive banking system also depends on a supervisory architecture that is clear,
331 coherent and free of unnecessary duplication. Today, overlaps between European and
332 national authorities frequently result in inconsistent mandates and blurred accountability. A
333 **structural review of the supervisory framework** is therefore needed to recalibrate
334 competences between the national and European levels, eliminate duplication and ensure
335 that each body has a defined and non-overlapping purpose.

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337 Strengthening supervision must also go hand in hand with **addressing gold-plating**, where
338 national rules or supervisory expectations exceed EU requirements without clear justification.
339 This practice fragments the Single Market and undermines the level playing field. The
340 European Supervisory Authorities should be empowered to challenge disproportionate
341 national add-ons more effectively.

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343 To support Europe's broader growth agenda, the **mandates of the ESAs should be broadened**
344 **to include an explicit competitiveness and innovation dimension**. A modernised mandate
345 could take inspiration from the mandate of the U.S. Securities and Exchange Commission that
346 focusses on protecting investors, maintaining fair, orderly and efficient markets and
347 facilitating capital formation or the secondary mandates for the UK's PRA and FCA. Aligning
348 the ESAs' objectives with growth and competitiveness considerations as a formal secondary
349 objective would strengthen their ability to safeguard stability while also promoting a
350 regulatory environment that supports investment, innovation and economic growth across
351 the EU.

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355 **AML: the next big frontier for effective and proportionate supervision**

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357 Europe's fight against money laundering is entering a new phase, and the creation of the Anti-
358 Money Laundering Authority (AMLA) offers an opportunity to strengthen the effectiveness,
359 coherence and proportionality of the EU AML framework. A risk-based and proportionate
360 approach will be essential to ensure that reporting requirements remain proportionate and
361 resources are focused where risks are highest, while maintaining an efficient and workable
362 framework for all institutions. The exchange of data between supervisors, Financial
363 Intelligence Units, and obliged entities is key to ensuring that the EU has a strong AML
364 framework.

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366 The Commission should ensure that proportionality remains a core guiding principle in
367 AMLA's Level 2 work. Requirements must be calibrated to the size and risk profile of
368 institutions. **AMLA should focus on clear, risk-sensitive rules** rather than exhaustive
369 prescriptive detail.

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375 **Harnessing the power of new technology:**

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377 Technological progress is reshaping financial services, and Europe's banking sector must be
378 able to harness this transformation. Modern digital tools including artificial intelligence,
379 advanced data analytics and cloud-based platforms offer banks the opportunity to streamline
380 operations, reduce costs and improve the speed and quality of customer service. Banks
381 should be encouraged to deploy AI in areas such as credit scoring, creditworthiness
382 assessments and risk management, where it can reduce information asymmetries and
383 enhance resilience. This requires a **principles-based and proportionate approach to**
384 **regulation and supervision** so that innovative use cases can be tested without being
385 prematurely categorised as high-risk under horizontal AI rules. Most importantly, EU-level
386 regulation must not become an obstacle to technological adoption. There is already
387 uncertainty and confusion among market actors regarding compliant AI use due to overlaps
388 and interactions between the AI Act and sectoral financial services legislation, particularly
389 regarding internal governance and quality management processes. There is thus an urgent
390 need to clarify how sectoral rules already apply to the use of AI in finance and where they
391 already cover requirements set out in the AI Act, which would provide assurance, reduce
392 administrative burdens and support effective uptake.

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394 The **tokenisation of money and assets** has the potential to deliver real-time settlement, lower
395 transaction costs, greater liquidity and new business models, offering banks meaningful
396 efficiency gains. For Europe, this is both a technological and strategic opportunity: by shaping
397 the regulatory framework for digital assets in the right way, the EU can preserve its role in
398 global finance and avoid dependence on non-European providers that are rapidly expanding
399 in digital payment and settlement systems. A competitive European banking sector will
400 depend on a regulatory framework that enables innovation rather than slows it down.