Working Lunch: Competitiveness in the European Banking Sector – where are we?

Taking stock of 15 years of banking sector reform

Banks play a crucial role in driving investment and growth in Europe, given the EU economy's heavy reliance on bank-based financing. A strong EU banking sector is an indispensable building block of Europe's competitiveness agenda.

Over the last 15 years, we have overhauled our banking framework, motivated by the damage caused by the banking crisis. We have implemented substantial reforms along two inter-connected dimensions: 1) a European dimension, with the creation of the Banking Union, recognising the need in an Economic and Monetary Union for a single rulebook, consistent supervision and joint crisis management instruments, and 2) a global dimension, with the development of the international Basel III standard and its implementation in the EU.

These reforms have significantly bolstered the resilience of the European banking sector, leading to increased capital and improved asset quality on banks' books. This resilience was particularly evident during the pandemic, the Russian invasion of Ukraine, and wider geopolitical turmoil; the European banking sector has been a source of stability rather than weakness. At the same time, major challenges remain to be addressed, which the Commission has laid out in its communication on the Competitiveness of the Banking Sector and the Single Market in Banking published on 17 July 2026.

The European banking market continues to be highly fragmented along national borders, with cross-border lending only contributing 8% of the volume of total (non-intrabank) lending. This fragmentation and a lack of scale hampers banks' ability to finance Europe's economy and the EU's wider priorities and dampens their profitability. The largest EU banks are outperformed by their US peers with respect to profitability and valuations. At the beginning of the 2000s, the five largest EU banks individually had a higher market capitalisation than the largest US bank.

Today, the single largest US bank has a higher market capitalisation than the five largest EU banks, combined.

Figure 1 Reform of the EU banking framework

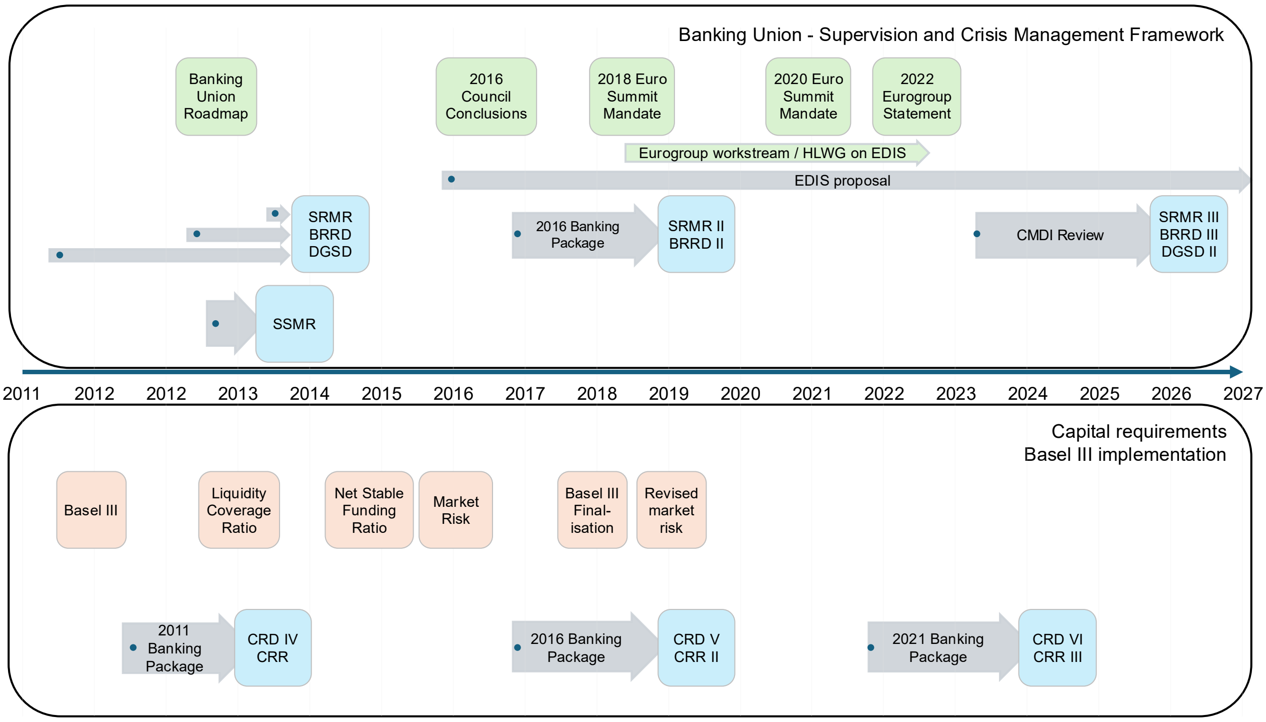
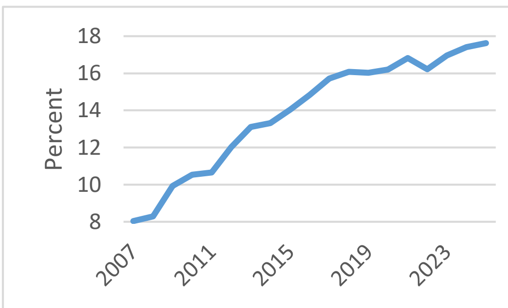
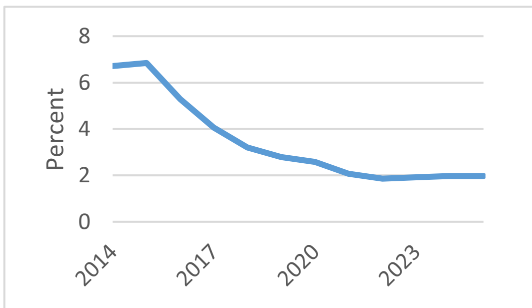


Figure 2 Increased resilience in the EU banking sector



EU banks financial strength (Tier 1 capital ratio). Source: ECB



Ratio of non-performing loans for EU banks (NPL-ratio). Source: ECB

Charting the path ahead

Banking reform remains a work in progress. On a global scale, the importance of maintaining a level-playing field with other jurisdictions in finalising the implementation of Basel III has come into focus. To this end, the European Commission recently introduced time-limited amendments to the new market risk framework. This illustrates that ensuring the competitiveness of the European banking sector remains an ongoing issue, as pressure to modernise or deregulate intensifies across jurisdictions.

While the Single Supervisory Mechanism (SSM) and the Single Resolution Mechanism (SRM) have been operational for more than a decade, Banking Union's third pillar, a common European Deposit Insurance Scheme (EDIS), originally proposed in 2015, has remained politically deadlocked. Following a mandate by the Euro Summit in 2018, the Eurogroup has been working on a way forward on Banking Union, culminating in its 2022 statement and paving the way to the Crisis Management and Deposit Insurance (CMDI) review.

In its communication, the European Commission has outlined its plan for the way forward. Based on an encompassing vision for the EU banking sector, it identifies three focus areas for its legislative proposal announced for Q1 2027:

- **Fostering integration with appropriate safeguards,** including by adapting the rules governing the intra-group movement of liquidity and capital, replacing the 2015 EDIS proposal with a new proposal to reform the deposit insurance framework, adopting measures regarding the resolution of cross-border banks and by addressing non-prudential barriers to integration.
- **Implementing international standards while taking account of EU specificities and ensuring proportionality,** including by making proposals regarding the output floor and its transitional arrangements in the EU's Basel III implementation, monitoring the implementation of international standards across jurisdictions and improving the framework's proportionality for small and non-complex banks.
- **Simplifying the regulatory framework,** including by improving bank-specific capital guidance (Pillar 2), reducing the number of macroprudential buffers, harmonising the framework for Other Systemically Important Institutions (O-SIIs), better aligning requirements stemming from the European resolution framework with international standards, improving coordination mechanisms and streamlining reporting requirements.

At the same time, the Commission is clear that legislative reform alone will not be enough to deliver a stronger and more competitive banking sector. Sustainable competitiveness will require broad buy-in on all levels, including market participants and supervisors, and a holistic approach to legislation and implementation.

Recognising the inherent trade-offs in banking reform between preserving resilience and promoting innovation, between fostering harmonisation and maintaining national discretion and between boosting competitiveness and managing the impact on capital requirements, the Commission emphasises the need for political judgement. Heeding the Commission's call for feedback in preparation of the upcoming banking package, this session provides the first opportunity to engage with the Commission's report on a political level, to assess the overall state of play in the banking sector, and to identify political priorities with a view to follow-up work including at the October ECOFIN.

Questions for discussion:

- What have been the key drivers and defining features of the banking sector's transformation and what is your vision for an ideal EU banking sector?
- Recognising that a fit-for-purpose banking framework must strike the right balance between banking sector resilience, competitiveness and capacity to meet the economy's financing needs, which of these objectives should be in focus in the upcoming banking package?
- What areas do you see as deserving more in-depth discussion, including at the October ECOFIN meeting, which might help inform and shape the upcoming banking package?