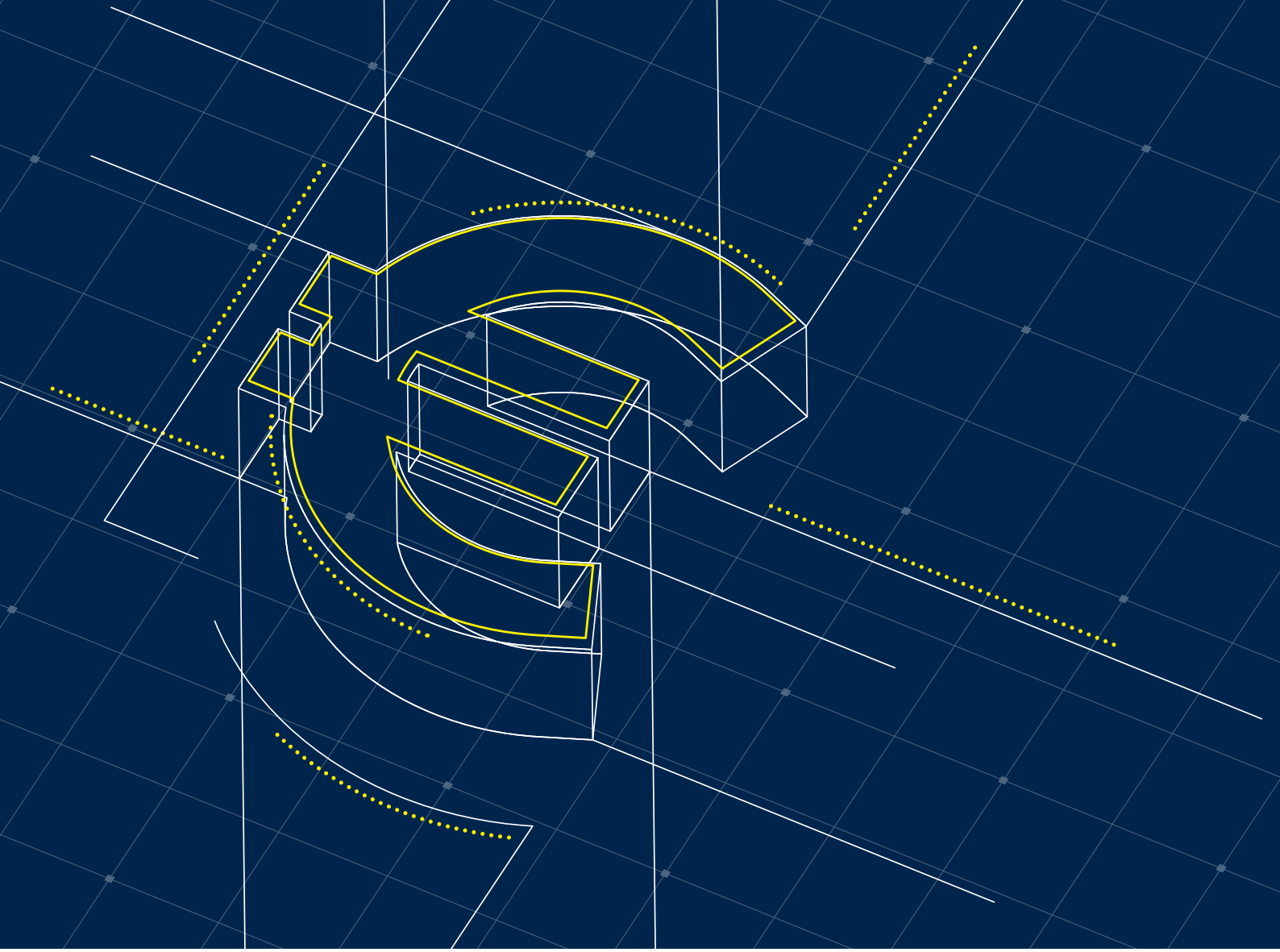

Unlocking Bank Capital to Support Europe's Competitiveness

BPFI proposals for a simpler and more effective EU banking framework

Banking & Payments Federation Ireland

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Executive Summary

Europe faces a defining competitiveness challenge. Delivering stronger growth, greater strategic autonomy, more housing, deeper capital markets, digitalisation, decarbonisation and defence investment will require capital at a scale Europe has not mobilised in decades. The Draghi report identified an annual EU investment gap of around €800 billion, while more recent analysis suggests that Europe's wider strategic investment needs may be closer to €1.2 – €1.4tn per year when energy, digital infrastructure, defence, innovation and environmental resilience are considered together.

Banks will be central to meeting this challenge. Europe remains a largely bank-based financial system, and banks are essential to financing households, SMEs, corporates, housing, infrastructure and the transition economy. They are also critical to building deeper capital markets through origination, underwriting, securitisation, market-making, distribution and investor intermediation.

At the same time, the EU banking framework has delivered resilience as shown through numerous recent crises. European and Irish banks are well capitalised, liquid and strictly supervised. However, resilience alone is no longer sufficient. The cumulative layering of capital requirements, supervisory expectations, reporting obligations, macroprudential buffers and national discretions is constraining the ability of banks to deploy capital efficiently in support of the real economy.

BPFI's position is clear: this is not a call for deregulation. It is a call for a simpler, more proportionate and more coherent framework that preserves financial stability while enabling capital to flow more efficiently to households, businesses and strategic EU priorities.

We recommend that the EU should:

- **Streamline and simplify the regulatory framework**, including the capital stack, Level 2 and Level 3 rulemaking, supervisory guidance and macroprudential buffers.
- **Update the capital framework so that it better reflects underlying risk**, including improved underwriting standards, borrower-based macroprudential measures, collateral, social and affordable housing lending, and technology investment.
- **Embed genuine proportionality across regulation and supervision**, particularly for smaller, medium-sized and lower-risk banks, and for institutions with simpler business models.
- **Complete the Banking Union and remove barriers to scale**, including trapped capital and liquidity within cross-border banking groups.
- **Ensure a level playing field within the EU and globally**, by reducing gold-plating, national divergence and international competitive disadvantages.
- **Support market liquidity and capital markets intermediation**, through recalibration of securitisation and investment firm rules.
- **Simplify the digital and payments framework to support innovation** by avoiding regulatory overlap, ensuring proportionality and safeguarding investment in digital and cyber resilience.

Ultimately, Europe needs banks with greater capacity to support growth, so the goal should be a banking framework that is safe, simple, proportionate and growth-enabling.

Context: Why bank competitiveness matters for Europe

Europe's competitiveness challenge is now widely recognised. The Draghi report highlighted the scale of the investment needed to restore productivity, support decarbonisation, advance digitalisation and strengthen Europe's strategic autonomy.

This investment challenge cannot be met by public finance alone. Nor can it be met solely through capital markets, given that Europe's Savings and Investment Union (SIU) remains incomplete and market-based finance remains less developed than in other major jurisdictions. Europe therefore needs a financing system that combines resilient banks, deeper capital markets and better connections between savings and productive investment. Banks are central to that system. They provide loans to households and businesses, support SMEs and corporates, finance housing and infrastructure, and help channel investment into capital markets.

However, Europe's banking sector is operating within a framework that has become increasingly complex, capital-intensive and fragmented. Post-crisis reforms have made banks safer and more resilient, but the cumulative effect of regulation, supervisory expectations, macroprudential buffers, national discretions and reporting obligations has created costs and constraints that can limit the ability of banks to support long-term growth.

For Ireland, these issues are particularly important. Banks in Ireland have significantly strengthened post-financial crisis, with better asset quality, stronger governance, and more conservative lending practices. At the same time, Irish banks continue to operate in a small market with high fixed costs, significant regulatory and supervisory intensity, and capital requirements that remains significantly higher than the European average.

A stronger EU banking sector is therefore not a narrow sectoral objective. It is a strategic economic requirement. If Europe wants to finance housing, SMEs, innovation, infrastructure, decarbonisation and digitalisation, it must ensure that banks can deploy capital efficiently while continuing to operate safely.

BPFI's core position: Resilience and competitiveness must be pursued together

The EU banking framework has been designed, understandably, with financial stability as its central objective. That objective must remain paramount. But the next phase of reform should recognise that financial stability and competitiveness are not competing goals. A profitable, investable and efficient banking sector is better able to generate capital organically, invest in technology and cyber resilience, support customers through the cycle and finance the real economy. Conversely, a structurally constrained banking sector will be less able to support Europe's wider economic and strategic objectives.

EU banks are not currently a primary source of systemic risk. They are well capitalised, liquid and supported by solid asset quality. The main challenge is longer-term earnings capacity and competitiveness in a market that remains fragmented, capital-intensive and increasingly exposed to competition from large international competitors.

The current improvement in the earnings of European banks should not obscure the fact that the balance of power in global finance has shifted since the financial crisis. Without strategic adjustments, this trend is likely to continue, especially given other jurisdictions, such as the US, intend to further reduce the regulatory burden on their banks.

The policy question is therefore whether the framework has reached a point where additional complexity is delivering diminishing financial stability benefits while imposing real costs on lending capacity, market integration and investment. In other words, European banks have become safer, but also more constrained, with higher capitalisation, more liquid balance sheets and a shift towards lower-risk activities. This matters from a long-term public policy perspective that all stakeholders need to reflect upon. Europe needs economic growth in order to fund its social model and fundamentally this requires a rebalancing of risk appetite within the economy to incentivise this growth. For the banking sector, the focus should be on simplification, proportionality, consistency and capital efficiency. That means removing duplication, reducing unnecessary supervisory burden, recalibrating rules where they do not reflect actual risk, and ensuring that EU banks can compete on equal terms within Europe and globally.

1

Priority One: Streamline and simplify the regulatory framework

The EU banking framework has become increasingly complex, with requirements layered across Level 1 legislation, Level 2 measures, Level 3 guidance, supervisory expectations, national implementation and macroprudential decisions.

The problem is not any one rule in isolation. It is the cumulative effect of multiple requirements that may target similar risks through different channels. Pillar 1, Pillar 2, the capital conservation buffer, countercyclical capital buffer, systemic risk buffer, O-SII buffer, Pillar 2 guidance and supervisory add-ons can overlap in ways that are difficult to justify from a risk perspective.

This complexity has real-world consequences. Capital that is held against duplicative or overlapping requirements is capital that cannot be used to support additional lending for housing, infrastructure or SME expansion. Complexity also reduces predictability for investors, increases compliance costs and makes it harder for banks to plan strategically.

BPFI recommends that the EU should:

- Conduct a full review of the capital stack to identify overlaps between Pillar 1, Pillar 2 and macroprudential requirements.
- Ensure that risks already addressed through borrower-based macroprudential tools, underwriting standards or Pillar 1 requirements are not duplicated through additional buffers.
- Reduce reliance on Level 2 and Level 3 measures where they materially expand or alter the policy intent of Level 1 legislation.
- Improve transparency around Pillar 2 requirements, by requiring supervisors to explain the risk drivers, expected remediation path and conditions for removal of add-ons.
- Introduce a formal competitiveness and proportionality check for new banking rules and supervisory measures.

A simpler framework would not result in a weaker framework. It would mean it is easier to understand, more predictable to supervise, less costly to comply with and better aligned with the risks it is intended to address.

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Priority Two: Update capital rules so they better reflect underlying risk

Capital requirements should be robust and reflect real underlying risk. In our view, the existing requirements do not always reflect the actual risk profile of bank balance sheets, particularly where major risk-mitigating measures are already in place.

This is particularly relevant in Ireland. Since the financial crisis, underwriting standards have improved materially and macroprudential borrower-based measures such as strict loan-to-value and loan-to-income limits have helped create more conservative mortgage books. Yet this improvement is not always reflected in capital calculations, partly because banks internal models are based on historical losses and the likelihood of those losses reoccurring.

We therefore recommend that the EU capital framework should be updated in four areas.

- Capital requirements should take better account of improved underwriting standards and macroprudential measures. Where borrower-based tools materially reduce credit risk, the capital framework should recognise this rather than relying solely on historical loss experienced from a period before those tools existed.
- The EU should review whether total Tier 1 capital levels remain appropriately calibrated, taking account of approaches in other major jurisdictions and the cumulative impact of requirements across the stack. Our objective is to ensure the overall capital in the system is appropriate.
- The framework should support lending for social and affordable housing across all Member States. The current rules favour certain market structures, but all EU banking markets should be able to benefit from lower requirements where lending supports social and affordable housing. This is particularly important given the supply of housing in Ireland and across the EU.
- The EU should remove the CET1 deduction for software assets. At a time when banks are expected to invest heavily in digitalisation, fraud prevention, cyber resilience, data infrastructure and customer service, the prudential framework should not unnecessarily penalise technology investment.

More broadly, we believe capital should be associated with risk. Where risk is lower, better managed or already mitigated, the framework should reflect that reality. This would improve capital efficiency without reducing resilience.

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Priority Three: Embed genuine proportionality

Proportionality has long been recognised as an EU principle, but it is not sufficiently embedded in practice. Smaller, medium-sized and less complex banks often face requirements designed for larger and more complex institutions. This creates disproportionate compliance costs, diverts management attention and can weaken competition by making it harder for smaller firms to absorb fixed regulatory costs.

This issue is especially relevant in smaller Member States where banks cannot spread fixed regulatory, reporting, technology and compliance costs across the same scale as larger institutions in larger jurisdictions. It is the scale and weight of operating costs, including regulation, innovation, IT and labour costs, that have a major impact on profitability, alongside the interest rate environment.

We recommend a more effective proportionality framework based on the following principles:

- Requirements should be linked to business model, risk profile, complexity and systemic footprint, rather than applied in a largely uniform way.
- The EU should create a simplified prudential and supervisory regime for small and medium-sized low-risk banks (e.g. above its current €5bn regime), based on harmonised EU-wide criteria.
- Reporting obligations should be reduced where data is duplicative, rarely used or not proportionate to the risks being supervised.
- Supervisory engagement should be outcomes-focused and risk-based, with better coordination across horizontal teams, supervisory teams and inspection processes.
- Supervisory fees and information requests should be subject to stronger discipline and proportionality controls.

Proportionality is essential to a competitive and diverse banking system. Europe benefits from a varied banking landscape, including universal banks, local lenders, mortgage banks, specialist institutions, digital banks, investment firms and international banks. This diversity is an economic and strategic asset that supports resilience, competition and access to finance.

4

Priority Four: Complete the Banking Union and remove barriers to scale

Europe's banking market remains fragmented. Despite the Single Rulebook and the Single Supervisory Mechanism (SSM), banks continue to face national barriers, trapped capital and liquidity, divergent supervisory practices, different insolvency regimes, different consumer protection rules and inconsistent implementation of EU law.

This fragmentation prevents banks from realising the full benefits of scale. It weakens the business case for cross-border activity, reduces efficiency and limits the ability of banking groups to allocate resources where they are most needed. As is often highlighted, capital and liquidity are trapped within national borders, reducing the ability of banks to deploy resources efficiently across the Single Market.

Completing the Banking Union should therefore remain a strategic priority. But we also recognise that progress is likely to be gradual. For that reason, work on the Banking Union should not delay more immediate reforms to the prudential and supervisory framework. The EU should pursue both tracks at the same time - near-term simplification and recalibration, alongside longer-term integration.

To achieve this, we recommend that the EU should:

- Make better use of existing rules to permit the movement of capital and liquidity within banking groups.
- Harmonise national discretions and options to ensure a true Single Rulebook and level playing field.
- Harmonise key areas that affect cross-border banking, including insolvency, collateral enforcement and supervisory processes.
- Support cross-border consolidation where it strengthens efficiency, resilience and customer choice.
- Ensure that macroprudential requirements – in particular the OSII & CCyB buffers – are calibrated in a way that does not disproportionately affect banks in smaller Member States.

Completing the Banking Union is a longer-term project, but practical measures can be taken now to reduce fragmentation and improve capital mobility.

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Priority Five: Ensure a level playing field within the EU and globally

A competitive banking sector requires a level playing field. This means consistency within the EU and fairness between EU banks and global competitors. Too often national gold-plating remains a significant problem. Such additional national requirements can increase costs, deter new entrants, encourage firms to locate elsewhere, divert resources from innovation and weaken investor perception.

As a priority, the EU should tackle gold-plating by making greater use of regulations rather than directives. Regulations can reduce divergent implementation and support a more consistent Single Rulebook.

The EU should also engage with Member States on domestic measures that distort the level playing field such as specific bank taxes, inconsistent resolution requirements or obligations imposed only on certain market participants.

International competitiveness also matters. EU banks compete with global peers that may operate in larger, more integrated home markets and under different regulatory, remuneration and market structures. As an example, US banks benefit from deeper capital markets, greater scale, a more developed securitisation market, government-sponsored entities in mortgage finance and a more unified legal and regulatory environment, all of which support the growth of its banking sector.

We recommend that the EU should:

- Ensure gold-plating does not occur in the implementation of international and EU rules.
- Make greater use of regulations rather than directives where consistent application is essential.
- Benchmark EU requirements against those in other major jurisdictions.
- Ensure that EU-specific requirements are justified by clear evidence of additional risk.
- Re-examine remuneration rules where they undermine competitiveness.
- Apply a competitiveness check before introducing new regulatory or supervisory requirements.

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Priority Six: Support market liquidity and capital markets intermediation

A stronger banking sector and deeper capital markets are mutually reinforcing. Europe's SIU will not succeed if banks are treated as separate from, or secondary to, capital markets development. Banks are central to origination, underwriting, market-making, securitisation, custody, distribution and investor intermediation.

BPFI therefore supports reforms that improve market liquidity and enable effective capital markets intermediation.

Securitisation

A particular priority is securitisation. This is a vital tool for connecting capital markets with corporate debt financing, freeing up bank balance sheets and creating investment opportunities for institutional investors. Given the size of the EU, the market is moribund, especially compared to that of the US where securitisation acts as a key bridge between bank-based financing and capital markets.

The EU's securitisation framework should therefore be recalibrated to support issuance and investment while maintaining appropriate safeguards. We recommend that policymakers should:

- Recalibrate p-factors and risk-weight floors to make securitisation economically viable for a broader range of assets.
- Streamline safeguards and remove overlapping or unnecessary requirements.
- Support investor demand by making due diligence requirements more proportionate and ensuring EU investors can access diversified global securitisation markets.
- Improve liquidity treatment so that securitisations are not unfairly disadvantaged compared with similar instruments such as covered bonds.
- Ensure that the definition of "resilient positions" is broad enough to support meaningful market development.

Investment firms and market liquidity

EU regulations and directives in relation to investment firms also require adjustment. In our view, the relevant legislation should better reflect the business models and risk profiles of non-bank intermediaries, including market makers and proprietary trading firms that do not take deposits or engage in maturity transformation.

This matters because these firms support liquidity, price formation and market depth, which are all critical to the development of a well-functioning SIU. A framework that treats them too much like banks can overstate their risk and reduce their ability to support capital markets.

We recommend that the EU should:

- Improve proportionality within the IFR/IFD framework.
- Revisit classification thresholds and governance requirements.
- Ensure prudential requirements support, rather than weaken, liquidity provision.
- Remove proprietary trading firms from resolution fund contributions where they would be wound down rather than resolved.
- Ensure that regulation supports market depth and price formation.

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Priority Seven: Simplify the digital, cyber and payments framework to support innovation

Digital, cyber and payments regulation has expanded significantly in recent years. The EU has introduced or advanced major initiatives across operational resilience, cyber security, open finance, payments, artificial intelligence and the digital euro. These initiatives are individually important, but collectively they can create overlap, cost and uncertainty. In our view, they should be assessed holistically to avoid duplication and ensure that innovation, efficiency and resilience are supported.

We recommend that the EU should:

- Avoid duplication between DORA and broader cyber legislation – particularly the Cyber Resilience Act.
- Simplify FiDA so that it is market-driven, customer-focused and proportionate.
- Ensure that any digital euro complements, rather than duplicates, trusted private-sector payment solutions.
- Preserve the ability of banks to invest in digital services, fraud prevention and cyber resilience.
- Assess the cumulative impact of digital regulation on cost, innovation and competitiveness.

Conclusion

Europe's banking framework has delivered resilience. The task now is to ensure that it also supports competitiveness, investment and growth. The EU does not need to choose between financial stability and economic dynamism; it can have both. However, this requires a shift in policy focus from further increasing regulation to simplification; from fragmentation to integration; and from uniformity to proportionality.

BPFI's proposals are practical and targeted. They do not seek to weaken prudential standards. They seek to make those standards more effective, coherent and supportive of Europe's wider economic objectives.

A competitive European economy needs competitive European banks. Unlocking bank capital is therefore not just a banking issue, it is central to Europe's ability to finance its future.

Banking & Payments Federation Ireland,
Floor 3, One Molesworth Street,
Dublin 2, D02 RF29, Ireland.

info@bpfi.ie
www.bpfi.ie

Dublin • Brussels • Frankfurt