European Banking Union: from firewall to engine of growth

The European banking sector is in a stronger position than it was a decade ago, yet it remains too fragmented to play its full role in financing Europe's strategic agenda. Completing the Banking Union, alongside achieving deeper capital markets, is no longer merely a matter of financial stability: it is a key lever for mobilising savings, achieving scale, reducing financing costs and narrowing Europe's investment gap. Ultimately, it is a driver of competitiveness and growth.

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A new context: the Commission places banking at the heart of the competitiveness agenda

The Banking Union was created in response to a crisis. Its original objective was to break the vicious circle between banks and national governments, enhance the credibility of supervision and establish common mechanisms for managing banking crises without burdening taxpayers. In this respect, progress has been considerable: common supervision, European resolution mechanisms, and stronger capital and liquidity positions have made the euro-area banking system more resilient than it was before 2012.

Completing the Banking Union is not a matter of technical reform: it represents an agenda for growth, competitiveness and strategic autonomy

However, nowadays the debate in Europe is different. The question is no longer simply whether banks are sufficiently resilient, but whether Europe has a financial architecture capable of transforming its savings into productive investment and, ultimately, fostering competitiveness and growth. The European Commission[1] is working to resolve this question under the umbrella of the Savings and Investments Union (SIU), designed to connect citizens' savings with productive investment, broaden companies' sources of finance and reduce fragmentation within the Single Financial Market.

The Commission's roadmap organises the SIU initiative around four areas: citizens' savings, investment and financing of the real economy, integration and scale, and efficient supervision within the Single Market.

Therefore, throughout this analysis, we to the Banking Union as a broad concept. Here it encompasses not only a common supervision, resolution framework and European Deposit Insurance Scheme (EDIS), but also the wider institutional, regulatory and market architecture required for banks to operate across the European Union (EU) as a genuine single market — including the cross-border mobility of capital and liquidity,

[1] European Commission (2025), 'The Savings and Investments Union: Connecting savings and productive investments', factsheet.

reduced national fragmentation, and greater consistency across prudential, crisis-management, insolvency and deposit-protection frameworks.

The policy debate has now moved from diagnosis to implementation. In July 2026, the European Commission adopted its Communication on the competitiveness of the EU banking sector and the Single Market in Banking. It identifies three connected constraints: persistent national fragmentation, an implementation of international standards that does not always reflect the specific features of the EU banking system, and undue regulatory complexity. The Commission intends to translate this diagnosis into legislative and non-legislative measures in the first quarter of 2027. Banking integration has therefore become a core component of Europe's competitiveness agenda.

The ECB estimates that the EU's strategic financing needs for the green, digital and defence transitions will average close to 1.2 trillion euros per year over the 2025–2031 period

Among the announced measures are proposals to facilitate the group-wide allocation of capital and liquidity, a new common deposit insurance proposal replacing the 2015 EDIS initiative, and targeted simplification of prudential, supervisory and resolution requirements, while preserving financial stability and appropriate safeguards for host jurisdictions.

The new macrofinancial environment reinforces the urgency. The European Central Bank (ECB)[2] estimates that the EU's strategic financing needs for the green, digital and defence transitions will average close to 1.2 trillion euros per year over the 2025–2031 period. At this scale, completing the Banking Union ceases to be an unfinished institutional project and becomes a lever for mobilising private capital, increasing financing capacity and strengthening Europe's economic autonomy.

The Banking Union has made banks stronger, but it has not yet created truly pan-European banks

Diagnosis: stronger banks, but a market that remains national

The current problem is not banks' solvency. It is one of scale, resource mobility and the ability to operate in a continental market

The European paradox is clear: there is greater resilience, but not significantly greater integration[3]. The Banking Union has improved the quality of supervision, reduced legacy risks and strengthened banks' loss-absorbing capacity. Nevertheless, lending, deposits, mergers, capital and liquidity management, and business models continue to be organised largely along national borders.

Recent microeconomic evidence is compelling. Research by the ECB and the International Monetary Fund (IMF)[4] based on AnaCredit and RIAD shows that cross-border bank lending to firms within the euro area has accounted for less than 6% of total lending to non-financial corporations since 2019. In the most relevant dimension — the bank-firm relationship — integration is even lower: cross-border relationships

[2] Bouabdallah, O., Dorrucci, E., Nerlich, C., Nickel, C. and Vlad, A. (2025), 'Time to be strategic: how public money could power Europe's green, digital and defence transitions', The ECB Blog, 25 July.
[3] Angeloni, I., Haselmann, R., Heider, F., Pelizzon, L., Schlegel, J. and Tröger, T. H. (2024), 'Can Banking Union foster market integration, and what lessons does that hold for capital markets union?', European Parliament, EGOV.
[4] Capelle, D., Fernandes, A., Kruger, J. J. and McAdam, P. (2026), 'Barriers to a European Banking Union', IMF Working Paper WP/26/123 and ECB Working Paper Series No. 3249.

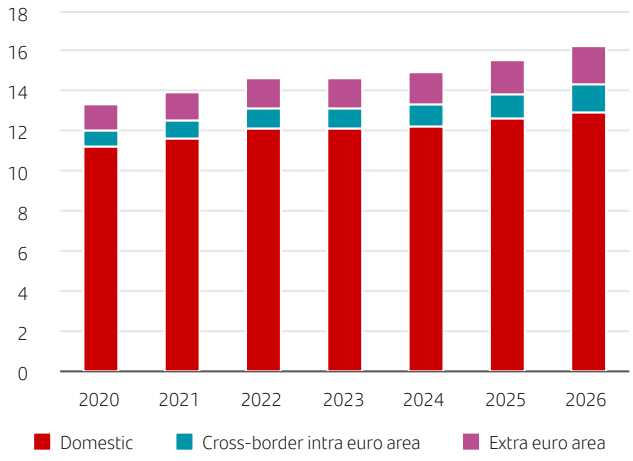
account for less than 1% of the total, although they tend to be larger than domestic ones.

As the European Commission shows, 56% of EU banks' exposures are in their home country. Cross-border exposures are almost evenly split between other EU countries (21%) and non-EU markets (22%), suggesting that expanding within the EU can be as difficult as expanding outside it[5].

Fragmentation is also evident in corporate operations. A 2025 assessment by the Association for Financial Markets in Europe (AFME) found that cross-border banking services remain marginal, subsidiary and branch activity has failed to create a de facto single banking market, deposit and lending activity has scarcely increased, and cross-border consolidation has weakened over the past two decades, with major banking groups continuing to display a strong domestic bias.

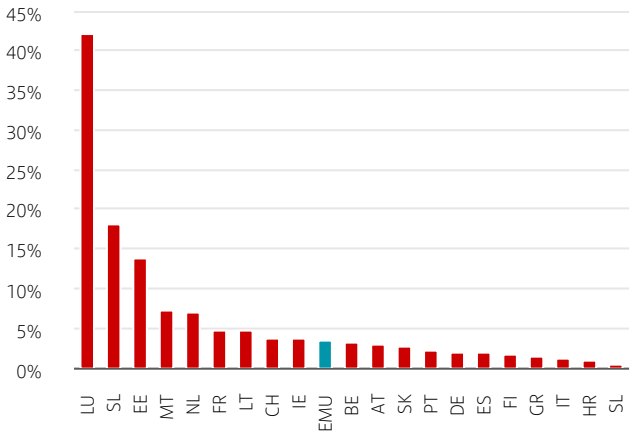
This domestic bias matters because it reduces effective competition[6] and limits the matching of firms with financiers. A European company does not necessarily gain access to the European bank best suited to its risk profile, but rather to the intermediary available within its own jurisdiction. In a single market seeking to finance innovation, infrastructure and the green transition, these invisible borders have tangible effects on competitiveness, productivity and, ultimately, economic growth.

Stock of retail bank loans in the euro area
(Trillion €)



Source: ECB.

Share of cross-border deposits in the euro area
(March 2026)



Source: ECB.

[5] European Commission (2026), Impact Assessment Report accompanying the proposal on the completion of the Banking Union, Commission Staff Working Document, SWD/2026/615 final.
[6] Buch, C. (2025), 'European banking integration: harnessing the benefits, containing the risks', speech, European Central Bank.

Invisible barriers: higher costs, less scale

Up to 475 billion euros of capital and liquidity is estimated to be constrained at subsidiary level

The barriers to banking integration do not usually take the form of explicit prohibitions. Instead, they operate as regulatory and institutional frictions: capital and liquidity requirements at subsidiary level, national discretions, differences in insolvency regimes, national deposit guarantee schemes, limits on intra-group exposures, divergent supervisory practices and the costs of entering other markets.

The most obvious obstacle is so-called "ring-fencing". Although the common prudential framework allows certain requirements to be assessed on a consolidated basis, in practice, cross-border subsidiaries continue to retain capital and liquidity within each jurisdiction. ECB Banking Supervision estimates that the transferability of around 230 billion euros of high-quality liquid assets is constrained by the application of full liquidity requirements at national level. AFME[7] separately estimates that around 250 billion euros of liquidity and 225 billion euros of capital are constrained within subsidiaries of EU banking groups. These estimates illustrate the scale of balance-sheet fragmentation, although they should not be interpreted as immediately deployable lending capacity and not all of the capital held at subsidiary level necessarily results from prudential ring-fencing. This immobilisation reduces balance-sheet efficiency, discourages cross-border expansion and limits the ability to reallocate resources to where they are most productive or most needed during periods of stress.

A common European deposit insurance scheme: aligning risk-sharing and depositor protection at European level creates the conditions for capital and liquidity to move more freely across borders

The second barrier is the absence of an EDIS. As long as deposit protection continues to rely on national schemes, host supervisors will retain incentives to preserve resources within their own borders, while depositors will continue to perceive differences in safety depending on the jurisdiction. A common European deposit insurance architecture is therefore not merely a symbolic component of the Banking Union: by aligning risk-sharing and depositor protection at European level, it could help create the conditions for capital and liquidity to move more freely across borders while addressing legitimate host-country concerns.

The third barrier is regulatory and legal heterogeneity. The ECB/IMF research[8] measures regulatory distance between countries and finds that differences in national frameworks — including insolvency, deposit insurance, corporate governance, macroprudential and microprudential regulation, resolution and supervision — are associated with greater frictions when it comes to establishing cross-border banking relationships and enabling banks' entry into other countries.

The most important finding is that the main friction arises before any loans even exist. The estimates point to an extensive-margin problem: cross-border bank-firm relationships are around 95% less likely to develop than comparable domestic relationships. The IMF[9] translates this model-implied wedge into an implicit tax of approximately 99%. Once the relationship has been established, however, differences

[7] Association for Financial Markets in Europe (2025), 'Banking Union: measuring progress and identifying implementation gaps'.
[8] Capelle, D., Fernandes, A., Kruger, J. J. and McAdam, P. (2026), 'Barriers to a European Banking Union', IMF Working Paper WP/26/123 and ECB Working Paper Series No. 3249.
[9] Brandao-Marques, L. et al. (2026), 'Deeper and More Integrated Financial Markets to Foster Growth and Resilience in Europe', IMF Staff Discussion Note SDN/2026/002.

in pricing and lending volumes are much smaller. The policy priority, therefore, is not merely to reduce the cost of existing relationships, but to make it possible for many more European bank-firm relationships to be established.

Benefits: from 3% of GDP to Europe's strategic investment challenge

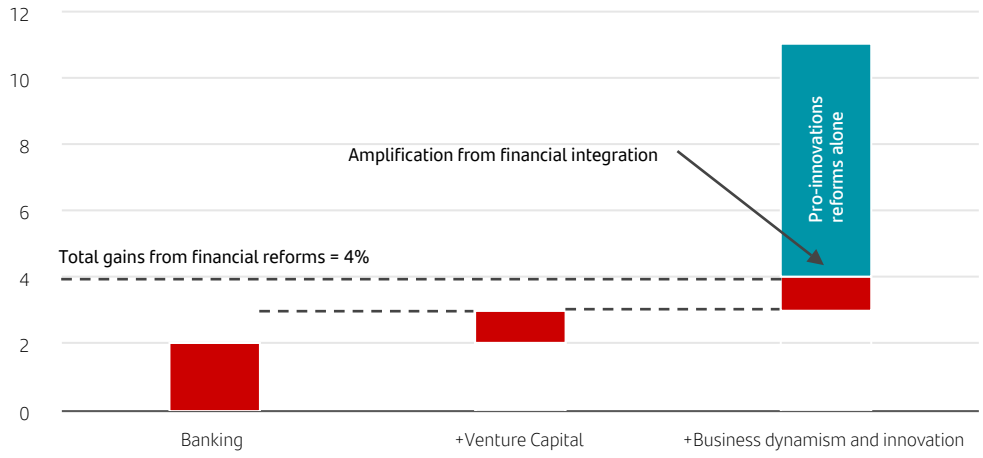
Banking Union could unlock up to €310bn annually, delivering a powerful boost to euro-area growth and competitiveness.

Quantification helps transform an institutional discussion into an economic agenda. The IMF estimates that a moderate package of financial reforms could increase EU gross domestic product (GDP) by around 3% in the long term, with approximately two-thirds of this gain stemming from deeper banking integration and the remainder from greater development of venture capital and risk financing. Moreover, these financial reforms would amplify the benefits of real structural reforms aimed at enhancing business dynamism and innovation.

Applied to the current size of the euro-area economy, the order of magnitude is highly significant. Taking the euro area's annual nominal GDP in 2025 (approximately 15.8 trillion euros) as a reference, a 3% increase in GDP would amount to around 474 billion euros extra per year. The banking component of the IMF's estimated effect — roughly two-thirds — would represent approximately 316 billion euros annually.

An alternative estimate from the ECB/IMF study, which simulates a 10% reduction in the barriers to forming cross-border banking relationships, points to a GDP gain of around 1.6%, equivalent to approximately 253 billion euros per year. In any case, the studies reach the same conclusion: advancing the Banking Union would generate tangible and substantial benefits of between 250 billion euros and 310 billion euros to support competitiveness and growth.

More integrated and deeper financial markets could raise Europe's GDP
(% change)



Source: IMF.

The comparison with Europe's strategic investment needs is striking. If Europe requires approximately 1.2 trillion euros of additional investment each year to finance its green, digital and defence transitions, the bill would exceed 6 trillion euros over five years. Total financial integration could amount to almost 40% of that cumulative figure in terms of additional annual economic capacity. The banking component alone would cover slightly more than one-quarter. Even the more conservative scenario of a 1.6% increase in GDP would cover approximately one-fifth.

A note of caution is important: this does not represent budgetary resources available from the first year, nor are we talking about a direct fiscal transfer. What we're looking at is an increase in the long-term level of GDP. However, the scale changes the debate. Completing the Banking Union would not, on its own, finance Europe's investment needs, but it would generate a macroeconomic dividend equivalent to a very substantial share of them. That is a significant difference.

Banking integration is essential to unlock growth, investment and competitiveness.

Simplifying to finance investment, innovation and employment

Policy priorities: turning the SIU into a banking agenda for growth.

The Commission's agenda offers a window of opportunity that must be translated into operational reforms. The SIU should not be viewed as a capital markets agenda separate from banking. In Europe, banks, securitisation, venture capital, equity markets, pensions and retail investment all form part of the same financing chain. They are part of a single ecosystem. Without a more integrated banking sector, the SIU risks mobilising savings without removing one of the principal bottlenecks in Europe's financial system.

Europe does not lack savings or capital; it lacks alignment between stability, growth and competitiveness.

In the short term, the priority is to align supervision with growth. This means: introducing a formal secondary objective of competitiveness and growth for supervisors alongside the primary mandate of financial stability; strengthening the accountability of the Single Supervisory Mechanism (SSM); simplifying regulation and supervision; requiring robust and independent cost-benefit analyses for new rules; and undertaking a holistic review of regulation and excess capital requirements to avoid overlaps between Pillar 1, Pillar 2, capital buffers, add-ons and margins of conservatism.

A more competitive framework should also recognise the international footprint of European banking groups. When calculating consolidated prudential requirements, the EU should allow appropriate recognition — upon request by the institution and subject to robust supervisory assessment — of equivalent local regulatory and supervisory frameworks, as well as the economic realities of the jurisdictions in which subsidiaries operate. Mechanically applying EU assumptions to third-country exposures can overstate risks, create unjustified capital burdens and penalise geographically

diversified European banks, weakening their ability to compete internationally without delivering commensurate benefits for financial stability.

In the medium term, the agenda should accelerate the SIU, simplify resolution and digitalisation, and prevent new technological frameworks from overlapping incoherently. In the field of resolution, the priority is to align the Minimum Requirement for Own Funds and Eligible Liabilities (MREL) and Total Loss-Absorbing Capacity (TLAC) requirements for major European banks, while avoiding duplications that increase funding costs without clear prudential justification. In the digital sphere, the challenge is to reduce overlaps between the various regulatory frameworks (Artificial Intelligence, the General Data Protection Regulation (GDPR), cybersecurity and the Digital Operational Resilience Act (DORA)), ensure fair competition with large technology platforms and design the digital euro in a way that preserves financial stability without undermining banks' funding base.

The Banking Union must cease to be a defensive architecture born out of crisis and become an infrastructure for growth

In the longer term, completing the Banking Union will be essential. The Commission's intention to replace the 2015 EDIS proposal with a new common deposit insurance architecture could provide a pragmatic route forward. The new framework should align responsibilities for crisis management with the financing of deposit protection, ensure equal protection of covered deposits, address potential liquidity shortfalls in national schemes and provide credible safeguards for host jurisdictions.

This should be accompanied by greater cross-border mobility of capital and liquidity, reduced national divergences in areas such as mortgage regulation, consumer protection and anti-money laundering/countering the financing of terrorism (AML/CFT) requirements, more effective digital onboarding, and a more jurisdiction-neutral framework for banking groups with significant pan-European operations.

The proposal to establish a European deposit insurance scheme by building on existing structures[10], such as the Single Resolution Fund, points towards a pragmatic solution: less duplication, greater confidence and a safety net consistent with a genuine European banking market.

Conclusion

Europe has made substantial progress in banking resilience, but far too little in integrating its national banking systems. The Banking Union has functioned as a shield, but not yet as an engine. The result is a contradiction: an economy that needs to mobilise around 1.2 trillion euros of additional investment every year, with abundant private savings and strong banks, yet with a financial system that continues to operate behind too many internal borders and is therefore unable to channel the existing raw material into competitiveness and growth.

Banking fragmentation is not a minor issue. It reduces competition, raises financing costs, limits economies of scale, immobilises capital and liquidity, hinders the expansion of European companies and weakens the capacity to absorb shocks. Recent

[10] Banco Santander (2026), 'Santander proposal of measures to promote competitiveness in the EU/concrete proposals on competitiveness'.

evidence shows that the greatest frictions arise before credit is granted: when banks enter new markets and when cross-border banking relationships are established.

Europe has savings, strong banks and investment needs. What it lacks is integration

The Commission now has a window of opportunity. The SIU, the 2026 report on the competitiveness of the European banking sector and the 2027 mid-term review can transform what has historically been a defensive agenda into one centred on growth. To achieve this, Europe must move decisively in a clear direction: less internal fragmentation, greater intra-group mobility of resources, more European supervision and resolution, lower regulatory complexity, and an explicit link between financial stability, competitiveness and the financing of the real economy.

Only then will the Banking Union cease to be an unfinished institutional project and become one of the principal levers for financing Europe's economic future.