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PMEU targeted reply to the consultation on the competitiveness of the EU banking sector

1. How is the banking sector currently supporting economic growth in the EU, and to what extent (for example, by providing loans to households and businesses, supporting innovative sectors, and helping channel investments into capital markets (including for retail investors))? How could banks do more to boost productivity and economic growth, thereby supporting the priorities of the EU and accelerating the green, digital and social transitions? Please give concrete examples and evidence.

EU banks remain the backbone of European corporate finance and continue to play a central role in supporting economic activity. Bank loans account for approximately 75% of corporate borrowing in the EU and around 30% of total external funding, while banking sector assets represent close to 290% of EU GDP. This structurally bank-based system contrasts with the United States, where capital markets play a significantly larger role. As a result, European banks are the primary providers of finance to households and firms, particularly small and medium-sized enterprises (SMEs), which remain heavily dependent on bank lending.

However, this central role also means that weaknesses in the banking sector translate directly into constraints on economic growth. Despite its scale, the EU banking system does not allocate capital efficiently across the Union. Cross-border lending has declined since 2014, and banking consolidation remains overwhelmingly domestic. National ring-fencing of capital and liquidity continues to fragment the internal market and prevents banking groups from reallocating resources where they are most needed. This fragmentation contributes to persistent divergences in financing conditions, with higher borrowing costs in smaller and peripheral Member States. The coexistence of national and EU prudential layers further adds complexity and reduces the efficiency of financial intermediation.

At the same time, bank credit remains disproportionately concentrated in residential mortgages and real-estate-related lending rather than in finance for non-financial corporations. ECB analysis finds that corporate bank lending is disproportionately concentrated in real estate, trade and construction sectors that contribute relatively little to productivity growth. In practice, this means that the sectors most critical for future productivity gains are not those receiving the bulk of bank financing.

The gap is particularly visible in the context of the green transition. Despite strong policy prioritisation, the green asset ratio of the EU banking sector remains low (2.76% in 2025), while the majority of banks are exposed to significant climate and transition risks. At the same time, a large share of corporate lending income continues to be derived from greenhouse gas-intensive sectors. This is not simply a transitional issue but reflects structural features of current banking models.

Three main barriers can be identified. First, a bankability gap: many green investments, such as energy-efficiency retrofits or early-stage clean technologies, do not generate sufficiently predictable short-term cash flows to meet standard credit criteria, particularly in a higher interest rate environment. Second, a business model bias: traditional lending practices rely heavily on physical collateral, systematically disadvantageous for asset-light investments typical of green and digital sectors. Third, a policy and regulatory gap: current prudential frameworks do not adequately reflect climate transition risks, nor do they provide strong incentives to support green lending and transition finance. In addition, the absence of sufficiently scaled public risk-sharing mechanisms limits banks' ability to engage in higher-risk green lending.

To enable banks to more effectively support productivity and economic growth, policy action should address these structural shortcomings.

First, completing the Banking Union is essential to reduce fragmentation. The absence of a European Deposit Insurance Scheme (EDIS), combined with restrictions on capital and liquidity mobility, continues to prevent the emergence of truly integrated cross-border banking groups. Without meaningful progress in this area, capital will remain inefficiently allocated across the Union.

Second, targeted reforms are needed to align banking regulation with the EU's strategic priorities. This includes better integrating climate transition risks into prudential frameworks, developing operational and standardised green lending definitions that are compatible with supervisory requirements, putting in place strong sustainability reporting requirements, and significantly expanding public risk-sharing instruments. For example, scaling up EIB and EIF guarantee schemes could enable banks to finance green SMEs by absorbing part of the first-loss risk that currently constrains lending.

Third, a shift in credit assessment practices is required. Current frameworks remain overly reliant on backward-looking indicators and collateral-based risk models. Moving towards more forward-looking, cash-flow-based approaches, while integrating sustainability and innovation-related criteria, would allow banks to better serve sectors that are central to the EU's future growth model, including clean technologies, digital infrastructure, and social housing.

Finally, monetary policy can also play a more targeted role in supporting the reallocation of credit. The ECB could introduce dual interest rate structures, whereby more favourable refinancing conditions are offered for lending aligned with EU policy priorities, such as the green and digital transitions. Building on the experience of targeted longer-term refinancing operations (TLTROs), such instruments could help reduce the cost of capital for priority investments and partially offset the structural disincentives faced by banks when financing higher-risk or longer-horizon projects. As explained in Positive Money report "Nature's Nudge", the ECB could further adjust its collateral framework to address biodiversity through stricter asset criteria, concentration limits and higher haircuts for harmful assets.

In sum, without addressing fragmentation, business model biases, regulatory misalignments, and the broader policy framework (including the role of monetary policy) the banking sector will remain structurally ill-equipped to finance the green, digital, and social transitions at the required scale.

2. Is current credit demand adequately met by banks and how is the demand and the capacity to meet it likely to evolve in the medium and long-term? Are you observing barriers affecting bank financing in support of the economy, including in areas identified as political priorities by the EU or Member States? Please elaborate by providing evidence and identifying economic sectors where access to credit could be improved.

Current credit demand in the EU is not adequately met in several economically significant segments. While overall credit volumes remain substantial, allocation patterns indicate persistent gaps in financing for productive and growth-enhancing activities.

ECB data show that bank lending remains disproportionately concentrated in residential mortgages and real estate-related activities rather than in financing for non-financial corporations. Moreover, ECB analysis indicates that corporate lending is itself concentrated in sectors such as real estate, construction, and trade, which tend to contribute less to long-term productivity growth.

This allocation bias has broader economic implications. A sustained prioritisation of real estate and asset-based lending can contribute to rising asset prices without a corresponding increase in productive capacity. Over time, this risks weakening productivity growth and exacerbating wealth inequality, as gains accrue primarily to asset owners. While banks operate on a commercial basis, these patterns suggest that credit allocation does not always align with broader economic and societal objectives.

Several supply-side barriers and structural issues help explain the observed gaps in credit provision.

Credit misallocation is driven in part by the structure of central bank liquidity provision and collateral frameworks. By accepting certain assets, such as government bonds and mortgage-related securities, on more favourable terms, central banks effectively increase their liquidity and attractiveness. This creates structural incentives for banks to allocate credit towards activities that are easily collateralisable, particularly real estate, rather than towards productive investment that generates long-term economic value.

Regulatory and monetary policy frameworks further reinforce this bias. Risk models and prudential rules tend to treat lending secured against existing assets as lower risk, while cash-flow-based lending to productive sectors is often penalised. At the same time, changes in interest rates disproportionately affect long-term investment projects, such as infrastructure or clean energy, while having a more limited impact on borrowing driven by expectations of asset price increases. As a result, monetary policy can unintentionally constrain productive investment more than speculative activity.

This bias is reinforced by banks' credit risk assessment frameworks and collateral requirements, which disadvantage innovative, green, and intangible-intensive sectors. EU banks continue to rely predominantly on physical collateral and stable cash flows, limiting access to finance for service-based, digital, and platform-oriented business models that depend largely on intangible assets such as intellectual property. In addition, current methodologies rely heavily on historical financial data and established credit histories, which are often unavailable for innovative or early-stage companies. As a result, these firms face structurally higher barriers to accessing bank finance, despite their potential contribution to productivity growth and EU strategic priorities. The ECB Bank Lending Survey (Q4 2025) confirms that higher perceived risks and reduced risk tolerance are key drivers of tighter credit standards.

The prioritisation of return on equity by listed EU banks constrains risk-taking and reinforces conservative lending patterns. Pressure to maximise shareholder returns,evidenced by substantial share buybacks, even among banks assessed by the ECB as having surplus capital, drives a preference for low-risk, collateralised lending. This systematically disadvantages the financing of the green and digital transitions, which require longer-term and higher-risk investment. There is little evidence that easing capital requirements leads to increased real-economy lending; instead, released capital has largely been redistributed to shareholders, limiting its contribution to productive investment.

More fundamentally, the current system reflects a misalignment between public support and private incentives. Bank lending is underpinned by central bank liquidity and public backstops, yet credit allocation decisions remain largely driven by short-term profitability considerations. In the absence of an explicit and democratically guided credit policy, this results in a persistent bias towards lending that supports existing asset markets rather than investment that expands productive capacity and supports long-term economic growth.

These structural constraints are particularly relevant in areas identified as EU priorities. Green transition projects often involve long payback periods and uncertain revenue streams, making them less compatible with standard lending criteria. Similarly, digital and knowledge-intensive firms face difficulties due to their reliance on intangible assets. Social investments may generate high societal returns but comparatively lower or delayed financial returns, further limiting their access to bank financing.

Looking ahead, both demand for and supply of credit are likely to face increasing pressures in the medium to long term. The ECB Bank Lending Survey (Q4 2025) highlights that rising geopolitical and trade policy uncertainty is already reducing banks' risk tolerance. Persistently high energy costs and economic uncertainty are also weakening the pipeline of bankable investment projects. This points not only to constraints on credit supply, but also to a structural shortage of sufficiently profitable and predictable investment opportunities, linked to fragmentation and uncertainty within the Single Market.

Better credit policy could help correct the current misallocation of finance by explicitly distinguishing between credit that supports new productive investment and credit that primarily fuels asset price inflation. As highlighted by Positive Money report 'Taking all the credit: Future-proofing money and credit policy for the 21st century', central bank liquidity provision, collateral frameworks, and refinancing operations are not neutral: they structurally shape the allocation of credit in the economy. These tools can therefore be used more deliberately to favour cash-flow-based lending that generates future income, such as investment in renewable energy, new housing, infrastructure, and productive SMEs, over lending backed by existing assets and expected capital gains. In practice, this implies more targeted refinancing schemes (including preferential funding rates for priority sectors), differentiated collateral eligibility and haircuts that reward socially and economically useful assets, and broader asset-side approaches such as pre-positioning requirements. In addition, greater democratic steering of credit policy (such as through a preferred asset taxonomy) could help align central bank operations with public policy objectives. Together, these instruments would enable a more strategic allocation of credit towards activities that enhance productivity, resilience, and long-term economic development.

8. What are in your view the main risks faced by EU banks today?

EU banks face a combination of structural, macroeconomic, and emerging systemic risks, which are closely interlinked.

A first major source of risk relates to climate-related financial risks. On the one hand, banks are exposed to physical risks (e.g. climate-related damages) and transition risks (e.g. abrupt policy changes or asset repricing), which may lead to significant losses over time. On the other hand, the financial system itself can amplify these risks through disorderly adjustments, including sudden repricing of carbon-intensive assets and correlated exposures across institutions. Addressing these risks requires both sufficient loss-absorbing capacity and a more forward-looking integration of climate risks into prudential and monetary frameworks.

A second key vulnerability lies in the structural fragility of bank balance sheets. Despite regulatory reforms, there is evidence that effective capital buffers remain relatively limited compared to historical levels, raising concerns about the system's ability to absorb large shocks. At the same time, the long-standing presence of implicit public guarantees, such as deposit insurance and the "too-big-to-fail" framework, may weaken market discipline by reducing incentives for creditors and investors to fully price risk.

Third, regulatory complexity and interactions between prudential tools may themselves constitute a source of risk. The increasing complexity of frameworks such as Basel III, including liquidity requirements (LCR and NSFR), can generate unintended interactions with capital requirements and affect banks' behaviour in ways that are difficult to predict. This may reduce transparency and contribute to regulatory arbitrage, without necessarily improving systemic resilience.

Finally, macro-financial and structural risks remain significant. These include prolonged low productivity growth in the EU, high exposure to real estate markets, and increasing geopolitical and trade-related uncertainty. Banks' concentration in mortgage lending and real estate-related activities makes them particularly sensitive to housing market corrections. At the same time, the transition to a higher interest rate environment, combined with elevated debt levels, increases credit risk for households and firms, while also potentially reducing the value of existing assets on bank balance sheets.

Overall, these risks point to a system that remains vulnerable to both external shocks and internal amplification mechanisms. Strengthening resilience therefore requires not only maintaining adequate capital and liquidity buffers, but also addressing structural incentives and improving the alignment between financial regulation, monetary policy, and long-term economic objectives.

9. What are in your view the main risks stemming from EU banks today?

EU banks can be a source of systemic risk through both their balance sheet structures and their role in allocating credit across the economy.

A first key dimension relates to climate-related systemic risks, While banks are exposed to climate risks (as explained above), they also actively shape them through their financing decisions. At the micro level, individual exposures may appear manageable; however, at the macro level, the aggregate allocation of credit, particularly towards carbon-intensive sectors, directly influences the pace of the transition and the accumulation of physical risks. This creates a feedback loop whereby current lending patterns contribute to future systemic instability. As such, there is a strong case for integrating climate considerations into macroprudential policy, including through the calibration of systemic buffers.

More broadly, banking system structure and interconnectedness can amplify shocks. The high degree of interconnectedness between financial institutions means that distress can spread rapidly across the system, as illustrated during the global financial crisis.

Finally, insufficient loss-absorbing capacity has broader societal implications. When capital buffers are thin, losses are more likely to be transmitted beyond the banking sector, either through credit contractions or through the need for public intervention. This creates a structural risk transfer from private stakeholders to the public sector, particularly in stress scenarios.

Addressing these risks also requires improvements in data and supervisory infrastructure. The increasing complexity of risks, particularly climate-related risks, more dynamic and forward-looking approaches to risk management. This includes better availability of macro-level data from public authorities and enhanced micro-level data sharing between financial institutions and supervisors.

12. How would you assess the current level of competition in the banking sector within the single market?

Competition in the EU banking sector is characterised by limited competition within the Single Market, combined with strong competitive pressure from non-EU actors. While European banks often operate in fragmented national markets with limited cross-border integration, key segments of financial services are dominated by large non-European firms. This reflects structural barriers within the EU that constrain internal competition while leaving space for external players to capture significant market share.

This dynamic is particularly evident in the payments sector. Card payments across the EU are effectively dominated by a duopoly of US firms, Visa and Mastercard, which benefit from strong network effects, economies of scale, and integrated cross-border infrastructures. European payment solutions, by contrast, remain fragmented and have struggled to scale beyond national markets. As a result, intra-EU competition is weak, and European banks remain dependent on external providers for core payment services. Addressing this structural weakness requires more than incremental regulatory change. As explained in this Positive Money position paper, the development of a digital euro could play a central role by providing a pan-European, publicly governed payment infrastructure. Such an infrastructure would reduce reliance on dominant international schemes, lower barriers to entry, and enable European providers to compete at scale across the Single Market.

At the same time, ownership structures within the EU banking sector may further limit competitive dynamics. Large US asset managers, such as BlackRock, Vanguard, State Street and Fidelity, hold significant stakes across many EU banks. This pattern of common ownership can contribute to more homogeneous governance and strategic alignment across institutions, potentially weakening incentives to compete aggressively on pricing, innovation, or market expansion. It also increases the sector's exposure to external financial and political developments, while contributing to the transfer of influence and profits outside the EU.

Current supervisory frameworks only partially address these issues, as they focus primarily on risks at the level of individual institutions. A more comprehensive approach would require greater transparency around ownership and voting practices, as well as a supervisory perspective that captures system-wide interactions and their implications for competition.

27. What are, in your view, the effects of digitalisation on the activities and business model of EU banks in the single market?

Digitalisation has significantly transformed the activities and business models of EU banks, but its effects have been uneven and, in some respects, misaligned with the core function of banking in supporting the real economy.

On the one hand, digitalisation has accelerated the expansion of banks' activities in payments and transactional services. These areas have become increasingly central to banks' revenue models, driven by fee-based income and the scalability of digital platforms. Digitalisation seems to reinforce existing trends towards business models

focused on low-risk, high-volume activities, rather than supporting the financing needs of the green, digital, and industrial transitions.

At the same time, in the absence of a strong EU digital industry, digitalisation has increased EU banks' dependence on non-European infrastructures. In payments, the growing reliance on international card schemes and digital payment providers, primarily US-based, has strengthened external dominance in a core financial function. Similarly, in IT infrastructure, cloud services, and data processing, EU banks are increasingly dependent on a small number of large global technology firms. This concentration raises concerns not only about competition, but also about operational resilience, data sovereignty, and strategic autonomy.

In this context, the development of strong European digital public payment infrastructures is essential. Initiatives such as the digital euro could provide a common, pan-European foundation for payments, reducing reliance on dominant international schemes and enabling greater competition within the Single Market. More broadly, strengthening public capabilities in digital payment infrastructure would help realign the banking sector with its core function of financing the real economy, while enhancing resilience and strategic autonomy.

95. In light of the ongoing revision of a number of pieces of EU legislation on sustainability (CSRD delegated acts, Taxonomy delegated acts, SFDR), do you see the need for amending any provision of the banking regulatory framework with a view to ensure achieving the objective of properly managing sustainability-related risks faced by banks?

The ongoing revision of EU sustainability legislation risks weakening banks' ability to manage sustainability-related financial risks by reducing the availability of reliable and standardised corporate-level data. Diluting reporting requirements under the Corporate Sustainability Reporting Directive (CSRD) does not reduce underlying risks; it reduces transparency around them. As highlighted by the ECB and EBA, recent changes to the European Sustainability Reporting Standards (ESRS) may significantly limit the availability of consistent, comparable information needed for effective risk assessment.

This creates a core constraint: banks cannot manage what they cannot measure. Access to granular, standardised and decision-useful data on corporates' sustainability risks and transition plans is a prerequisite for prudent risk management. In this context, it is essential to reopen the CSRD framework to ensure that it delivers sufficiently detailed and harmonised information. Without such data, banks' ability to identify, price and manage sustainability-related risks will be impaired, undermining both financial stability and the financing of the transition.

At the same time, the framework governing financial product disclosures, notably under the Sustainable Finance Disclosure Regulation (SFDR), creates asymmetries that may distort incentives. Products labelled as "sustainable" face significantly more stringent

disclosure requirements than conventional products, while sustainability risks embedded in the latter remain less visible. This uneven treatment risks discouraging green product development without ensuring comprehensive risk transparency across the system.

Beyond reporting, the current approach remains overly reliant on backward-looking, compliance-based frameworks. This is insufficient for managing forward-looking and rapidly evolving risks such as climate transition, biodiversity loss, cyber threats and geopolitical shocks. A complementary shift towards forward-looking data infrastructures, such as the one implemented by the Banco Central do Brasil, is therefore needed. This includes real-time provision of macro-level risk data by public authorities, combined with confidential micro-level data sharing between financial institutions and supervisors, enabling continuous monitoring of systemic vulnerabilities.

These shortcomings reflect a broader structural mismatch between the scale of sustainability-related risks and banks' ability and incentives to manage them. Some targeted amendments follow from this diagnosis. First, ensure robust corporate data availability by maintaining and strengthening CSRD, as the primary source of information for banks' risk assessments. Second, address disclosure asymmetries under SFDR by applying baseline sustainability risk transparency requirements across all financial products. Third, strengthen prudential integration by embedding sustainability risks more systematically into CRR/CRD and aligning prudential treatment with the EU Taxonomy to enable forward-looking risk assessments.