Updating EU Banking Regulation: From Post-Crisis Prudence to Growth and Competitiveness

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About the author

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Foreword

The IE Competitiveness Hub Brussels is the platform through which IE University brings its academic voice to the heart of the European policy debate. Supported by the IE Foundation and its partners, it was created to inform the discussion now shaping the future of European competitiveness with rigorous, independent analysis, bringing together scholars, policymakers, and practitioners around the questions that will determine whether Europe can compete, invest, and grow in the decade ahead.

When I presented my report to the European Council, Much More Than a Market, I argued that the Single Market is not a finished achievement but an unfinished project, one whose largest gains still lie ahead. It was there that the idea of a Savings and Investments Union took shape, and with it the diagnosis that runs through these pages: Europe's weakness is, above all, a weakness of integration. We are not one financial market, but twenty-seven.

Of all the dimensions of our competitiveness, the financial ecosystem may be the least developed and the richest in untapped potential. Europe does not lack savings; it lacks the institutions to put them to work. Every year, hundreds of billions of euros in European household savings leave the continent to finance growth elsewhere, mostly in the United States. That outflow is not a technical detail of market plumbing. It is a strategic loss, and reversing it is among the most consequential things the Union can do for itself. The green and digital transitions, and the renewed demands of security, cannot be financed by public budgets alone; they depend on private capital, and so on a financial system deep, liquid, and integrated enough to mobilise that capital at scale. The Savings and Investments Union is, to my mind, a cornerstone for making Europe's most important goals achievable.

This is where Giovanni Sabatini's analysis makes its essential contribution. The stability built after the financial crisis was necessary, and it must remain central to everything we do; on that, there can be no retreat. Yet stability alone has not translated into a financial system that stimulates growth. The prudential architecture that protected us was calibrated for another purpose, and its accumulated weight now presses on the very lending and risk-taking that European firms need to expand. The answer is not to dismantle that framework but to recalibrate it, so that a banking system which is safe also becomes one that finances investment, innovation, and scale. Sabatini suggests where that recalibration should begin, and how to pursue it without surrendering what we have secured. It is precisely the kind of contribution the Hub was created to advance.

Enrico Letta

Executive Summary

This paper examines the institutional constraints limiting the effectiveness of the European Union's financial integration agenda, with particular focus on the Savings and Investments Union (SIU). While post-crisis reforms have significantly strengthened financial stability, the current regulatory and supervisory architecture remains institutionally incomplete. As a result, integration is often formal rather than functional, constraining scale, investment, and competitiveness.

The paper identifies four interrelated dimensions of persistent fragmentation: supervision, adjudication, market infrastructure, and scale. Supervisory mandates and incentives remain structurally biased toward risk minimisation, fostering defensive and highly prescriptive oversight. Centralised supervision operates within decentralised judicial frameworks, reintroducing divergence at the enforcement stage and weakening legal certainty. In highly technical areas of financial regulation, this asymmetry is compounded by the limited specialised capacity of generalist courts to assess complex prudential judgments, valuation models, and market practices. Strengthening specialised adjudicatory capacity, at both national and EU level, would therefore enhance legal certainty, accountability, and supervisory effectiveness. Market infrastructure — particularly in post-trading — remains fragmented despite corporate consolidation, limiting liquidity pooling and efficiency gains. Finally, the geographic scale of European capital markets is constrained, notably by the exclusion of the United Kingdom from integrated frameworks.

These dimensions are mutually reinforcing. Judicial fragmentation amplifies supervisory conservatism; conservative supervision entrenches national silos; fragmented infrastructure prevents scale; and insufficient scale undermines the objectives of the SIU. Retail-focused reforms, while beneficial, cannot offset these structural constraints and should be seen as complementary rather than transformative.

Addressing these challenges does not require deregulation, but institutional recalibration. Financial stability, growth, and competitiveness should be treated as joint objectives. This implies closer alignment between supervision and adjudication, consolidation and integrated oversight of post-trade infrastructure, and an explicit policy focus on scale—including through variable-geometry frameworks such as a Single European Capital Markets Area capable of accommodating external participation.

The paper concludes that Europe faces a strategic choice between defensive integration, ensuring stability but limiting dynamism, and a model of dynamic resilience that combines prudential soundness with scale, investment, and long-term growth. Only the latter can enable the SIU to fulfill its economic and strategic objectives.

Introduction

Over the past fifteen years, the European Union has undertaken a profound transformation of its financial regulatory and supervisory framework. In response to the global financial crisis and the subsequent euro area sovereign debt crisis, policymakers prioritised resilience, stability, and crisis prevention. Capital and liquidity requirements were significantly strengthened, supervisory powers centralised, and new institutional architectures — most notably the Banking Union — were established to mitigate systemic risk and restore confidence in financial intermediaries.

These reforms were largely successful in their primary objective. The European financial system is today more resilient, better capitalised, and less prone to disorderly failure than in the pre-crisis period. However, regulatory frameworks are inherently path-dependent. Institutional arrangements designed under crisis conditions tend to persist even as economic priorities evolve. As a result, a framework optimised for stability may become misaligned with the requirements of sustainable growth, disruptive innovation, and structural transformation.

This tension has become increasingly salient amid the European Union's renewed emphasis on competitiveness and investment capacity, as reflected in the Savings and Investments Union (SIU). Despite high household savings, Europe continues to underinvest relative to peer economies, particularly in innovation-intensive, scale-dependent sectors. Capital markets remain fragmented, cross-border financial activity is limited, and exit opportunities for high-growth firms are underdeveloped. These constraints have been recognised at the highest political level, including in recent policy initiatives associated with the Commission's competitiveness agenda, as well as in the reports by Mario Draghi and Enrico Letta, which identify regulatory fragmentation as a central obstacle to European growth.

This paper argues that the principal constraint on European financial integration is no longer primarily regulatory, but institutional. While legislative harmonisation has advanced significantly, the institutions that interpret, enforce, and operationalise these rules remain fragmented along national lines. As a result, integration is often formal rather than functional. Supervision is increasingly centralised, but adjudication remains decentralised; market infrastructures operate at European scale in corporate terms but remain nationally segmented in practice; and the geographic scope of integration is constrained, notably by the exclusion of the United Kingdom from key frameworks. These forms of fragmentation are mutually reinforcing, generating conservative incentives, weakening legal certainty, and limiting the financial system's ability to mobilise capital at scale.

The paper develops a unified framework centered on four interrelated dimensions of fragmentation: supervision, adjudication, market infrastructure, and scale. It shows how misalignment across these dimensions produces what can be described as a structurally conservative equilibrium, in which financial stability is preserved but at the cost of reduced dynamism, weaker investment, and limited competitiveness. In this setting, policy initiatives focused primarily on retail participation or disclosure, while valuable, cannot by themselves overcome the underlying structural constraints.

By shifting the focus from rulemaking to institutional design, this paper contributes to three strands of literature. First, it extends the literature on European financial integration and the Capital Markets Union by emphasising the limits of legal harmonisation in the absence of aligned institutions. Second, it builds on the law and finance tradition by highlighting the role of enforcement heterogeneity — beyond legal origin — in shaping financial outcomes. Third, it contributes to the literature on regulatory design by analysing how asymmetric supervisory incentives generate defensive behaviour and constrain efficient risk allocation.

The central claim advanced here is that Europe's financial integration challenge has evolved from a problem of regulatory fragmentation to one of institutional misalignment. Addressing this challenge does not require deregulation, but recalibration. Financial stability, growth, and competitiveness should be treated as joint objectives, requiring closer alignment between supervision and adjudication, more integrated market infrastructure, and an explicit policy focus on scale.

The remainder of the paper proceeds as follows. Section 1 situates the post-crisis regulatory legacy within the EU's evolving economic priorities and introduces the Savings and Investments Union. Section 2 develops the conceptual framework linking stability, growth, and institutional incentives. Sections 3 to 6 analyse the structure and effects of post-crisis banking regulation, including supervisory mandates, prudential calibration, and operational complexity. Sections 7 and 8 examine the asymmetry between integrated supervision and fragmented adjudication and its implications for legal certainty and market integration. Sections 9 and 10 focus on market infrastructure, scale, and the role of EU–UK integration. Section 11 discusses the role of retail participation as an outcome of institutional design. Section 12 concludes with policy implications for a next-generation framework of financial integration.

I. From Crisis Stability to Institutional Misalignment

1. The post-crisis regulatory legacy

The European Union's contemporary financial regulatory framework is the product of an extraordinary historical shock: the global financial crisis of 2008–2009 and the subsequent sovereign debt crisis in the euro area. In response to systemic instability, institutional failure, and an acute loss of confidence in financial intermediaries, EU policymakers prioritised resilience, loss absorption, and crisis prevention as overriding objectives. Capital and liquidity requirements were substantially strengthened, supervisory powers expanded and centralised, and new institutional architectures — most notably the Banking Union — were created to contain risk and sever the link between banks and sovereigns (Pierson, 2000).

From the standpoint of financial stability, these reforms achieved their core objective. European banks today are better capitalised, less leveraged, and subject to more intrusive and standardised supervision than at any point in the pre-crisis period. Stress testing, resolution planning, and macroprudential oversight have become permanent features of the regulatory landscape. The probability of disorderly bank failure has been significantly reduced, and taxpayer-funded bailouts have become politically and legally exceptional rather than routine.

However, regulatory systems are inherently path-dependent. Frameworks designed under crisis conditions tend to persist even as economic priorities evolve (Pierson, 2004). What emerges over time is not merely a stable system, but a defensive equilibrium—one in which regulatory success is measured primarily by the absence of failure, rather than by the system's capacity to support growth, innovation, and structural transformation.

2. The Savings and Investments Union: objectives and emerging limits

The Savings and Investments Union (SIU) reflects a growing recognition that financial stability, while indispensable, is not sufficient to meet the Union's long-term economic and strategic challenges. Despite abundant household savings, the EU continues to underinvest relative to peer economies, particularly in high-growth sectors such as digital technologies, clean

energy, and scale-intensive industrial innovation. Empirical evidence confirms this structural gap. According to the International Monetary Fund, total investment in the European Union has remained persistently below that of the United States by approximately 2–3 percentage points of GDP over the past decade, with the gap particularly pronounced in intangible and innovation-related investment (International Monetary Fund, 2023). Similarly, the European Commission estimates that EU firms raise significantly less late-stage venture capital than their US counterparts, with scale-up financing in the EU amounting to less than half of US levels (European Investment Bank, 2024). This gap is not explained by savings constraints, but by the inability of fragmented capital markets to intermediate savings into high-risk, high-growth investment.

European start-ups and scale-ups frequently rely on non-EU capital at later stages of growth, while deep and liquid exit markets remain underdeveloped (Draghi, 2024; Letta, 2024). Banks, meanwhile, have become more conservative in risk-bearing intermediation, especially in long-term and equity-like financing. Capital markets remain fragmented, liquidity pools are shallow, and cross-border investment is constrained. These outcomes have prompted a reassessment at the highest political level. Financial stability is increasingly understood not as an end in itself, but as a necessary — though not sufficient — precondition for growth, competitiveness, and innovation.

The SIU is therefore rightly ambitious in seeking to mobilise European savings and channel them into productive investment. Yet its effectiveness is constrained by structural features of the EU financial system that go beyond disclosure, investor participation, or product design.

3. The central problem: national fragmentation in an integrated financial system

The central constraint facing the SIU is not the absence of EU-level rules, but the persistence of national fragmentation in a system that is otherwise highly integrated. Legislative harmonisation has advanced significantly, yet supervision, adjudication, market infrastructure, and enforcement remain largely organised along Member State lines. Integration is therefore often formal rather than functional.

This fragmentation manifests across four closely related dimensions:

- **Supervision**, where EU-level rules coexist with national practices, incentives, and interpretations that encourage conservatism and mi-

cro-regulation.

- **Adjudication**, where centralised supervisory decisions are subject to decentralised judicial review, reintroducing divergence at the enforcement stage.

- **Market infrastructure**, where trading, clearing, settlement, and custody continue to operate through nationally segmented systems despite corporate consolidation.

- **Scale**, where fragmentation limits liquidity formation, weakens exit markets, and constrains Europe's capacity to mobilise savings at continental scale.

The performance and structure of the European financial system are shaped by the interaction of three factors: (i) structural conditions, including market fragmentation and macroeconomic environment; (ii) regulatory design, particularly the calibration and complexity of prudential frameworks; and (iii) institutional alignment, notably the interaction between supervision, adjudication, and market infrastructure. This paper treats these elements not as isolated problems, but as components of a single structural constraint on European financial integration.

II. Conceptual Framework: Stability, Growth, and Institutional Design

1. Financial stability and growth as joint objectives

Financial regulation is often framed as a trade-off between stability and growth. From this perspective, greater resilience necessarily entails reduced risk-taking, lower leverage, and constrained intermediation, with negative implications for investment and innovation. This logic dominated the post-crisis reform agenda, where the social costs of instability were immediate and politically salient.

However, a growing body of economic literature challenges the assumption that stability and growth are inherently antagonistic. Financial systems play a dual role: they mitigate risk through diversification and loss absorption, but they also create risk by reallocating capital toward uncertain but productive activities (Levine, 2004). Innovation, in particular, is inseparable from risk-taking, long-term financing, and tolerance for failure (Aghion et al., 2004).

Excessive conservatism can therefore be as socially costly as excessive risk. Underinvestment in innovation, infrastructure, and human capital weakens long-term growth potential and reduces resilience to structural shocks. The relevant policy question is not how to minimise risk, but how to allocate and absorb risk within a stable institutional framework.

2. Incentives, loss functions, and defensive supervision

Institutional economics helps explain why regulatory systems tend to overshoot toward conservatism. Supervisors operate under asymmetric loss functions. Failures — bank distress, supervisory lapses, or crisis interventions — carry immediate reputational, legal, and political consequences. By contrast, foregone growth, investment, or innovation rarely generate equivalent accountability (Holmstrom & Milgrom, 1991).

In the EU context, this asymmetry is reinforced by fragmented responsibility. Supervisory authority is increasingly centralised, while political accountability for growth and competitiveness remains largely national. Supervisors therefore internalise downside risk while externalising opportunity costs.

Over time, these incentives produce what this paper defines as defensive supervision: a mode of regulatory behaviour in which supervisory authorities, facing asymmetric accountability and legal risk, systematically prioritise the avoidance of observable failure over the facilitation of efficient risk-taking. This results in an equilibrium characterised by procedural intensity, conservative calibration, and reduced reliance on supervisory judgment.

3. The limits of legal harmonisation without institutional alignment

EU integration has relied heavily on legal harmonisation, on the assumption that uniform rules generate uniform outcomes. This assumption holds only if interpretation, enforcement, and adjudication are equally aligned. Where these functions remain decentralised, harmonisation risks becoming symbolic rather than substantive (Weatherill, 2016).

Highly integrated policy areas such as banking and capital markets are particularly sensitive to this limitation. Financial actors operate across borders, but enforcement is filtered through national institutions with distinct legal cultures, procedural traditions, and standards of review. In such settings, divergence re-emerges at the operational level even under formally identical rules.

4. Scale, network effects, and financial market infrastructure

Scale is a structural variable in financial integration. Financial market infrastructures — trading venues, clearing houses, settlement systems, and custodians — exhibit strong economies of scale, network effects, and high fixed costs. Fragmentation, therefore, imposes persistent efficiency losses and limits liquidity formation.

While competition and diversity may be beneficial at the trading level, post-trading infrastructures tend toward natural monopoly characteristics. Where legal, supervisory, or operational barriers prevent consolidation or interoperability, markets remain shallow and segmented, constraining the ability of the financial system to mobilise savings at scale.

This logic underpins the analysis of infrastructure and scale developed later in the paper. It also explains why incremental regulatory refinement, absent institutional alignment and scale, yields diminishing returns.

III. Supervisory Mandates and the Stability Bias

This section develops three arguments. First, EU supervisory mandates are structurally oriented toward stability. Second, asymmetric accountability reinforces conservative supervisory behaviour. Third, this dynamic has contributed to an increasingly granular and prescriptive regulatory framework, with implications for proportionality and efficiency.

1. Stability-oriented mandates in the EU supervisory framework

The institutional design of EU banking supervision reflects the political priorities that prevailed in the immediate aftermath of the global financial crisis. The Single Supervisory Mechanism (SSM), entrusted to the European Central Bank, was established with a clear and narrowly defined mandate: to ensure the safety and soundness of credit institutions and the stability of the financial system. Similar stability-focused mandates apply to the European Banking Authority (EBA) and to national competent authorities (NCAs), albeit with different operational responsibilities.

This mandate configuration was both deliberate and appropriate in its historical context. Restoring confidence, limiting moral hazard, and preventing future taxpayer-funded bailouts were overriding objectives. However, mandates do more than allocate legal responsibilities; they shape institutional incentives, supervisory culture, and day-to-day decision-making. Where mandates are narrowly framed around stability, other policy objectives — such as growth, competitiveness, and market integration — are treated as external to the supervisory function.

As a result, supervision is structurally insulated from the economic consequences of its own conservatism.

2. Incentive asymmetries and defensive supervisory behaviour

As already noted in section 2, supervisory authorities operate under asymmetric accountability: failures (such as bank distress or missed risks) entail immediate political, legal, and reputational costs, whereas the opportunity costs of excessive conservatism — reduced lending, weaker investment, and limited integration — remain largely unobserved. Over

time, this imbalance fosters a defensive supervisory approach.

A possible objection to the argument advanced in this paper is that the conservative bias embedded in the current framework reflects not a distortion, but a rational response to the severe social costs of financial crises. From this perspective, fragmentation in supervision or adjudication may act as a safeguard, preventing excessive centralisation of risk and allowing for institutional diversity. Similarly, higher capital requirements and supervisory conservatism may be seen as necessary correctives to pre-crisis under-regulation.

These arguments are valid and highlight the importance of preserving prudential discipline. However, the issue is not the existence of safeguards, but their calibration and interaction. Where conservatism becomes structurally embedded and unresponsive to changing economic conditions, it may generate second-order risks by constraining investment, weakening growth, and shifting activity outside the regulated perimeter. The objective is therefore not to relax safeguards, but to ensure that they operate within a framework that remains proportionate, predictable, and aligned with broader economic objectives.

One of the most visible manifestations of the stability bias is the steady shift toward micro-regulation. EU banking supervision has evolved from principle-based standards toward increasingly granular, prescriptive, and data-intensive requirements. This evolution is evident in the proliferation of detailed reporting obligations, governance expectations, internal-model constraints, and overlapping capital buffers[1].

Micro-regulation reduces supervisory and managerial discretion by substituting rule-based compliance for judgment-based oversight. While this approach increases formal consistency and auditability, it also reduces flexibility and weakens proportionality. Institutions with markedly different sizes, business models, and risk profiles are increasingly subject to similar compliance expectations, regardless of their systemic relevance.

The burden of this shift falls unevenly. Smaller and mid-sized banks face

[1.] Concrete regulatory examples further illustrate the unintended consequences of excessive conservatism. For instance, prudential rules requiring banks to hold additional capital against software investments create a structural disadvantage relative to technology firms entering financial services. Similarly, thresholds such as the 1% net present value test for loan forbearance may, in practice, prevent banks from supporting viable firms facing temporary financial distress. These examples highlight how micro-regulatory provisions can have macroeconomic consequences.

disproportionately high fixed compliance costs, while larger cross-border groups encounter constraints on optimising capital and liquidity allocation across jurisdictions. In both cases, management attention is diverted away from strategic decision-making and toward regulatory process management. The proliferation of regulatory technical standards (RTS) and implementing technical standards (ITS) has contributed to regulatory inflation. While technical standards are essential for operational consistency, their cumulative effect has been to narrow discretion and to embed detailed supervisory expectations into quasi-binding instruments.

The growing reliance on soft law — guidelines, supervisory expectations, thematic letters, FAQs, and handbooks — has blurred the boundary between binding requirements and informal guidance. While soft law offers flexibility **and can support supervisory convergence**, its proliferation creates legal uncertainty and weakens accountability. From the perspective of regulated entities, it is often unclear which expectations are mandatory, which are best practice, and which reflect temporary supervisory priorities. This ambiguity encourages conservative behaviour and over-compliance, reinforcing the stability bias identified earlier.

At the same time, important corrective steps are already underway. The ECB has acknowledged the need to streamline supervisory practices and has launched reforms to make supervision more risk-based, integrated, efficient, and effective, including through the reform of the Supervisory Review and Evaluation Process and the broader "next-level supervision" agenda. These initiatives are welcome and indicate that the problem is increasingly recognised within the supervisory community itself. The point, therefore, is not that EU supervision is static or unreformable, but that these efforts should be consolidated into a more systematic framework for supervisory simplification, legal clarity, and proportionality.

A more disciplined hierarchy of norms would enhance clarity and legitimacy. Core obligations should be anchored in legislation or formally binding standards, while soft law should be used sparingly and transparently to interpret, rather than expand, regulatory requirements.

These dynamic risks reintroducing national or institutional "gold-plating" through interpretation and implementation, even where formal legislative harmonisation exists. It also makes the regulatory framework less adaptable to innovation and structural change. Periodic consolidation, sunset clauses, and systematic cost–benefit analysis of technical standards would help limit unintended accumulation and preserve regulatory clarity.

3. The case for mandate recalibration

Recalibrating supervisory mandates does not imply weakening prudential standards or relaxing resilience requirements. Rather, it entails explicitly recognising that financial stability, growth, competitiveness, and market integration are joint public objectives. A more explicit recognition of competitiveness as a complementary objective — alongside financial stability — would align supervisory behaviour with the broader strategic priorities of the European Union. Such an approach would support a transition from defensive supervision toward a model of enabling supervision, in which prudential soundness is preserved while facilitating efficient capital allocation and long-term economic growth.

A useful institutional analogy can be drawn from the ECB's monetary policy mandate. Article 127(1) TFEU[2] clearly establishes a hierarchy in which price stability is the primary objective of the European System of Central Banks, while broader economic objectives are to be supported "without prejudice" to price stability. This mandate applies to the ECB in its monetary policy capacity and should not be conflated with its separate supervisory role within the Single Supervisory Mechanism. Nevertheless, it offers a relevant template for thinking about mandate design: a clear prioritisation of a core public objective, combined with explicit recognition of broader economic goals. In this perspective, financial stability would remain the primary anchor of banking supervision. However, it could be framed as a constrained objective: one that must be pursued without unduly hampering growth, competitiveness, innovation, or market integration. Such an approach would not weaken prudential discipline. Rather, it would align supervision more closely with the broader economic mission of the Union, fostering a regulatory model that is both resilient and enabling.

In this respect, the introduction of systematic competitiveness and proportionality assessments in the legislative and supervisory process would represent a meaningful step forward. Regulatory initiatives should be subject to structured evaluations of their impact on financing conditions, cost of capital, and cross-border activity. Such assessments should not be limited to the initial legislative proposal but extended throughout the policy cycle, including Level 2 and Level 3 measures, where a substantial portion

[2] "The primary objective of the European System of Central Banks (hereinafter referred to as the 'ESCB') shall be to maintain price stability. Without prejudice to the objective of price stability, the ESCB shall support the general economic policies in the Union with a view to contributing to the achievement of the objectives of the Union as laid down in Article 3 of the Treaty on European Union." Article 127(1) — Treaty on the Functioning of the European Union (TFEU)

of regulatory burden is often introduced.

Establishing an independent body within or attached to the European Commission, with representation from policy (Commission/ECB), industry, and academia, could help assess the cost-benefit trade-offs of regulation. This body would ensure that prudential measures enhance stability without unduly restricting lending, investment, or competitiveness.

Absent such adjustments, supervisory behaviour will remain structurally biased toward caution, regardless of legislative ambition. The result is a system that is resilient in narrow prudential terms but insufficiently equipped to support the scale and dynamism required by the Savings and Investments Union.

IV. Post-Crisis EU Banking Regulation: Achievements and Structural Biases

1. The Banking Union: centralised supervision with incomplete integration

The creation of the Banking Union represented a qualitative leap in European financial integration. By centralising supervision of significant institutions within the Single Supervisory Mechanism (SSM) and establishing a common resolution authority through the Single Resolution Board (SRB), the EU sought to ensure consistent oversight and to break the sovereign–bank nexus.

In institutional terms, this was a major achievement. Supervisory practices across the euro area have converged, information sharing has improved, and national forbearance has been significantly reduced. For large cross-border banking groups, the SSM provides a single supervisory interlocutor and a common methodological framework.

However, the architecture remains structurally incomplete. Deposit insurance remains national, capital and liquidity are still ring-fenced along Member State lines, and supervisory practices continue to diverge in their application despite common rules. More importantly, while supervision has been centralised, enforcement and judicial review have not. This asymmetry — examined in detail in later sections — limits the functional integration of the Banking Union and reinforces conservative supervisory behaviour.

As a result, the Banking Union delivers formal consistency without fully unlocking cross-border integration or scale.

2. Basel III in the EU: resilience gains and economic trade-offs

The EU's implementation of Basel III marked a decisive shift away from the permissive pre-crisis regulatory environment. Capital requirements were raised, leverage constrained, liquidity buffers introduced, and internal risk models subjected to far greater scrutiny. Through the Capital Requirements Regulation and Directive (CRR/CRD), these standards were embedded directly into EU law, substantially reducing national discretion in formal rule-setting.

European banks are significantly better capitalised, liquidity risk is more tightly managed, and system-wide resilience has increased. Stress testing, supervisory benchmarking, and macroprudential oversight have become permanent features of the regulatory landscape. The likelihood of disorderly bank failure has been materially reduced.

These gains, however, have not been costless. Higher capital and liquidity requirements increase the cost of balance-sheet intermediation, particularly for long-term, low-liquidity, and equity-like assets. Empirical evidence suggests that banks have responded by rebalancing toward lower-risk activities, shortening maturities, reducing cross-border exposures, and retreating from capital-intensive lending. While such adjustments enhance individual balance-sheet resilience, they also constrain the financial system's capacity to support long-term investment and innovation (Bank of International Settlements, 2023).

A substantial empirical literature documents the impact of higher capital requirements on lending behaviour. Using granular bank-level data, leading economists from the Bank of International Settlements find that a 1 percentage point increase in capital requirements is associated with a reduction in loan growth of between 1.2 and 1.5 percentage points in the short run (Gambacorta & Shin, 2016). More recent evidence from Mandas and Goodell (2025) shows that capital-based macroprudential tightening also induces banks to raise capital ratios and shift toward safer, more liquid assets, thereby reducing lending and profitability but enhancing financial stability.

While these adjustments enhance resilience, they also imply a measurable contraction in risk-bearing intermediation capacity, particularly for innovation-intensive sectors.

A growing body of evidence also suggests that an excessively stringent regulatory framework applied to the banking sector may generate **unintended consequence**s, notably the migration of credit intermediation outside the regulated perimeter. Since the Global Financial Crisis, tighter capital and liquidity requirements — introduced through the Basel III framework — have strengthened resilience but also increased the relative cost of bank lending, particularly for riskier borrowers. A well-documented effect has been the expansion of **non-bank financial intermediation (NBFI)**, including private credit funds, which now play a significant role in corporate and consumer lending. As highlighted by the Financial Stability Board, the NBFI sector has grown to account for nearly half of global financial assets, reflecting a structural shift in credit provision (Global Monitoring Report on Non-Bank Financial Intermediation, 2023). Academic literature

confirms this substitution effect: when banks are more tightly constrained, lending activity tends to migrate toward less regulated entities rather than disappear (Adrian et al., 2010; Buchak et al., 2018). Crucially, this process does not reduce aggregate risk, but instead **relocates it to segments of the financial system where transparency, supervision, and prudential safeguards are weaker**, thereby complicating macroprudential oversight (International Monetary Fund, 2024).

Recent developments provide concrete evidence of these dynamics and their potential risks. The growing importance of private credit markets — now a critical source of funding for both firms and households — has been accompanied by concerns over underwriting standards, leverage, and opacity. The Bank of England Governor, Andrew Bailey warned that "alarm bells" are ringing in private credit markets following the collapse of First Brands and Tricolor (Smith et al., 2025). This concern is echoed in policy and academic analyses: private credit funds often operate with limited disclosure requirements, complex fund structures, and significant interconnectedness with regulated banks through funding and risk-transfer channels (Aramonte & Avalos, 2021). While the expansion of private credit has helped sustain financing in the face of tighter bank regulation, it also underscores a key policy trade-off: over-calibration within the banking sector may inadvertently amplify systemic vulnerabilities elsewhere. The implication is not a rollback of prudential standards, but rather the need for a more holistic regulatory approach, capable of balancing financial stability with growth while ensuring that risks do not accumulate in less visible and less regulated parts of the financial system.

The issue is therefore not that Basel III was excessive, but that its EU implementation has occurred in an institutional context that amplifies conservatism and limits offsetting mechanisms for growth and integration.

V. The need for Prudential Recalibration: Proportionality, Tiering, and the 28th Regime

1. Basel III implementation and EU-specific overlays

Basel III provides a globally agreed baseline for prudential regulation. However, its implementation within the European Union has been characterised by the addition of multiple layers of complexity, including EU-specific overlays, extensive technical standards, and conservative calibrations in key areas. While some divergence reflects legitimate policy choices, the cumulative effect has been to increase capital requirements and constrain lending capacity beyond what is justified by underlying risk. A particular concern arises from the interaction of multiple prudential tools, including capital buffers, macroprudential measures, and the output floor. In practice, these instruments may overlap, leading to duplicative capital requirements and reduced transparency in the overall calibration of the framework. The lack of consistency in the application of macroprudential tools across Member States further contributes to fragmentation and undermines the level playing field within the Single Market.

Improving clarity would require greater transparency around Pillar 2 methodologies, clearer articulation of end-state expectations, and more systematic disclosure of supervisory rationales. Predictability strengthens market discipline and enhances the effectiveness of prudential policy.
Clear separation between Pillar 1 requirements and Pillar 2 measures is essential for transparency and credibility. Pillar 1 should define binding, rule-based minimum standards applicable across the Union. Pillar 2 should address genuinely institution-specific risks that cannot be captured ex ante through harmonised rules.

In practice, the boundary between the two has become blurred. Pillar 2 requirements are often perceived as opaque, discretionary, and duplicative of baseline standards. This perception matters, because uncertainty about future capital demands encourages banks to hold precautionary buffers well above regulatory minima, further constraining lending and investment. A central concern for market participants is not only the level of capital requirements, but their predictability. Banks operating without clarity on their future capital position face difficulties in pricing risk, allocating capital, and supporting long-term investment. In the EU, the multiplicity of

authorities involved in prudential supervision and resolution contributes to uncertainty regarding the trajectory of capital requirements, leading to the emergence of a "regulatory premium" that is reflected in lower market valuations for European banks.

These dynamics have important economic implications. Higher and less predictable capital requirements increase the cost of financing for European corporates, particularly for long-term and risk-bearing investments. At the same time, international asymmetries — especially in the implementation of Basel standards across major jurisdictions — risk placing European banks at a competitive disadvantage in global capital markets.

Empirical and policy evidence confirm that the implementation of Basel III reforms has materially increased capital requirements for European banks, with estimates suggesting increases in risk-weighted assets of over 10% and corresponding pressures on capital adequacy and lending capacity.

2. Regulatory Divergence and Banking Competitiveness: Evidence from Recent Developments

Recent policy developments indicate a growing divergence in regulatory approaches across major jurisdictions, with important implications for bank profitability, lending capacity, and global competitiveness. In the United States, regulators have moved toward a recalibration of post-crisis capital rules, reducing the expected impact of Basel III finalisation. Estimates suggest that proposed reforms could bring capital increases close to neutral levels, thereby supporting lending capacity, shareholder returns, and profitability. This shift reflects a broader policy objective of enhancing the competitiveness of the US financial sector and supporting domestic investment.

The United Kingdom has similarly adopted a more flexible regulatory approach following its departure from the European Union. Leveraging its regulatory autonomy, the UK has increasingly emphasised competitiveness and proportionality, aligning more closely with US policy trends while maintaining core prudential safeguards. By contrast, the European Union has largely pursued a full and relatively conservative implementation of Basel III standards. As a result, European banks have been required to absorb substantial additional capital requirements. Industry estimates suggest that more than €100 billion in additional capital has been accumulated in recent years, absorbing a significant share of internally generated resources and potentially constraining lending capacity, with some estimates pointing to an impact of up to €1.5 trillion. These effects are particularly relevant in

a context where European banks, on average, continue to exhibit lower profitability and operate in more fragmented markets compared to their US counterparts.

Comparative evidence highlights a persistent and widening competitiveness gap between US and European banks. Over the past decade, US banks have consistently achieved higher returns on equity than their euro area counterparts, with aggregate ROE typically in the low-to-mid teens in the United States compared with high single digits in the euro area. ECB supervisory data indicate euro area bank ROE of around 8–10% in recent years, while FDIC data show US bank profitability above 11% (ECB, 2025; FDIC, 2025). This sustained differential, amounting to several percentage points over time, reflects not only differences in market structure, but also deeper regulatory, institutional, and financial system characteristics that shape capital allocation, scale, and profitability across the two banking systems.

The divergence in regulatory trajectories is therefore translating into measurable differences in economic outcomes. Lower capital constraints in the US and, to a lesser extent, the UK support higher return on equity and greater balance sheet flexibility. In contrast, higher and less predictable capital requirements in the EU may constrain the ability of banks to finance long-term investment and compete in global capital markets. Lower profitability in turn constrains internal capital generation and lending capacity, reinforcing the investment gap identified earlier.

This evidence highlights a key policy challenge for the European Union: ensuring that prudential regulation continues to support financial stability while avoiding unintended constraints on investment capacity and competitiveness. In the context of the Savings and Investments Union, addressing this balance is critical to enabling the financial system to effectively mobilise and allocate capital across the Union. These effects are particularly relevant in a context of international regulatory divergence. While some jurisdictions — most notably the United States — are moving toward a partial easing or recalibration of capital requirements, European banks are expected to operate under comparatively stricter prudential conditions, potentially constraining their ability to support investment and compete globally.

A systematic review of the EU prudential framework is therefore warranted to simplify the macroprudential toolkit, reduce overlaps, and enhance consistency across jurisdictions. Greater standardisation in the application of buffers, clearer separation between Pillar 1 and Pillar 2 requirements, and improved transparency in supervisory expectations would strengthen both

credibility and predictability. Prudential recalibration does not imply abandoning the lessons of the financial crisis. Rather, it reflects the recognition that excessive conservatism can itself become a source of systemic risk by weakening investment, innovation, and long-term growth. A prudential framework that is proportionate, transparent, and internationally consistent can preserve financial stability while supporting banks' capacity to finance the real economy. In this sense, prudential policy should be understood not only as a safeguard against risk, but also as a key determinant of Europe's investment capacity and long-term competitiveness.

3. The limits of one-size-fits-all prudential regulation and the benefit of a tiered prudential and supervisory framework

The EU prudential framework remains heavily influenced by a one-size-fits-all logic. While proportionality is formally recognised in legislation and supervisory guidance, its practical application is uneven and often limited. Institutions with very different business models, risk profiles, and systemic relevance are frequently subject to similar prudential expectations, reporting requirements, and supervisory intensity.

This approach reflects the post-crisis emphasis on resilience and comparability. However, in a heterogeneous financial system, uniform prudential treatment can generate inefficiencies. Excessive uniformity constrains the ability of institutions to specialise, grow, and intermediate risk efficiently across borders. A more effective approach is a genuinely tiered prudential framework that distinguishes clearly between institutions based on their systemic relevance, complexity, and geographic footprint.

Under such a framework, **significant institutions** with cross-border activities and systemic importance would operate under a more integrated EU-level regime. This would include a single supervisory interface, consistent application of prudential standards, and recognition of group-wide capital and liquidity management. In return, these institutions would be subject to higher governance, transparency, and loss-absorbing capacity requirements.

Less significant institutions, by contrast, would remain primarily under national supervisory responsibility, but benefit from materially simplified reporting, governance, and supervisory expectations. Proportionality would be applied in substance rather than form, reducing compliance burdens while preserving resilience.

Explicitly acknowledging and designing for this tiered reality would enhance

legal certainty and align the prudential framework with how the European banking system already functions in practice.

4. The 28th regime as an integration instrument

Within a tiered framework, an optional EU-wide prudential regime, a "28th regime", could serve as a catalyst for cross-border integration. By offering participating institutions a single supervisory and regulatory framework, it would reduce fragmentation, eliminate duplicative compliance requirements, and facilitate more efficient cross-border operations.

Recent European Commission initiatives reinforce both the relevance and the feasibility of such an approach. The 28th regime has emerged as a central element of the Union's broader competitiveness and Single Market agenda, notably within the 2025 Competitiveness Compass and subsequent policy initiatives on the Savings and Investments Union and the start-up and scale-up strategy. These initiatives converge on a common objective: to enable firms to operate across the Union under a single, harmonised set of rules, thereby overcoming the structural fragmentation associated with 27 parallel national frameworks.

The Commission's recent proposal for an EU-wide corporate framework ("EU Inc.") further illustrates the operational logic of the 28th regime. Conceived as an optional, digital-by-default legal regime, it would allow firms to organise, scale, and operate across the Union under a unified set of rules governing core aspects such as incorporation, governance, and insolvency. This initiative responds directly to calls from both the European Council and the European Parliament to facilitate cross-border scaling and to reduce legal and administrative barriers to investment and growth.
While current proposals focus primarily on corporate law and innovative firms, their underlying rationale is directly applicable to the prudential domain. Just as a unified corporate regime aims to reduce legal fragmentation and enable scale, a prudential "28th regime" could provide a single supervisory interface, harmonised reporting, and full recognition of group-wide capital and liquidity management for cross-border banking groups.

Crucially, such a regime should be conceived as an enabling instrument rather than a deregulatory shortcut. Its purpose would not be to lower standards, but to align incentives, reduce institutional frictions, and support the efficient allocation of capital across the Union. In this sense, it would complement existing Single Market and Capital Markets Union initiatives by addressing one of their central structural constraints: the persistence of regulatory and supervisory fragmentation despite formal harmonisation.

If appropriately designed, a prudential 28th regime could therefore represent a natural extension of the Commission's broader integration strategy, translating the logic of a single European rulebook from corporate law into the core architecture of financial supervision.

VI. Supervision, Resolution, and Simplification: From Micro-Control to System Effectiveness

1. Supervisory processes and administrative burden

Beyond formal mandates and prudential calibration, the operational design of supervision plays a decisive role in shaping institutional behaviour and market outcomes. Over the past decade, the European supervisory framework has become increasingly complex, characterised by extensive reporting requirements, overlapping data requests, and a growing reliance on detailed technical standards and soft law instruments.

Institutions are required to comply with a dense and evolving body of Level 1, Level 2, and Level 3 measures, often accompanied by national discretions and supervisory interpretations. This layered structure increases compliance costs, diverts managerial resources, and reinforces a shift toward procedural compliance at the expense of strategic decision-making.

In particular, greater discipline is needed in the use of Level 2 and Level 3 instruments. While technical standards are essential for operational consistency, their proliferation has contributed to regulatory inflation and reduced transparency. A clearer hierarchy of norms, anchoring core obligations in Level 1 legislation and limiting the expansion of technical mandates, would enhance legal certainty and accountability.

In parallel, supervision should move toward a “data efficiency” model, based on the systematic reuse of existing information and the reduction of redundant reporting requirements. The adoption of a “one data point” approach, whereby data is collected once and reused across supervisory processes, would significantly reduce operational burden while improving data quality and consistency.

Joint Supervisory Teams combine ongoing supervision, thematic reviews, on-site inspections, internal model investigations, stress testing, and frequent ad hoc data requests. Each element has a clear rationale. Taken together, however, they impose significant compliance costs, divert senior management attention, and create uncertainty regarding supervisory expectations.

The cumulative burden of regulatory complexity is increasingly visible at the level of senior management. Survey-based evidence supports the claim that compliance requirements impose significant managerial costs: a joint report by the Institute of International Finance and EY finds that senior executives in large banks devote a substantial share of their time to regulatory compliance and supervisory engagement, particularly in areas such as reporting, model validation, and governance requirements (IIF & EY, 2023). Complementary evidence from Thomson Reuters shows that the cost and resource intensity of compliance functions have continued to rise, with firms allocating increasing staff and budgets to meet regulatory demands (Thomson Reuters, 2023). Taken together, this reallocation of managerial attention represents an indirect but significant cost of regulatory complexity, with implications for innovation, competitiveness, and long-term growth.

Where supervisory systems prioritise exhaustive data collection and granular procedural checks over materiality and risk relevance, they risk becoming inefficient without becoming more effective. Simplification should be embedded in the broader legislative process. Introducing mandatory competitiveness and necessity checks, alongside comprehensive and continuous impact assessments, as already discussed in par. 3.3, would help ensure that regulation remains proportionate and aligned with economic objectives.

Where supervisory systems prioritise exhaustive data collection and granular procedural checks over materiality and risk relevance, they risk becoming inefficient without becoming more effective.

A supervisory framework that is simpler, more predictable, and more focused on material risks would not weaken financial stability; on the contrary, by enhancing clarity, reducing unnecessary burden, and allowing institutions to allocate resources more efficiently, simplification can strengthen both resilience and the capacity of the financial system to support growth and innovation, a goal that is closely aligned with the EU's broader ambition of digital-by-default administration, which financial supervision has yet to fully internalise, as institutions are still frequently required to submit overlapping datasets in different formats to multiple authorities with limited reuse of existing information.

A shift toward genuinely digital supervision would therefore involve harmonised EU-wide reporting taxonomies, systematic reuse of existing data before new requests are issued, and greater stability of data requirements over multi-year horizons, with risk-based materiality thresholds determining when data quality issues warrant supervisory action rather

than automatically escalating minor discrepancies; such reforms would reduce administrative burden while improving data quality and supervisory insight, while also supporting integration by enabling consistent analysis across institutions and jurisdictions.

2. Resolution frameworks: predictability, proportionality, and usability

The EU bank resolution framework established by the Bank Recovery and Resolution Directive (BRRD) and the Single Resolution Mechanism constitutes a fundamental improvement over the pre-crisis bailout model. By equipping authorities with harmonised resolution tools—most notably bail-in—and by creating a supranational resolution authority, the framework seeks to internalise the costs of bank failure, limit taxpayer exposure, and strengthen market discipline.

Resolution reform has been a cornerstone of post-crisis policy. However, its effectiveness depends on predictability and operational usability. In practice, resolution planning and Minimum Requirement for Own Funds and Eligible Liabilities (MREL) calibration have become increasingly complex, with limited transparency regarding methodologies and end-state expectations. For many institutions, particularly mid-sized and cross-border banks, resolution requirements create funding uncertainty and strategic constraints. Excessive complexity can undermine credibility by making resolution plans difficult to execute under stress.

Simplifying resolution frameworks would involve clearer alignment with international standards, greater transparency in calibration, and proportional application of requirements based on systemic relevance. Predictable and usable resolution regimes strengthen market discipline more effectively than complex but opaque ones. A supervisory and resolution framework that is too complex to be operationally credible weakens, rather than strengthens, financial stability. In stress situations, authorities and market participants rely on clarity, predictability, and confidence in institutional processes.

Operational simplification should therefore be understood as a stability-enhancing reform. By reducing unnecessary complexity, clarifying expectations, and focusing supervisory resources on material risks, the EU can preserve resilience while improving effectiveness. Such an approach aligns supervision and resolution with the broader objectives of the Savings and Investments Union: enabling scale, supporting integration, and mobilising capital efficiently without compromising prudential soundness. In practice, however, the credibility of the resolution regime depends less

on the existence of formal legal powers than on their operational usability in crisis conditions. Bail-in is legally and technically complex. It requires rapid and defensible asset valuation, strict observance of creditor hierarchies, and compliance with the no-creditor-worse-off principle, all under the threat of ex post judicial review. These constraints reduce predictability and may discourage consistent application, particularly where losses would fall on politically sensitive investors (Fromage, 2025).

The cases of Banco Popular and the Italian banks Banca Popolare di Vicenza and Veneto Banca are frequently cited in the literature as emblematic of both the limited and uneven use of the EU resolution framework: while Banco Popular was formally resolved under the BRRD through a rapid and highly managed sale process, the Italian banks were excluded from resolution altogether and handled via national liquidation with state support. These contrasting outcomes illustrate how discretionary assessments, particularly the public interest test applied by the Single Resolution Board, can lead to divergent results that undermine the consistency, credibility, and market-disciplining role of the Banking Union regime.

Minimum Requirement for Own Funds and Eligible Liabilities (MREL) has substantially improved resolvability, but it does not resolve all operational challenges. In particular, liquidity in resolution remains a persistent weakness. While bail-in can restore solvency, it does not guarantee short-term funding or market confidence. Compared with more centralised crisis-management frameworks, the EU system relies on fragmented national arrangements and layered decision-making, which may hinder speed and clarity in stress situations (Gordon & Ringe, 2015).

These features create an inherent tension: a resolution regime designed to be rule-based and predictable may, in practice, encourage caution and discretionary interventions when tested.

3. Stability without dynamism: the limits of the current equilibrium

Taken together, post-crisis reforms have delivered a banking system that is demonstrably safer than its pre-2008 predecessor. This achievement should not be understated. However, safety has been achieved within an institutional configuration that prioritises risk minimisation over risk allocation and absorption.

The resulting equilibrium is one of high resilience but limited dynamism. Banks operate with strong buffers but constrained risk appetite; supervision is consistent but defensive; resolution frameworks are comprehensive but

complex. Cross-border integration remains shallow, capital allocation is conservative, and the banking system's contribution to long-term growth and innovation is uneven.

This diagnosis does not imply regulatory failure. Rather, it reflects a temporal mismatch between a framework designed for crisis prevention and an economic environment that increasingly requires scale, risk-sharing, and long-term investment. Addressing this mismatch requires not deregulation, but institutional recalibration—an issue taken up in the following sections.

VII. Integrated Supervision and Fragmented Adjudication

1. The supervision–adjudication asymmetry

One of the most distinctive and least examined features of the EU's financial governance architecture is the institutional asymmetry between supervision and adjudication. Over the past decade, supervisory authority in banking and capital markets has been progressively centralised at the EU level. In contrast, judicial review of supervisory decisions remains overwhelmingly national.

Decisions taken by EU-level authorities — most notably the ECB in its supervisory capacity, but also the European Banking Authority and the European Securities and Markets Authority — ultimately operate within national legal systems when challenged or enforced. This means that formally uniform supervisory actions are filtered through diverse judicial traditions, procedural rules, and standards of review.

In a highly integrated financial system, this asymmetry is not neutral. It reintroduces national divergence at precisely the stage where uniformity matters most: enforcement. As a result, integration achieved at the level of rules and supervision is partially undone through decentralised adjudication (forth. Sabatini & Caputo Nassetti, 2026).

2. National courts as structural fragmenters

National courts do not intentionally fragment the Single Market. Their role is to ensure legality, protect fundamental rights, and uphold domestic constitutional principles. However, when operating within distinct legal cultures and procedural frameworks, courts can produce materially different outcomes when applying identical EU rules.

Divergence arises across several dimensions: the degree of deference accorded to supervisory discretion; the intensity of review of complex economic assessments; the availability of interim relief and suspension of supervisory measures; and the scope of remedies, including damages and contract nullity. In financial supervision, where decisions often rely on forward-looking risk judgments and probabilistic assessments, these differences are especially consequential.

The result is that similar supervisory actions may be upheld swiftly in one Member State, delayed or modified in another, and annulled in a third. From the perspective of regulated institutions, legal certainty becomes jurisdiction-dependent.

In several Member States, courts increasingly engage in substantive review of prudential assessments, valuation methodologies, and risk models. While judicial oversight is essential for accountability and legitimacy, intensive review of technical supervisory judgments can effectively transform courts into de facto co-supervisors[3].

This dynamic creates three systemic problems. First, it dilutes supervisory authority by introducing multiple centres of judgment. Second, it delays corrective action, particularly where interim measures suspend supervisory decisions. Third, it incentivises supervisory authorities to adopt defensive positions, anticipating potential litigation and adjusting decisions to minimise legal exposure rather than maximise supervisory effectiveness. These effects are not hypothetical. They are reflected in supervisory practice, where authorities internalise litigation risk and increasingly favour procedural robustness and formal compliance over timely intervention and qualitative judgment.

Judicial fragmentation produces behavioural effects that extend well beyond individual cases. Supervisors adjust behaviour to minimise legal risk, reinforcing the stability bias described in the previous section. Banks, in turn, adapt to uncertainty by limiting cross-border exposure, favouring domestic organisational structures, and reducing reliance on innovative or complex instruments that are more likely to attract scrutiny.

At the market level, these dynamics reinforce home bias and discourage cross-border consolidation. Legal uncertainty becomes a hidden but material cost of integration. Firms factor national judicial environments into strategic decisions on location, structure, and risk-taking, fostering forum shopping and regulatory arbitrage.

3. An emblematic example comes from Italy and concerns derivative contracts. In recent years, a jurisprudential trend has emerged that conditions the validity of these contracts on the "sharing" of complex mathematical formulas and probabilistic scenarios between the bank and the client. A requirement not provided for by European legislation and regulation and hardly feasible in practice.

This interpretation has spread especially after the interest rate collapse following the 2008 crisis, when many derivatives entered into to hedge against rising rates turned out to be costly. The rulings have paved the way for extensive litigation, often on contracts concluded years ago, with effects that go far beyond individual cases.

Decentralised adjudication undermines the credibility of centralised supervision and weakens the EU's ability to deliver consistent outcomes across the Single Market.

The Court of Justice of the European Union plays a critical role in ensuring interpretative coherence of EU law. However, the preliminary ruling mechanism is ill-suited to address the structural fragmentation described above. It operates ex post, addresses abstract questions of law, and does not harmonise procedural rules, evidentiary standards, or remedies.

As a result, reliance on judicial harmonisation alone cannot compensate for the institutional misalignment between integrated supervision and decentralised adjudication. Without more direct alignment of adjudicatory mechanisms, fragmentation will continue to re-emerge at the enforcement stage, regardless of the degree of legislative harmonisation.

VIII. Judicial Fragmentation and the Savings and Investments Union

1. Enforcement certainty as a precondition for capital markets integration

Capital markets are uniquely sensitive to legal certainty. Unlike traditional bank lending, market-based finance relies on predictable enforcement of contracts, consistent application of rules, and credible exit mechanisms. Even small variations in judicial interpretation or procedure can materially affect risk assessment, pricing, and investment decisions.

The Savings and Investments Union seeks to mobilise household savings and channel them into productive investment across borders. Its success therefore depends not only on harmonised rules governing disclosure, conduct, and market access, but also on confidence that those rules will be enforced consistently across jurisdictions. Where enforcement outcomes are uncertain or jurisdiction-dependent, investors rationally limit cross-border exposure, regardless of formal passporting rights.

Judicial fragmentation thus operates as a hidden but powerful constraint on the SIU. It does not prevent cross-border activity outright, but it raises its cost, complexity, and perceived risk.

2. Passporting, sanctions, and forum shopping

The effectiveness of passporting regimes rests on mutual trust: trust that supervisory standards are equivalent, and trust that enforcement outcomes will be broadly consistent. Fragmented adjudication undermines both. Where national courts apply different standards of review or afford varying degrees of deference to supervisory authorities, the credibility of enforcement actions becomes uneven. Sanctions that are swift and decisive in one Member State may be delayed, reduced, or annulled in another. From the perspective of market participants, this asymmetry weakens deterrence and creates incentives for strategic behaviour.

Available indicators point to significant variation in the functioning of judicial systems across the European Union, with direct implications for financial regulation. Data from the World Bank and the European Commission show that the average duration of commercial and financial litigation varies

substantially across Member States, in some cases by a factor of two or more. Differences are also observed in the availability of interim relief, the intensity of judicial review, and the enforcement of administrative decisions. In financial matters, these variations translate into heterogeneous enforcement environments. Supervisory actions that are implemented swiftly and with limited judicial interference in some jurisdictions may be subject to prolonged litigation, suspension, or modification in others. For cross-border institutions and investors, this introduces a jurisdiction-dependent dimension to legal certainty, effectively re-fragmenting the Single Market at the stage of enforcement.

Firms increasingly factor national judicial environments into decisions on establishment, structuring, and risk-taking. This dynamic fosters forum shopping and regulatory arbitrage, not because rules differ formally, but because their enforcement does. Over time, such behaviour erodes the level playing field and re-nationalises activity that is nominally integrated. A more fundamental difficulty lies in the institutional role of national courts themselves. Generalist courts are not designed to act as financial market experts. Yet in the absence of specialised adjudicatory mechanisms, they are frequently called upon to assess complex prudential judgments, valuation models, and market practices.

Even where courts act diligently and in good faith, outcomes may diverge simply because legal traditions, procedural norms, and evidentiary standards differ. Identical supervisory actions can therefore produce contradictory judicial outcomes across Member States, introducing legal uncertainty that cannot be resolved ex ante by market participants. This problem is structural rather than accidental. It reflects a mismatch between the technical nature of integrated financial supervision and the nationally bounded character of judicial review.

The limitations of generalist adjudication are further illustrated by recent case law. The Lexitor case provides a salient example. In that case, the Court of Justice adopted a broad interpretation of the Consumer Credit Directive, requiring the proportional reduction of all costs in the event of early repayment. While the judgment ensured formal legal uniformity, it effectively extrapolated a Union-wide rule from a context shaped, at least in part, by specific national practices. The resulting interpretation had significant economic implications across Member States, including in jurisdictions where the Directive had been implemented and applied in line with its original economic rationale, thereby affecting legal certainty and established business models.

More broadly, litigation relating to prudential measures — such as cases

concerning risk-weight calculations or supervisory discretion — illustrates how judicial review of highly technical financial matters can produce outcomes with system-wide implications that extend beyond the original factual context. While such rulings strengthen accountability, they also highlight the difficulty for generalist courts in fully capturing the interaction between legal interpretation, risk modeling, and market functioning.

In the absence of specialised adjudicatory capacity, courts — both at national and EU level — may be required to assess complex financial and prudential questions without the institutional tools or expertise typically available to supervisory authorities. This can lead to outcomes that are legally sound but economically disruptive, or that introduce uncertainty in areas where predictability is essential.

In this respect, the case for specialisation arises not only at the national level, through dedicated financial courts or specialised chambers, but also at EU level. In highly integrated areas of financial regulation, more specialised adjudicatory mechanisms could complement the existing judicial architecture by combining legal consistency with a deeper understanding of financial markets, thereby enhancing both legal certainty and the effectiveness of supervision.

3. Implications for capital allocation and market depth

Judicial fragmentation affects not only individual enforcement actions but also the aggregate functioning of capital markets. Investors demand higher risk premia where enforcement is uncertain. Issuers face higher costs of capital and less reliable access to cross-border funding. Intermediaries limit market-making activity and reduce balance-sheet commitment in jurisdictions perceived as legally unpredictable.

These effects are cumulative. Shallow liquidity reduces the attractiveness of secondary markets; weak secondary markets undermine exit opportunities; poor exits deter long-term and risk-bearing investment. The result is a negative feedback loop that directly undermines the SIU's objective of mobilising savings at scale.

Importantly, these dynamics cannot be remedied through retail participation alone. Encouraging households to invest more broadly does not address the institutional factors that constrain market depth and cross-border allocation.

Addressing judicial fragmentation does not require undermining national

judicial independence or constitutional traditions. Rather, it calls for institutional alignment commensurate with the degree of market integration. Possible approaches include clearer allocation of interpretative authority in highly integrated policy areas; greater use of EU-level adjudication or specialised review mechanisms for supervisory decisions; and convergence of procedural standards and remedies where EU authorities exercise direct powers.

Absent such alignment, further legislative harmonisation is likely to yield diminishing returns. Integrated supervision operating within fragmented adjudicatory frameworks will continue to produce conservative behaviour, legal uncertainty, and suboptimal capital allocation, outcomes fundamentally at odds with the ambitions of the Savings and Investments Union.

IX. Market Infrastructure, Scale, and Cumulative Fragmentation

1. Market infrastructure as a structural determinant of integration and scale

Financial market infrastructure — trading venues, central counterparties (CCPs), central securities depositories (CSDs), settlement systems, and related post-trade services — constitutes the operational backbone of capital markets. It shapes liquidity formation, transaction costs, risk management, and the ability of an economic area to achieve scale.

In markets characterised by strong network effects and high fixed costs, infrastructure design determines whether liquidity pools fragment or consolidate: where infrastructure remains nationally segmented, even formally integrated markets struggle to generate depth, resilience, and global relevance, whereas integrated infrastructure enables scale, enhances liquidity, and supports more efficient capital allocation (European Central Bank, 2024; European Commission, 2025; European Parliamentary Research Service, 2026).

Despite decades of integration efforts, EU financial market infrastructure remains fragmented along legal, supervisory, and operational lines. This fragmentation persists even after corporate consolidation. Ownership integration has not translated into functional integration, leaving Europe with infrastructure groups that operate at European scale in corporate terms but remain constrained to national silos in practice.

Not all fragmentation is economically harmful. At the trading level, diversity and competition can enhance efficiency, innovation, and resilience. Trading venues benefit from relatively low switching costs, product differentiation, and technological innovation. Fragmentation among trading platforms — when combined with effective interconnection and consolidated market data — can improve choice, foster innovation, and discipline pricing.

The EU's trading landscape reflects deliberate policy choices to promote competition and prevent monopolisation. Multiple venues serving the same instruments allow participants to optimise execution across price, speed, and market impact. In this segment of the value chain, fragmentation is compatible with integration, provided that interoperability and transparency are preserved; however, the ongoing transition to a T+1 settlement cycle

illustrates how such fragmentation becomes more problematic downstream, as the multiplicity of post-trade infrastructures, legal regimes, and operational standards across Member States significantly complicates coordination and compresses processing timelines compared to more centralised markets such as the US or UK.

Consolidation should not be pursued indiscriminately. The economic case for integration varies across the value chain and must be assessed in light of scale effects, switching costs, and systemic risk..

2. Post-trading infrastructure: economies of scale and structural inefficiency

The economic characteristics of post-trading infrastructure differ fundamentally from those of trading venues. Clearing, settlement, and custody exhibit strong economies of scale, network effects, and high fixed costs. Switching costs for users are significant, and the scope for meaningful product differentiation is limited.

In such settings, excessive fragmentation is economically inefficient. Multiple CCPs and CSDs serving the same markets dilute netting benefits, increase collateral requirements, raise operational complexity, and weaken risk management efficiency. From a system-wide perspective, fragmentation increases costs without delivering commensurate benefits in competition or innovation.

In the EU, post-trade fragmentation is sustained by divergent securities laws, settlement finality regimes, insolvency frameworks, and supervisory practices. Even where technical platforms such as TARGET2-Securities (T2S) have improved operational harmonisation, underlying legal and institutional differences continue to constrain interoperability and consolidation. As a result, T2S has reduced frictions but has not become a true integration layer. The cost implications are material and persistent. Post-trade inefficiencies raise transaction costs, increase settlement risk, and weaken secondary-market liquidity. These effects accumulate across the system, undermining the competitiveness of European capital markets (European Commission, 2025). Estimates by the European Commission suggest that cross-border securities transactions in the EU can be two to five times more expensive than domestic transactions due to legal and infrastructural fragmentation (European Commission, 2024). Academic studies (e.g. Viral Acharya et al., 2016) also show that fragmented clearing and settlement systems increase collateral requirements and reduce netting efficiency, thereby raising systemic liquidity needs. These findings are consistent with earlier evidence

from the Giovannini Group (2001; 2003), which identified key barriers to efficient cross-border clearing and settlement, and are further supported by subsequent analyses such as the Centre for European Policy Studies study on post-trading costs in the EU (CEPS, 2017), as well as more recent industry evidence from Bourse Consult and Civitta (Bourse Consult & Civitta, 2020), all of which highlight the persistent cost disadvantages, operational frictions, and inefficiencies arising from fragmented European post-trade infrastructures.

One of the most striking features of the European landscape is that corporate consolidation has failed to deliver Single Market outcomes. Large infrastructure groups operate multiple exchanges, CCPs, and CSDs across Member States, yet each entity remains subject to separate national authorisation, supervision, insolvency law, and operational constraints.

This structure produces duplication rather than efficiency. Group-level optimisation of capital, liquidity, risk management, and IT infrastructure is constrained by nationally bounded supervisory expectations and legal requirements. In some cases, vertical integration within groups further entrenches silos by incentivising the internal routing of transactions rather than open access across the market.

The experience mirrors earlier stages of banking integration, where cross-border groups existed in corporate form but remained functionally fragmented. The lesson is that supervision and governance must follow market reality, not legal form. Without genuinely integrated oversight, market-led consolidation cannot unlock scale.

3. Infrastructure fragmentation and the SIU negative feedback loop

Infrastructure fragmentation interacts with supervisory and judicial fragmentation to create a self-reinforcing negative feedback loop that directly undermines the Savings and Investments Union.

Fragmented post-trade infrastructure raises transaction and settlement costs. Higher costs reduce liquidity and market depth. Weak liquidity undermines credible exit opportunities for investors. Poor exits reinforce institutional risk aversion, constraining the supply of long-term and risk-bearing capital. As a result, firms struggle to scale, and investment either remains suboptimal or migrates outside the EU.

This loop illustrates why retail-focused reforms or disclosure improvements cannot, on their own, deliver the objectives of the SIU. Without deep, liquid,

and efficient markets supported by integrated infrastructure, increased participation does not translate into increased investment capacity. Breaking this feedback loop requires treating scale as an explicit policy objective rather than an incidental outcome. This implies a differentiated approach to infrastructure integration:

- **At the trading leve**l, competition, openness, and innovation should be preserved, supported by interoperability and consolidated data.
- **At the post-trading level**, consolidation, standardisation, and interoperability are economically necessary to achieve efficiency and resilience.
- **At the supervisory level**, genuinely integrated oversight is required for systemic, cross-border infrastructures, so that corporate consolidation can translate into functional integration.

Variable-geometry or opt-in models offer a pragmatic pathway where unanimity is unattainable. Allowing willing Member States to adopt harmonised legal regimes and centralised supervision for post-trade infrastructure would enable faster progress while preserving political feasibility.

In this sense, infrastructure reform is not ancillary to the SIU; it is foundational. Without decisive action on post-trade integration and supervisory alignment, Europe will remain structurally unable to mobilise its savings at scale or to compete effectively with other continental financial systems.

X. EU–UK Capital Markets Integration and Strategic Scale

1. Scale as a strategic variable in capital markets

Scale is not merely an outcome of market success; it is a structural determinant of how capital markets function. Liquidity attracts liquidity, deep markets attract issuers, and scale underpins both resilience and global relevance. Capital markets that fail to reach sufficient scale struggle to support large firms, deep venture capital ecosystems, and sustained investment in innovation-intensive sectors.

The Savings and Investments Union is premised on a correct diagnosis: Europe possesses abundant savings but lacks sufficiently deep and integrated markets to transform those savings into long-term, risk-bearing investment at scale. However, scale is constrained not only by internal fragmentation within the EU, but also by the geographic boundaries of the project itself.

2. The functional role of the United Kingdom in European capital markets

Notwithstanding Brexit, the United Kingdom remains Europe's largest and most sophisticated capital-markets hub. London continues to dominate European activity in equity trading, derivatives, foreign exchange, clearing, and risk management. UK-based institutions provide access to global investor pools, advanced market infrastructure, and deep liquidity that EU markets alone have not replicated.

EU and UK capital markets remain deeply intertwined. EU corporates rely on UK-based liquidity and services; EU investors access global markets through UK infrastructure; and key post-trade services—particularly in derivatives clearing—remain concentrated in London. The separation introduced by Brexit is therefore primarily legal and political, not economic.

This creates a structural tension. An EU-only SIU seeks to build scale while excluding the single largest pool of capital-market activity in Europe.

Excluding the UK from the SIU framework imposes a structural ceiling on what the Union can realistically achieve. Liquidity pools remain smaller and

more fragmented; exit markets for growth firms are shallower; and institutional investor participation is weaker than it would otherwise be.

Paradoxically, this exclusion increases Europe's dependence on non-European capital markets, particularly the United States, thereby undermining the very objective of strategic autonomy that motivates much of the SIU agenda. Fragmentation at the geographic level compounds fragmentation at the legal, supervisory, and infrastructural levels identified in earlier sections.

From this perspective, the question is not whether the EU should "reintegrate" the UK politically, but whether it can afford to pursue capital-markets integration at continental scale while structurally excluding its largest financial centre.

3. SECPA: a variable-geometry framework for capital markets integration

The "Study on consolidation and reducing fragmentation in trading and post-trading infrastructures in Europe" (Bourse Consult and Civitta September – 2025) explicitly recognises these scale constraints and proposes a novel institutional response: the creation of a **Single European Capital Markets Area (SECPA)**, conceived as an analogue to SEPA in payments.

SECPA is envisaged as a **variable-geometry, opt-in framework**, allowing willing Member States—and potentially key third countries—to participate in a deeply integrated capital-markets area without requiring full EU membership or Treaty change. Unlike a purely optional "28th regime", SECPA would constitute a genuinely unified legal, supervisory, and infrastructural space for participating jurisdictions.

Key features of a SECPA-style framework include:

- a single, harmonised legal regime for securities issuance, trading, clearing, settlement, and custody;
- centralised or genuinely integrated supervision for participating infrastructures and market participants;
- aligned insolvency, collateral, and settlement-finality rules;
- open and competitive access across the value chain, particularly in post-trade services.

Crucially, SECPA is explicitly designed to accommodate external participation, notably by the United Kingdom and Switzerland, alongside more forward-looking Member States. In doing so, it offers a mechanism to expand scale, liquidity, and global relevance without reopening fundamental political

questions of membership.

A SECPA-style framework reframes EU–UK capital markets integration as an institutional design choice rather than a political concession. Participation would be conditional, rule-based, and revocable, preserving regulatory autonomy while enabling functional integration where scale matters most. From a strategic perspective, this approach offers several advantages. It allows Europe to pool liquidity at scale, strengthens exit markets for European firms, and reduces dependence on non-European financial centres. At the same time, it avoids the binary choice between full inclusion and exclusion that has constrained post-Brexit policy debates.

The Commission ultimately chose not to pursue the SECPA proposal in its 2025 follow-up initiatives. Nevertheless, the logic underpinning it remains compelling. Strategic autonomy in capital markets does not imply insulation from global finance. It implies the capacity to finance European priorities domestically, retain value creation within Europe, and shape global standards. Achieving this requires openness combined with scale, not fragmentation disguised as sovereignty.

From this perspective, EU–UK integration through a SECPA-style framework is not a departure from the objectives of the Savings and Investments Union, but a necessary extension of them. Without such an extension, the SIU risks becoming a structurally constrained project, ambitious in scope, but limited in effect.

XI. Retail Participation in Context: An Outcome of Institutional Design

The previous sections have shown how fragmentation across supervision, adjudication, market infrastructure, and geographic scale constrains the efficient allocation of capital in European capital markets. These institutional frictions shape not only the supply of financial intermediation and investment opportunities, but also the behaviour of end investors. In this context, retail participation cannot be treated as an autonomous policy lever; rather, it reflects the depth, efficiency, and credibility of the underlying market environment. The limited and uneven engagement of European households in capital markets is therefore best understood as a symptom of structural fragmentation, not its cause. This section builds on this perspective by analysing retail participation as an endogenous outcome of institutional design, thereby completing the link between market structure, intermediation capacity, and the mobilisation of savings within the Savings and Investments Union.

1. Retail participation in the Savings and Investments Union narrative

Retail participation occupies a prominent place in the policy narrative surrounding the Savings and Investments Union (SIU). European households hold a substantial share of their wealth in bank deposits and low-yield instruments, while participation in capital markets remains uneven across Member States. From this perspective, increasing household engagement appears an intuitive mechanism to mobilise savings and broaden the investor base.

Policy initiatives have accordingly focused on improving financial literacy, simplifying disclosure, enhancing distribution channels, and promoting long-term investment products. These measures address genuine frictions and can yield incremental benefits, particularly in terms of inclusion and diversification.

However, this emphasis risks obscuring a more fundamental point: retail participation is not an independent driver of financial integration, but an endogenous outcome of the institutional environment in which financial markets operate.

Retail participation is, by construction, a demand-side intervention. It can increase the volume of savings seeking investment opportunities, but it cannot, on its own, create the conditions necessary for efficient capital allocation. The effectiveness of retail investment depends critically on the supply-side architecture of financial markets: market depth, liquidity, credible exit mechanisms, and consistent enforcement of rules.

Where these conditions are weak, increased retail participation does not translate into sustained investment capacity. Instead, it may expose households to higher volatility, limited diversification, and elevated intermediation costs. In such environments, the marginal impact of retail-focused reforms is inherently constrained.

The limitations of retail policy can be understood as a direct consequence of the broader institutional misalignments identified in this paper. Fragmented supervision encourages conservative intermediation; fragmented adjudication undermines legal certainty; fragmented market infrastructure limits liquidity and scale. Taken together, these factors constrain the supply of investable opportunities and weaken the functioning of secondary markets, thereby reducing the effectiveness of retail participation as a policy lever.

2. Retail participation in the Savings and Investments Union narrative

The transformation of household savings into productive investment is mediated by financial intermediaries and market infrastructures operating at scale. Banks, asset managers, pension funds, and insurance companies play a central role in allocating capital, diversifying risk, and providing access to markets.

Where these intermediaries face fragmented regulatory frameworks, conservative prudential incentives, or shallow and illiquid markets, the transmission mechanism between savings and investment becomes impaired. In such contexts, an increase in retail participation does not translate into a proportional increase in long-term or risk-bearing investment. Instead, it may result in greater reliance on external markets, concentration in low-risk assets, or higher costs of intermediation.

The effectiveness of retail participation is therefore contingent on the strength and integration of the broader financial ecosystem. Without deep and liquid markets, efficient infrastructure, and predictable enforcement, retail savings cannot be mobilised at scale.

From a systemic perspective, retail participation is best understood as an equilibrium outcome rather than a primary policy instrument. In deep, liquid, and predictable markets, household participation tends to expand organically, supported by lower transaction costs, broader investment opportunities, and credible exit mechanisms. Conversely, in fragmented and shallow markets, policy efforts to stimulate retail participation are likely to yield limited and potentially fragile results.

Empirical evidence is consistent with this interpretation. Cross-country comparisons suggest that higher levels of retail participation are strongly associated with market depth, institutional quality, and the efficiency of financial intermediation, rather than with standalone policy incentives.
The policy implication is therefore clear. Strengthening the institutional foundations of integration, aligning supervision and adjudication, reducing infrastructure fragmentation, and enabling scale are preconditions for the sustainable expansion of retail participation. Absent such reforms, retail-focused initiatives risk addressing symptoms rather than underlying constraints.

It should be noted that an active policy debate exists around the use of tax incentives to promote retail participation in capital markets. Several jurisdictions have introduced tax-advantaged investment schemes, including Denmark's Aktiesparekonto, which applies a preferential flat tax rate on equity returns, as well as the UK Individual Savings Account (ISA), the French Plan d'Épargne en Actions (PEA), the Italian PIR regime, and the Swedish investment savings account (ISK). While differing in design—ranging from full tax exemption to preferential or simplified taxation—these instruments share the objective of encouraging long-term household participation in capital markets. Their effectiveness, however, varies across jurisdictions and appears closely linked to underlying market depth, institutional quality, and the efficiency of financial intermediation. A detailed assessment of tax-based incentives falls outside the scope of this paper. The focus here remains on the structural conditions—market depth, legal certainty, supervisory alignment, and infrastructure integration—that ultimately determine whether increased retail participation can translate into efficient and sustainable capital allocation.

XII. Conclusion

The European Union has succeeded in building a financial system that is markedly more stable than it was prior to the global financial crisis. This achievement reflects deliberate policy choices, institutional innovation, and sustained political commitment. It should not be underestimated. However, stability alone is no longer sufficient to meet the Union's economic, technological, and geopolitical challenges.

While much of the current regulatory framework reflects the legacy of the global financial crisis, emerging risks are reshaping the financial landscape. Cyber risk, digital financial intermediation, and the growing role of technology firms in financial services challenge traditional regulatory boundaries. At the same time, the expansion of private credit and non-bank financial intermediation introduces new forms of systemic risk outside the regulated banking perimeter. These developments further reinforce the central argument of this paper: that institutional design, rather than rule quantity, determines system effectiveness.

Beyond prudential regulation, Europe's regulatory approach in the digital domain has significant implications for financial sector competitiveness. Frameworks such as GDPR, the AI Act, and Open Finance initiatives, while reflecting important societal objectives, may also constrain innovation and data-driven business models. The interaction between horizontal digital regulation and sector-specific financial rules creates asymmetries that may disadvantage European institutions relative to global competitors.

These developments highlight the need for a more adaptive regulatory framework, capable of addressing structural change without replicating the institutional inertia observed in the post-crisis period. A forward-looking approach should prioritise flexibility, cross-sector consistency, and the ability to monitor and address risks across the financial system as a whole.

This paper has argued that the central constraint on European financial integration today is not regulatory weakness, but institutional misalignment. Legislative harmonisation has advanced, yet supervision, adjudication, market infrastructure, and scale remain fragmented along national lines. As a result, integration is often formal rather than functional, and the Savings and Investments Union risks delivering incremental rather than transformative outcomes.

Three overarching insights emerge from the analysis.

First, **financial stability, growth and competitiveness must be treated as joint objectives**. Supervisory mandates, incentives, and processes remain structurally biased toward risk minimisation. While understandable in a post-crisis context, this bias has become increasingly misaligned with the Union's need for scale, innovation, and long-term investment. Recalibration does not imply deregulation, but it does require explicit recognition of opportunity costs and proportionality in prudential and supervisory decision-making.

Second, **institutional alignment matters as much as legal harmonisation**. Centralised supervision operating within decentralised adjudicatory frameworks reintroduces divergence at the enforcement stage and incentivises defensive behaviour. Judicial fragmentation undermines legal certainty, weakens market integration, and constrains cross-border capital allocation. This problem is particularly acute in technically complex areas of financial regulation, where generalist courts may be required to assess prudential judgments, valuation methodologies, risk models, or market practices without specialised institutional capacity. Developing specialised adjudicatory mechanisms or dedicated financial chambers would help bridge the gap between legal accountability and financial expertise. Without closer alignment between supervision and adjudication, further rulemaking is likely to yield diminishing returns.

Third, **scale is a structural variable, not an incidental outcome**. Fragmented market infrastructure, incomplete post-trade integration, and the exclusion of key financial centres impose a hard ceiling on the depth and liquidity of European capital markets. Addressing infrastructure fragmentation and enabling scale, potentially through variable-geometry frameworks such as a Single European Capital Markets Area, are therefore foundational to the success of the SIU.

Europe's financial governance framework has reached the limits of a defensive integration model.

The path forward lies in **dynamic resilienc**e—a model of financial governance that preserves stability while enabling risk-sharing, investment, and growth. This requires simplifying supervisory processes while strengthening effectiveness, aligning adjudication with integrated supervision, treating infrastructure as a strategic asset, and embracing scale as a policy objective rather than a by-product.

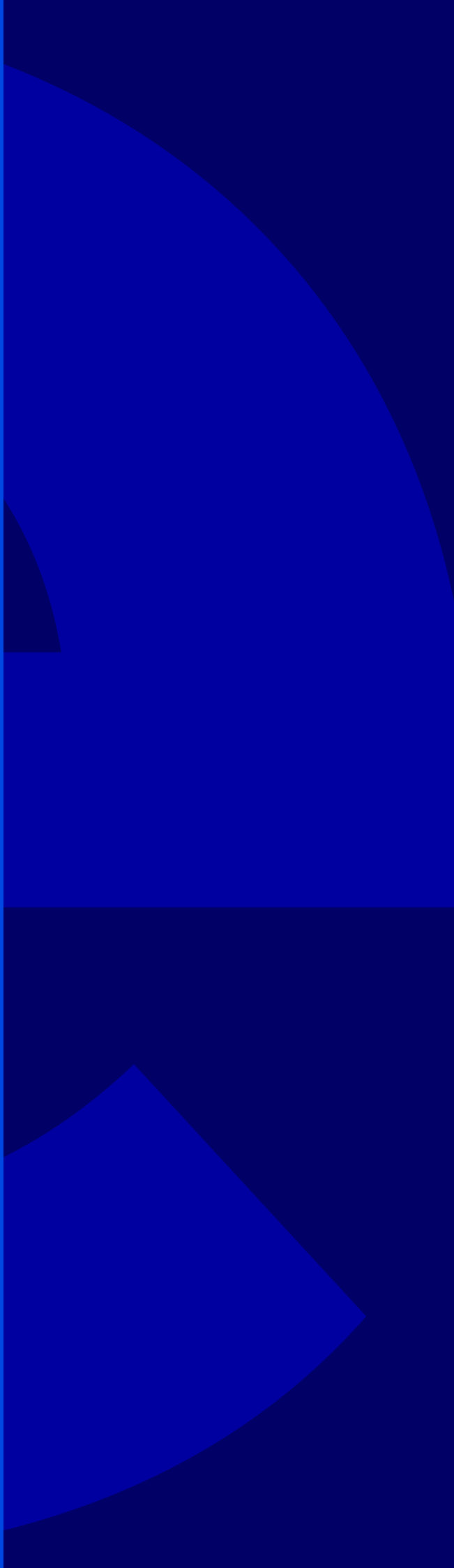
The central challenge is not whether Europe should choose between stability and growth, but whether it can design institutions capable of delivering both. A system that is resilient but unable to allocate capital

efficiently is not fully resilient in an economic sense. The next phase of integration must therefore move beyond rule harmonisation toward institutional alignment, scale, and operational coherence.

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