



EUROPEAN CENTRAL BANK

BANKING SUPERVISION

Evolving risks, evolving supervision: reforming European banking supervision

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- 1 How is banking supervision organised in Europe?
- 2 How has the risk environment evolved?
- 3 How is European supervision responding?

How is banking supervision organised in Europe?

The Single Supervisory Mechanism (SSM) was established ten years ago in response to the financial crisis.



The Supervisory Review and Evaluation Process (SREP) performs a comprehensive assessment of risks and controls.

1. Is the business model viable and sustainable?

2. Are risk management and governance adequate?

3. Is the capital position at risk?

4. Is the bank exposed to liquidity and funding risk?

Overall SREP assessment

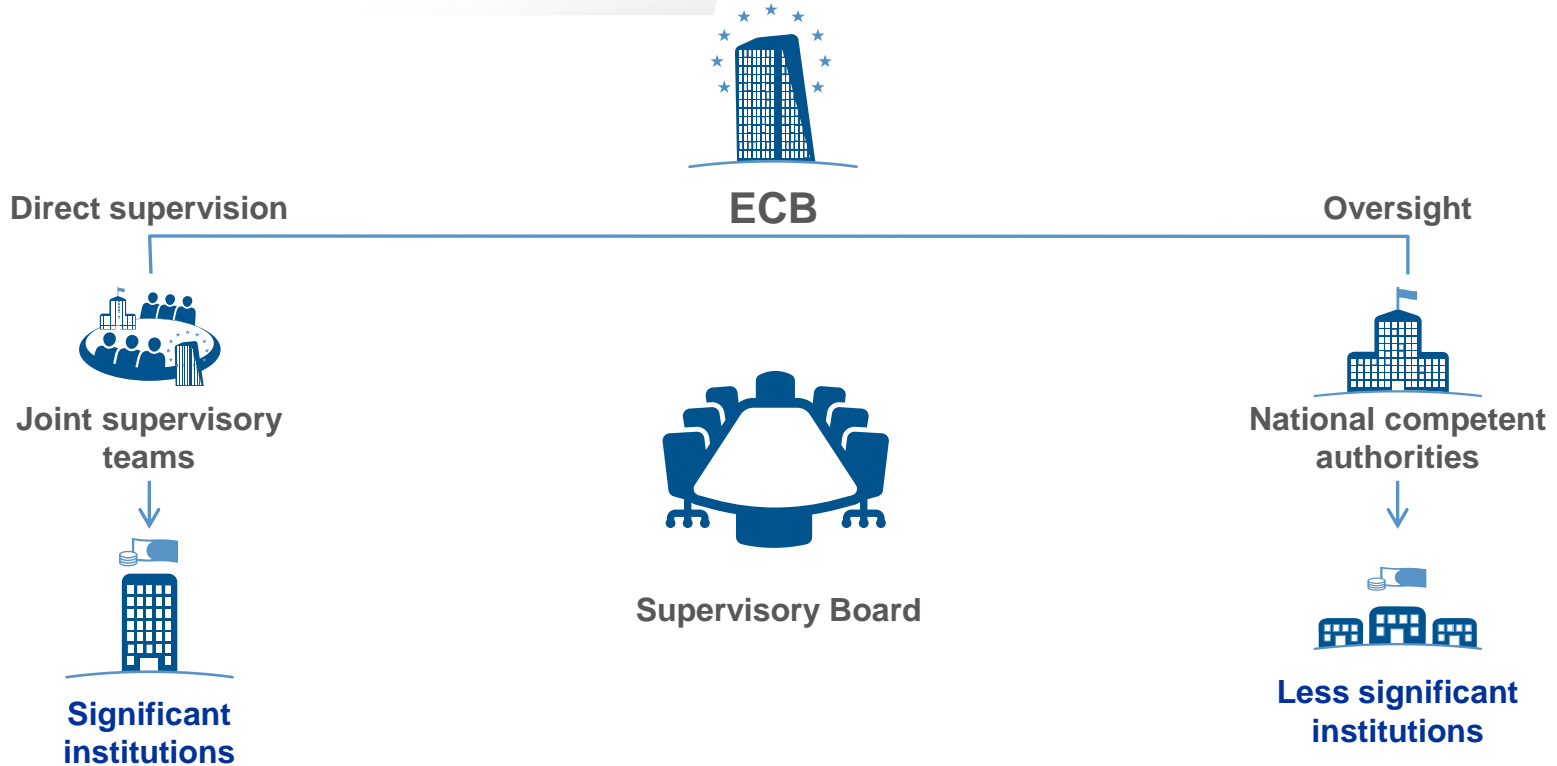
SREP decision

Qualitative supervisory measures

Quantitative liquidity measures

Quantitative capital measures

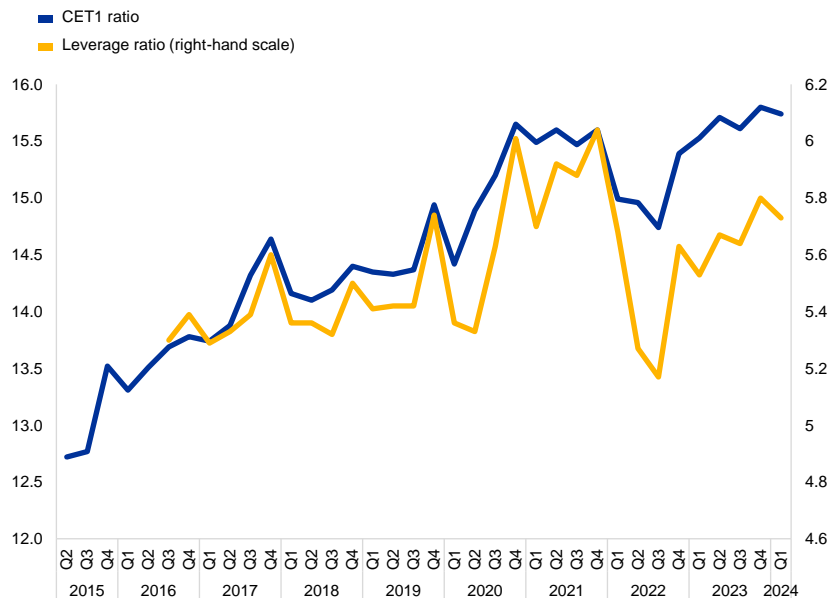
Within the Single Supervisory Mechanism, the ECB and national supervisors cooperate closely.



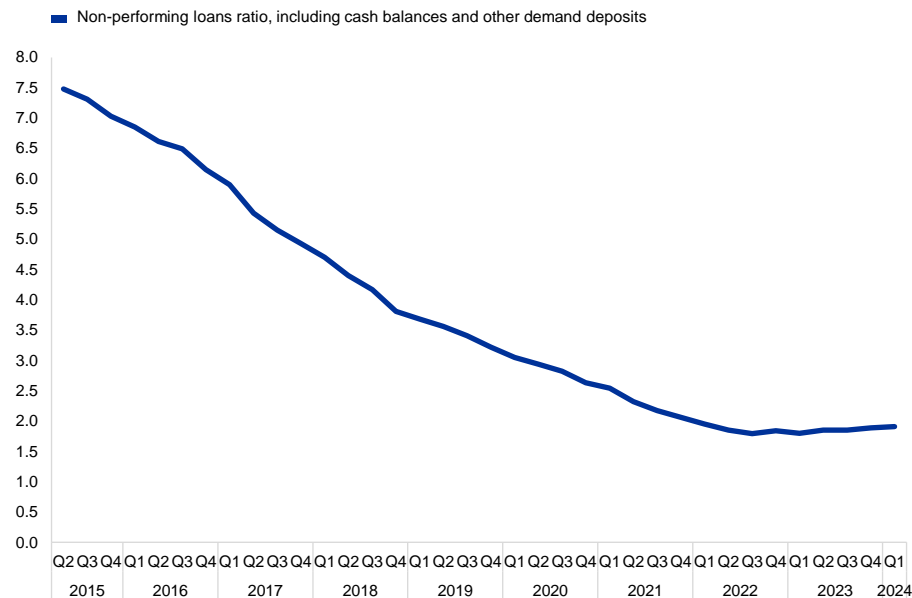
How has the risk environment evolved?

Over the past decade, the resilience of European banks has increased and non-performing loans have declined ...

Capital adequacy (percentage)

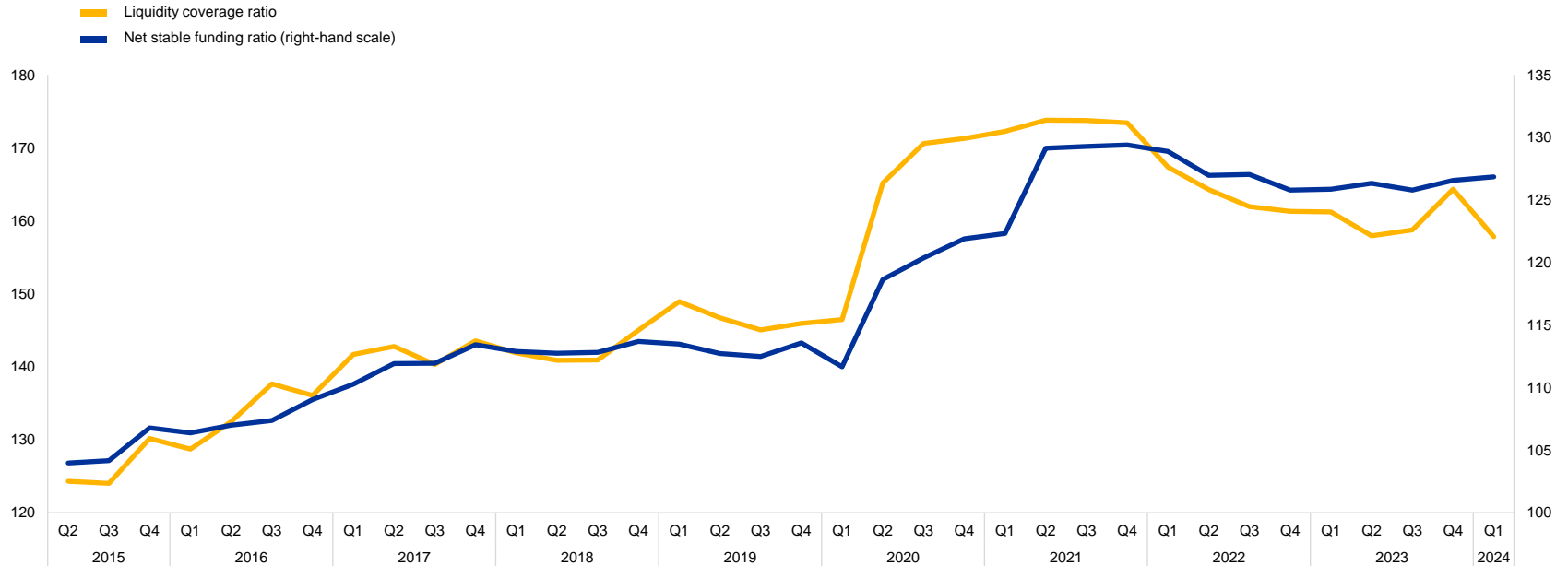


Non-performing loans (percentage)



...while liquidity ratios have improved.

Liquidity ratios (percentage)



At the same time, the risk environment has been evolving, as reflected in the SSM supervisory priorities.



New macro-financial environment



Heightened geopolitical risks



Climate-related and environmental risks



Digitalisation and demographic change



SSM supervisory priorities (2024-2026)

Priority 1

Strengthen resilience to immediate macro-financial and geopolitical shocks

Priority 2

Accelerate remediation of shortcomings in governance and the management of climate-related and environmental risks

Priority 3

Further progress in digital transformation and building robust **operational resilience** frameworks

How is European supervision responding?

The independent experts assessed the evolution of European banking supervision over the past decade.

- The independent expert group noted progress ...
 - *The SREP “has significantly helped to increase the resilience of the European banking sector and to promote a level playing field for all significant institutions.”*
- ... but it also indicated room for improvement:
 - *“Today’s environment calls for a careful recalibration of the SREP and other supervisory processes.”*

The reform of the supervisory process decided by the Supervisory Board in May 2024 has six objectives.

1 Focusing risk assessments

2 Better integrating supervisory activities

3 Using the full supervisory toolkit

4 Enhancing communication

5 Making methodologies more stable

6 Better use of IT systems and data analytics

Focusing risk assessments using multi-year assessments and a risk tolerance framework



- **Risk tolerance framework** (introduced in 2023)
 - Not every risk is of the same relevance for every bank in every year.
 - Prioritise risk assessments

- **Multi-year assessment** (introduced in 2023)
 - Risk assessment are spread over several years to focus on specific topics each year.
 - Risk assessment are updated every two years *if there is no material change in a bank's risk profile.*



Better integrating supervisory activities to use synergies and optimise planning

2

Stress testing and scenario analysis



Horizontal thematic reviews



Targeted deep-divide analysis



On-site inspections



Internal model assessments

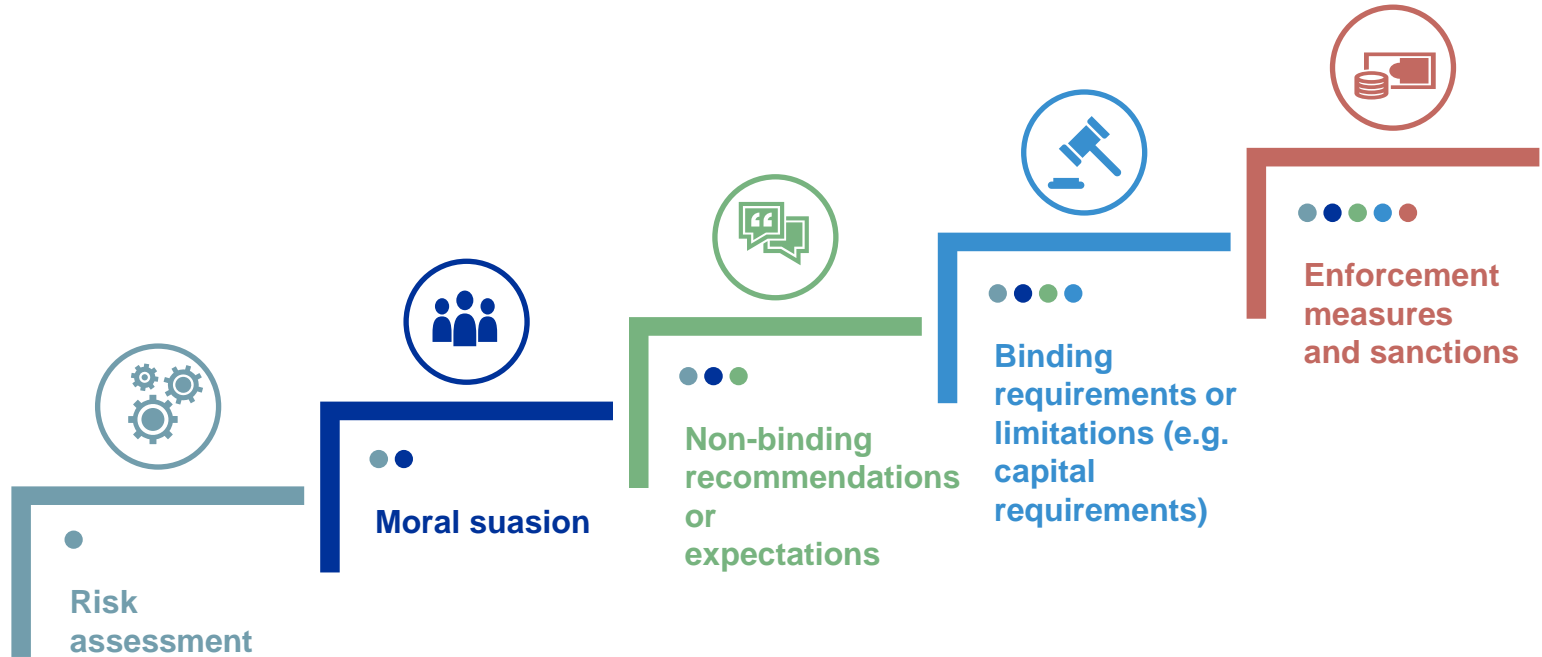


Off-site supervision



Using the full supervisory toolkit and moving up the escalation ladder faster to ensure findings are being addressed

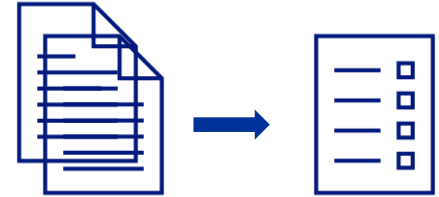
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Enhancing communication by streamlining the SREP decision

4

- **Supervisory communication to banks needs to be clear, concise and timely** – but SREP decisions can be long and complex.
- **Future SREP decisions will be more focused and conveyed earlier.**



Making methodologies more stable to allow focusing on newly emerging risks

5

1. Is the business model viable and sustainable?

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4. Is the bank exposed to liquidity and funding risk?



Methodology to calculate overall SREP score



SREP decision

Qualitative supervisory measures

Quantitative liquidity measures

Quantitative capital measures

Making better use of IT systems and data analytics to increase efficiency and save time on routine tasks

6



AI-powered textual analysis platform



Graph and network analytics platform



SSM-wide digital collaboration platform



Single data lake



Machine reading and analysis of fit and proper applications



Big data analytics

These reforms allow supervisors to more effectively respond to evolving risks.

- **Good supervision requires ...**
 - a critical mindset
 - sound analysis of microeconomic and macroeconomic risks
 - follow-up on findings not yet addressed
- **... and it needs to respond to evolving risks:**
 - through strong supervisory and regulatory standards
 - by ensuring sufficient operational and financial resilience of banks
 - by addressing risks outside of the banking sector

Suggestions for further reading

- Dahlgren, S. Himino, R. Restoy, F. Rogers, C. (2023), [“Assessment of the European Central Bank’s Supervisory Review and Evaluation Process – Report by the Expert Group to the Chair of the Supervisory Board of the ECB”](#)
- Buch, C. (2024), [“Reforming the SREP: an important milestone towards more efficient and effective supervision in a new risk environment”](#), *Supervision Blog*, 28 May
- [ECB Banking Supervision, Supervisory review \(SREP\)](#)
- [ECB Banking Supervision: SSM supervisory priorities for 2024-2026](#)