



EUROPEAN CENTRAL BANK

BANKING SUPERVISION

# Geopolitical Risks and SSM Supervisory Priorities

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*Geopolitics: Between Risk Factors and  
Opportunities – Italian Banking  
Association event*



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# What are geopolitical risks?

Tentative definition for complex and multi-faceted risks

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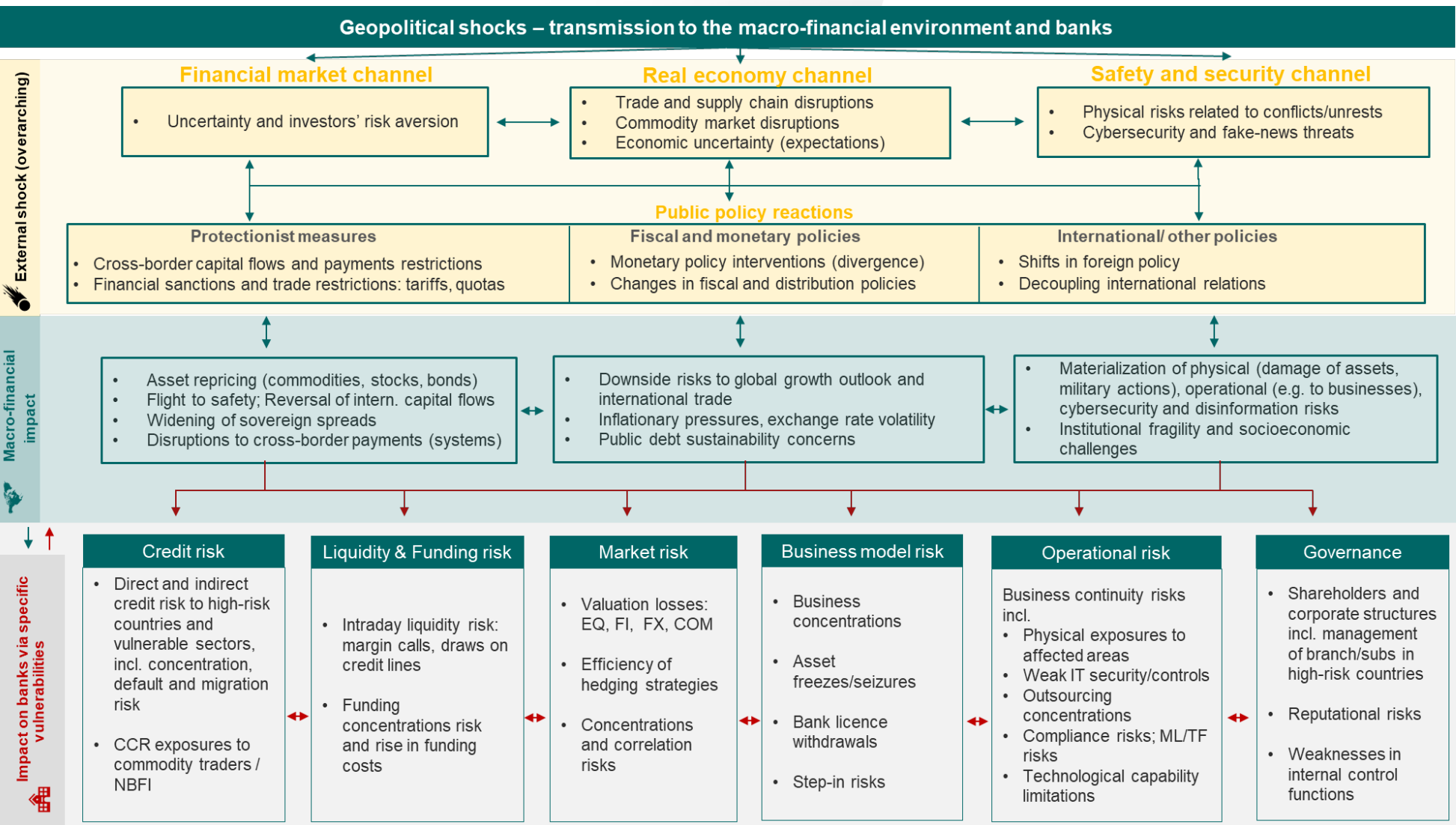
## Geopolitical risks definition:

*“Threat, realization, and escalation of adverse events associated with wars, terrorism, and any tensions among states and political actors that affect the peaceful course of international relations”\**.

**Multi-faceted**, geopolitical risks **span a broad and heterogenous set of issues** including political, economic, military and security, social, environmental risks. These risks **emerge whenever there is a major shift** in power, disruptions in international order and relations, rising inter-states tensions or a crisis and can **materialise** as wars, conflicts, terrorism, cyber-attacks, trade disputes, sanctions, regulatory changes, and political instability, each **capable of disrupting** global financial markets, economies, and diplomatic ties.\*\*

\*Definition from *Measuring geopolitical risk* (Iacoviello & Caldara, 2022) \*\* Broader definition based on *Measuring geopolitical risk* (Iacoviello & Caldara, 2022) and *Geopolitical risks and banking sector vulnerabilities: implications for the SSM* (Lehmann, 2022). See also: Economics observatory: “How are geopolitical risks affecting global economy”. See also Claudia Buch: , Sep 2024.

# Geopolitical risk as cross-cutting concern



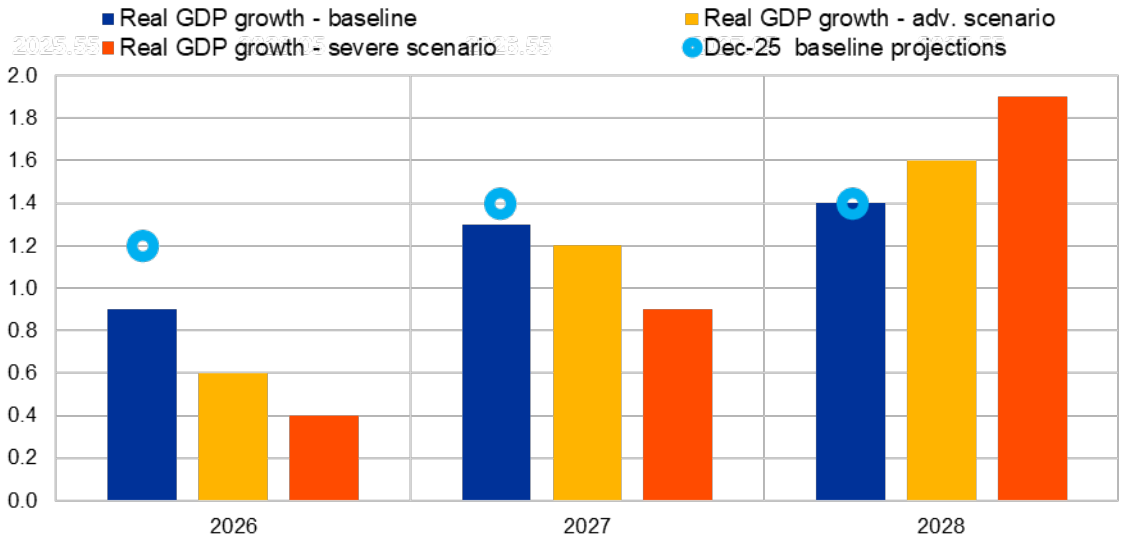
Three main transmission channels...

... impacting the macro-financial environment ...

... and susceptible to exacerbate banks' vulnerabilities across the supervisory taxonomy

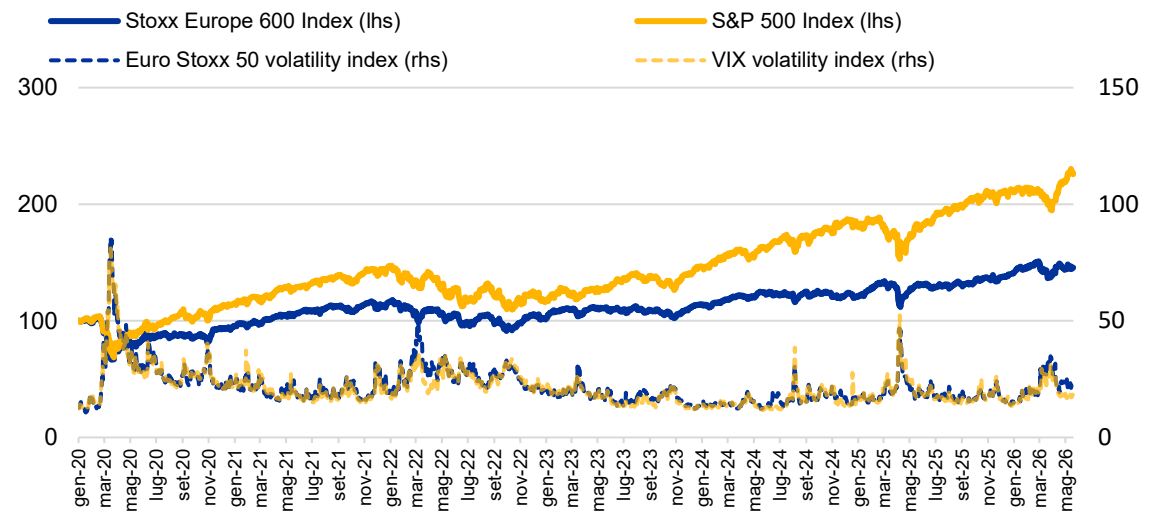
# High uncertainty and energy supply disruptions caused by the Middle East war challenge euro area economic resilience and trigger volatility in financial markets

**GDP growth in the euro area remained resilient in 2025, but the war in the Middle East clouded again the outlook**  
 Real GDP growth projections (in %)



Source: ESCB staff macroeconomic projections, March 2026.

**Middle East tensions led to an increase in volatility, high valuations highlight correction risks**  
 EA and US equity and volatility (1 Jan 2020 = 100)



Source: Bloomberg Finance L.P. Latest observation: 19 May 2026.

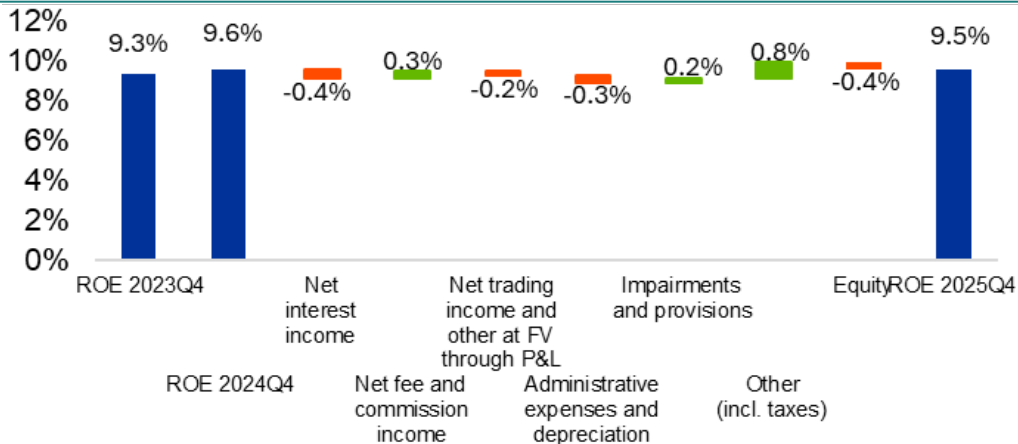
- Elevated energy prices and heightened uncertainty have led to a downward revision of the short-term growth outlook, while inflationary pressures are building up.
- High public debt and prospects of rises in budget deficits and tightening financing conditions are putting countries on a weaker fiscal trajectory.

- Escalating tensions in the Middle East triggered a sharp repricing in equities over March, followed by a quick rebound in April
- Financial markets remain vulnerable to sharp adjustments due to persistently high valuations and concerns about AI disruption risk.

# Supervised banks remain resilient so far in the challenging environment

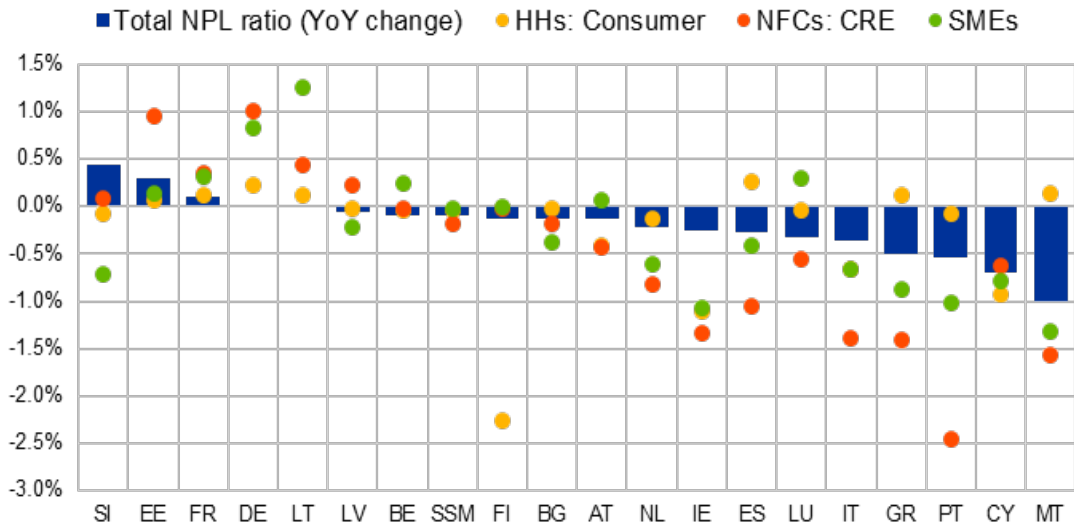
## Banks' profitability remains close to historical highs

ROE annualised YoY decomposition (%)



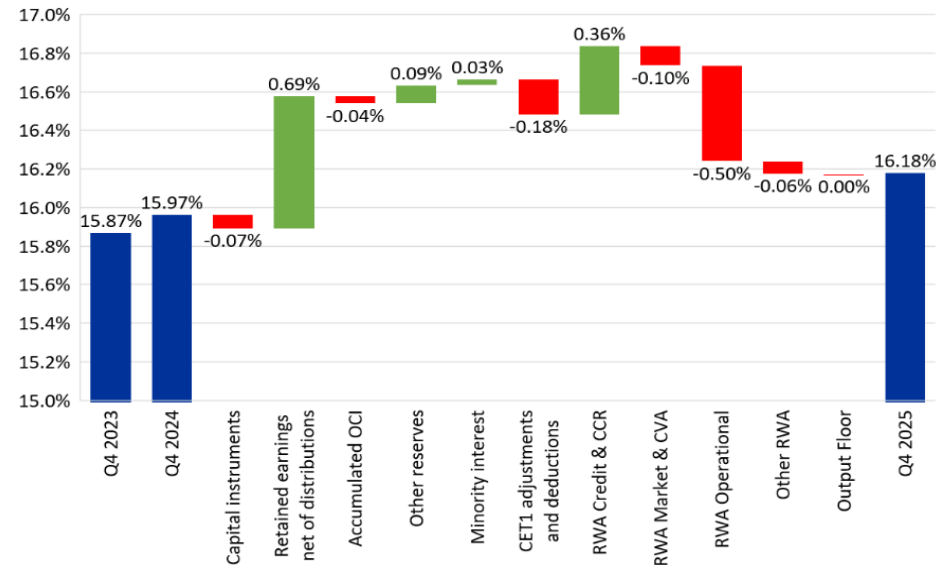
## Benign overall asset quality but with pockets of risks

NPL ratio by country and asset class (Q4 2025, %)



## CET1 ratio increased in 2025, primarily driven by earnings ...

CET1 ratios waterfall chart YoY evolution (Q42024-Q42025)

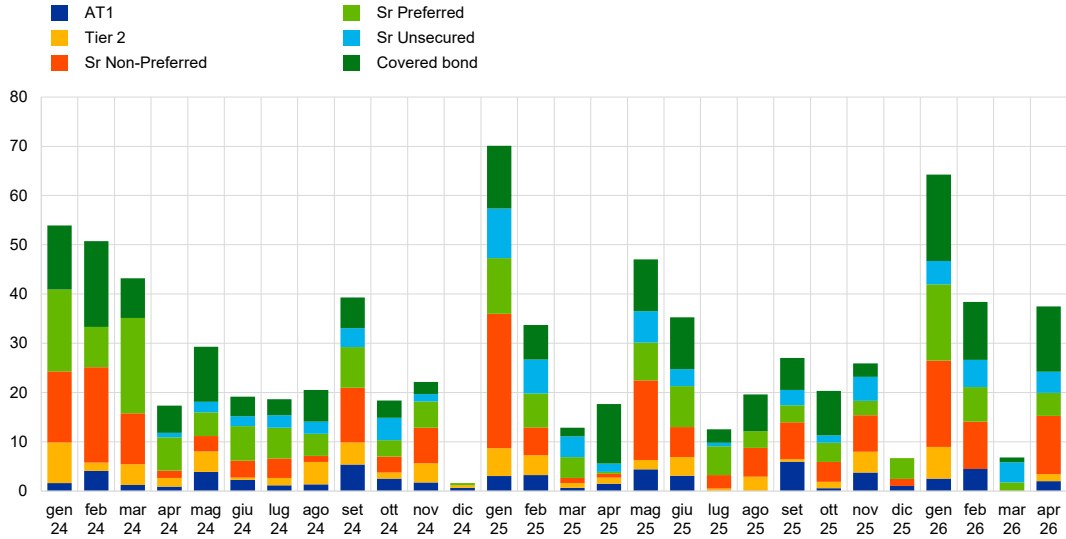


- Robust profitability driven by stronger-than-expected net operating income, cost discipline and limited credit risk.
- CRR3 implementation did not trigger major aggregate RWA impact.
- Healthy households' and firms' balance sheets are supporting asset quality at aggregate level, with only a few countries/banks recording some deterioration, especially in CRE and SME.
- Sectors more exposed to trade and more energy intensive may be particularly hit by ongoing geopolitical shocks.

# While liquidity ratios are robust, geopolitical uncertainties keep FX funding risks in the spotlight. Banks display robust IRRBB profiles while CSRBB is rising ...

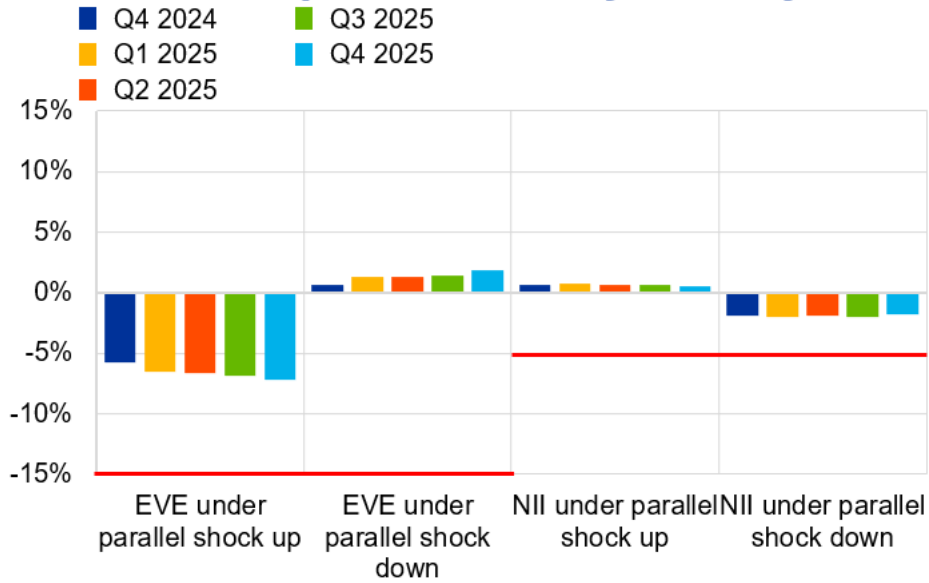
## Market-based funding conditions remained resilient despite geopolitical uncertainties

SSM SIs bond issuances (EUR bn)



## Stable and contained aggregate exposure to interest rates parallel shifts year-on-year

SOT: ΔEVE and ΔNII, +/-200bps IR scenario (% of T1 capital)



Sources: Supervisory reporting

- Robust and stable liquidity ratios (LCR: 158.6%, NSFR: 126.5% in Q4 2025)
- Market-based funding conditions proved resilient so far, despite the looming Middle East conflict-induced uncertainty. Execution of banks' 2026 funding plan on average well underway (~45% on average) due to front-loading at the end of 2025 and strong issuances at the start of the year.
- Strong reliance on short-term USD funding for certain banks remains "on watch".

- At end-2025, banks projected stable IRRBB exposures, and robust NII levels for 2026 in a baseline scenario.
- Limited EVE/NII SOT breaches under +/- 200 bps scenario.
- Growing sovereign debt holdings and tight spreads across markets to challenge CSRBB under adverse scenarios.

# Supervisory priorities for 2026-28: What's coming next?

## Strengthening financial and operational resilience of the banking sector

### Supervisory priorities for 2026-28

#### Priority 1: Strengthening banks' resilience to geopolitical risks and macro-financial uncertainties

Ensure prudent risk-taking and sound credit standards



Credit risk

Ensure adequate capitalisation and consistent implementation of CRR III



Multiple risk categories

Ensure prudent management of climate and nature-related risks



Multiple risk categories

#### Priority 2: Strengthening banks' operational resilience and fostering robust ICT capabilities

Implement robust and resilient operational risk management frameworks



Operational risk

Remedy deficiencies in risk reporting capabilities and related information systems



Governance

**Medium to long-term priority strategy** focusing on banks' digital and, in particular, AI-related strategies, governance and risk management



Multiple risk categories

1. **Supervisory priorities for 2026-28 are more targeted**, supported by a more streamlined set of activities.
2. **Timely and effective remediation of material findings** is a cornerstone of the supervisory strategy.
3. **Geopolitical risks and their potential impact on banks** remain a key driver of the prioritisation exercise.

# Special focus: 2026 SSM Geopolitical Risks Reverse Stress Test

## Complement EU-wide ST by focusing on supervised banks specific risks

**Objective: Identify bank-specific geopolitical risks vulnerabilities, assess and strengthen banks' risk management capabilities ....**



### 2026 thematic stress test key features

- **110 SSM Significant Institutions**
- GPR materialisation leading to a **targeted depletion**, before any discretionary mitigating actions.
- **Free-form approach**: banks will use own models, methodologies and scenarios, with standardised reporting.
- Apart from solvency focus, impact on **funding/liquidity**.

### Design and deliverables of the exercise

- **Lean approach**: Minimum methodological constraints, basic data quality checks and quality assurance.
- **High-level findings will feed into the SREP in a more qualitative way** in line with the broader 2026 ICAAP assessment. **No direct capital implications (P2G)**.
- **Bank-specific reports and aggregate results publication.**

# Governance and risk management of geopolitical risks

- *“Sound governance and risk culture contribute to promoting a more sustainable business model over the full business cycle. This is especially important in an environment in which banks face economic, financial, competitive, and geopolitical headwinds<sup>1</sup>.”*



- [Internal governance and risk management SREP methodology](#)
- [Guide on effective risk data aggregation and risk reporting](#) as reliable risk data aggregation and reporting capabilities play a key role in GPR risk monitoring and decision-making
- [Draft guide on governance and risk culture](#) e.g. on how GPR is reflected in RAF and internal control activities



- Targeted benchmarking exercise on risk appetite and risk culture, with a focus on reflecting the implications that geopolitical risks have for banks' risk identification and risk appetite frameworks (RAF).
- 4Q24-1Q26, sample of  $\approx 50$  SIs<sup>2</sup>



- On GPR governance and reporting, risk identification, RAF, decision-making
- Identified via **ongoing supervision**, **benchmarking exercises** and **reflected in the Guides**
- No new obligations/expectations for banks - **illustrative examples** of approaches that, in our experience, have worked well in certain contexts.

<sup>1</sup> Section 1 of the draft Guide on governance and risk culture. The Guide is still in draft stage and cannot be applied before its finalisation.

<sup>2</sup> See [Aggregated results of the 2025 SREP](#) and [supervisory priorities 2025-2027](#)

# Geopolitical risks: ECB Banking Supervision’s broader perspective to ensure that banks properly account for this cross-cutting risk driver

### Identify events and risks

- Develop internal processes to identify GPR events that could impact the institution or its clients
- Assess how direct and indirect exposures may be affected by events like sanctions, trade disruptions, energy price shocks etc.
- Consider potential impacts on delivery channels, financial markets, and international trade

### Assess need for action

- Ensure that all risks are well-managed and covered
- Evaluate whether additional actions are required to mitigate risks or reduce exposures
- Prepare also for low-probability, high-impact events

### Monitor and respond proactively

- Implement ongoing monitoring processes, including early-warning systems
- Tailor risk management strategies to the institution’s unique exposures and vulnerabilities



### Simulate impacts

- Use tools like stress testing and scenario analysis to simulate the effects of geopolitical events
- Assess potential impacts of events which may directly affect the business viability of bank clients

### Strengthen governance and resilience

- Establish robust governance frameworks, incl.:
  - Clear organizational structure and responsibilities
  - Effective risk management processes and control mechanisms
  - Strong risk appetite frameworks and data aggregation capabilities
- Enhance operational resilience by:
  - Managing dependencies on third-party providers
  - Protecting against cyber threats, IT disruptions, and physical risks
  - Ensuring contingency planning and preparedness for infrastructure

Source: [Final results 2025 stress test](#), Box 6 “Managing geopolitical risks”.

Since GPR is not a new risk but rather a risk trigger that can have effects on traditional banking risks, many existing recommendations could be applied to GPR. No dedicated guidelines were developed on GPR. See more at: [Addressing the impact of geopolitical risk](#)



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Thank you for your attention

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