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Revenue And Diversification in Europe. Evidence From EBA (2016Q1-2024Q4)

Ifigeneia Persaki

University Of Macedonia, Greece

Abstract

This paper examines the relationship between revenue diversification and bank performance and risk in Europe using a comprehensive quarterly panel of commercial banks based on supervisory data from the European Banking Authority (EBA) covering the period 2016Q2–2024Q4. Over the past decade, European banks have increasingly diversified away from traditional interest-based activities toward non-interest income sources in response to low interest rates, regulatory pressures, and structural changes in financial intermediation. Despite the growing importance of these activities, their implications for bank profitability and risk remain ambiguous, particularly in the European context and during periods of heightened economic uncertainty.

The analysis focuses on non-interest income as a central dimension of banks' business model diversification. Bank performance is measured using return on assets (ROA) and return on equity (ROE), while bank risk is captured through earnings volatility indicators based on the standard deviations of ROA and ROE. Revenue diversification is proxied by the ratio of non-interest income to total operating income. The dataset allows for a detailed and harmonized examination of bank balance sheet characteristics across European countries using supervisory information that is rarely exploited in the academic literature.

The empirical strategy relies on bank-level fixed-effects panel regressions that control for a rich set of covariates, including bank size, asset growth, balance sheet composition, capitalization, funding structure, and credit risk. To further explore dynamic effects and short-run adjustments, the paper employs change-in-change specifications based on quarterly variations in performance and risk measures. This approach helps capture how changes in revenue structure translate into contemporaneous changes in profitability and risk, while mitigating concerns related to unobserved heterogeneity.

The results indicate that revenue diversification does not uniformly improve bank performance. While greater reliance on non-interest income is associated with higher profitability in certain specifications, it is also linked to increased earnings volatility, pointing to a clear trade-off between returns and risk. Importantly, the findings show that these effects become more pronounced during the post-COVID period, suggesting that the role of non-interest income varies across economic conditions. In particular, diversification may act as a stabilizing factor for some banks while amplifying risk for others, depending on balance sheet characteristics and funding structures.

Overall, the paper contributes to the applied economics and banking literature by providing updated evidence on the performance–risk implications of revenue diversification in European banking using harmonized supervisory data over an extended post-crisis period. The findings offer relevant insights for researchers and policymakers concerned with bank business models, income sustainability, and financial stability in Europe.

Keywords: Revenue Diversification; Non-Interest Income; Bank Profitability; European Banking; Panel Data Analysis; Earnings Volatility