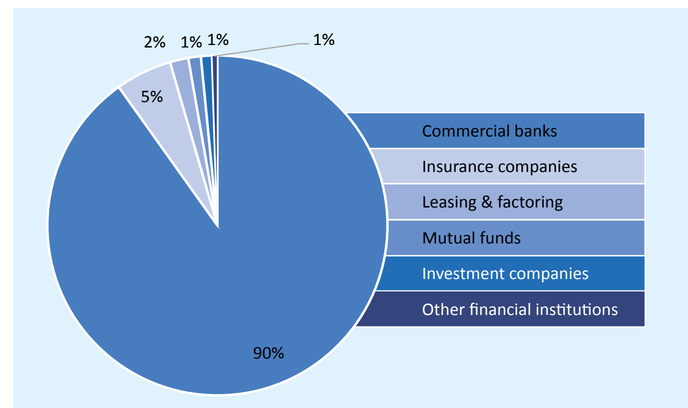
Black Sea Trade & Development Bank

Overview of the financial sector in Greece

The financial sector in Greece mostly consists of commercial banks which account for 90% of total financial sector assets. Insurance companies account for another 5%, while other financial institutions such as leasing and factoring companies, mutual funds, and investment companies are small with shares below 5% and do not have a significant impact on the health of the financial sector. The present analysis will focus on commercial banks.

Figure 1. **The structure of the financial sector in Greece, December 2020**



Source: Bank of Greece

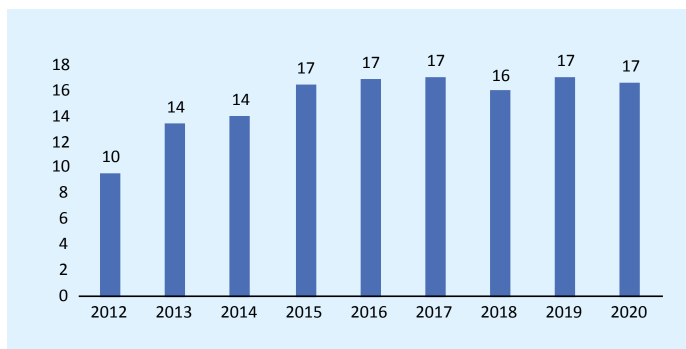
Banking is a large sector of the economy in Greece, with the sector's total assets at around 200% of GDP. The asset to GDP ratio ranks highest among the BSTDB member countries and is well above the euro area average of 86%. Banking sector loans corresponded to 93% of GDP in 2020, which is also the highest number in the region. The sector is relatively concentrated with the four largest banks holding more than 80% of assets. However, individual shares of these banks are around 20% each indicating a relatively competitive market structure.

The banking sector in Greece went through a series of crises in the period from the Great Financial Crisis in 2008 until 2016. This process was accompanied by large scale deleveraging as banks reduced lending significantly with the credit portfolio shrinking every year. As a result, the share of loans in total assets of the banking sector came down from more than 60% in 2017 to 46% in 2020, which is relatively low compared to other countries in the region. Liquid assets increased in recent years and accounted for 39% of total assets indicating the strong liquidity buffers in the system. Deposits accounted for 76% of total liabilities and remain the main source of funding for the banking sector. Household deposits that are considered a more stable source of funding, at around 60% have the largest share in total deposits. The reliance of the banking sector on central bank financing is relatively high, with the Bank of Greece accounting for 15% of total liabilities.

After dropping to 10% in 2012, the Capital Adequacy Ratio (CAR) recovered in the following years and reached 17% in 2020. Although CAR is well above the regulatory minimum, quality remains a concern as a significant part of the capital, roughly 60 percent of Common Equity Tier 1 (CET1) capital[1], consists of Deferred Tax Credits (DTCs) that has limited loss absorption capacity.

[1] Second post program monitoring discussions, staff report, November 2020, IMF.

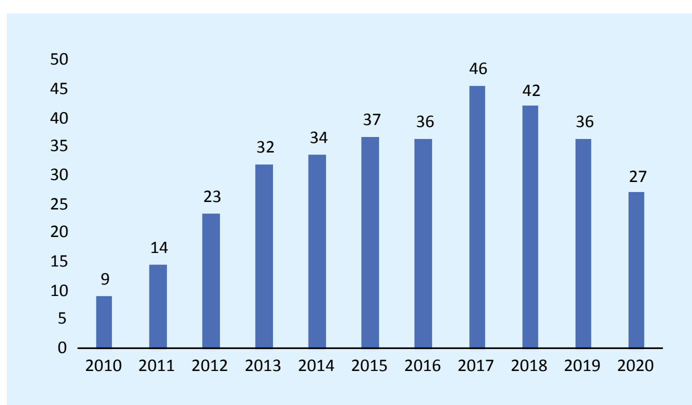
Figure 2. **Regulatory capital to risk-weighted assets (%)**



Source: Financial soundness indicators, IMF database

While down to 27% at the end of 2020, NPLs in Greece remain elevated and are the highest among EU countries and the second highest among BSTDB member countries after Ukraine. As such, they remain the major challenge for the banking sector. NPLs started to increase in Greece after the Great Financial Crisis in 2008. Sovereign debt and banking crises in the following years further accelerated the pace of NPL growth and in 2017 bad loans amounted to 46% of the total credit portfolio. To clean up the balance sheet of commercial banks, which is essential to support efficient financial intermediation in the country, the authorities proposed a debt securitization program – which was given the name “Hercules”. The program envisaged pooling non-performing loans that are restructured, securitizing them, and selling them to international and domestic investors while the government provides a guarantee for repayment. With the help of the program, NPLs came down by EUR 35bn in the last two years, corresponding to a 42% decline. Recently the government announced an extension of the loan securitization program that will further reduce NPLs in the system. However, economic recession stemming from the pandemic crisis could push NPLs upward as the loan moratoria and government introduced targeted subsidies for loan repayments are over.

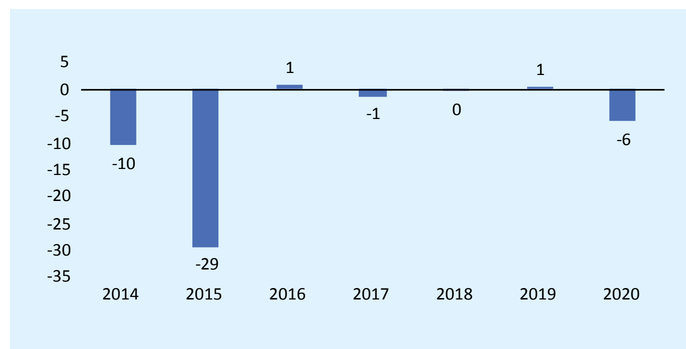
Figure 3. **Non-performing loans to total gross loans (%)**



Source: Financial Soundness Indicators, IMF database

The large volume of non-performing loans puts downward pressure on banks’ profitability. In 2014-2015 banks reported large losses as ROE dropped to -29%. In later years the banking sector performance improved somewhat, but ROE still stayed either negative or close to zero. In 2020, as the pandemic crisis hit, banks’ losses increased again, and ROE was negative at -6%.

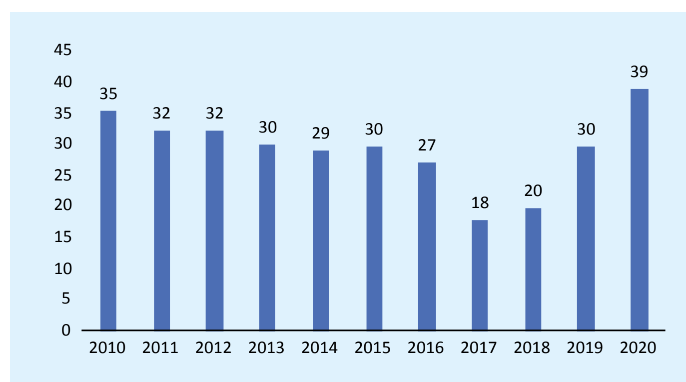
Figure 4. **Return on equity (%)**



Source: Financial soundness indicators, IMF database

At present, the banking sector maintains solid liquidity buffers. In 2015 the banking system experienced significant deposit outflow as an agreement could not be reached with European Commission on terms of the financial assistance. The deposit outflow intensified further after the country was unable to make IMF debt repayment and introduced capital controls to stop money leaving its banks. As a result, the sector suffered from scarce liquidity and consequently in 2017 the share of liquid assets dropped to 18% of total banking sector assets. In the last 3 years, together with the strong growth of deposits and gradual removal of capital controls liquidity in the system has recovered and by the end of 2020 reached to 39% of the total assets.

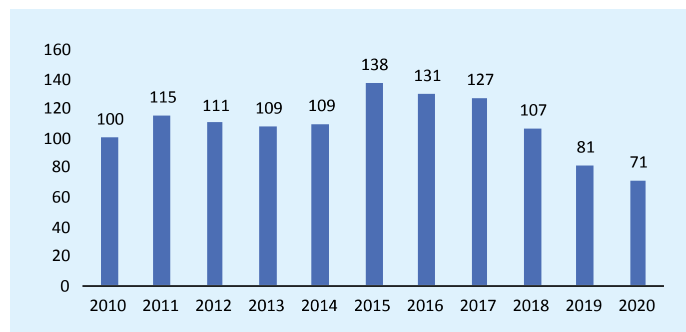
Figure 5. **Liquid assets to total assets (%)**



Source: Financial soundness indicators, IMF database

During the banking crisis, the loan to deposit ratio increased as the banking sector experienced a significant outflow of deposits with the deposit base almost halving in 2010-2015. By the end of 2015 loan to deposit ratio stood at 138%. In the last three years as deposit growth recovered while the loan portfolio continued to decline, the loan to deposit ratio declined significantly to one of the lowest levels among BSTDB member countries at 71%.

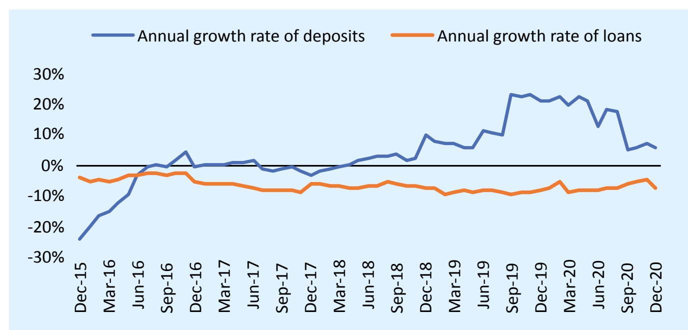
Figure 6. **Total loans to customer deposits (%)**



Source: Financial soundness indicators, IMF database

Since the financial crisis in 2008, the banking sector in Greece has shrunk significantly. Both credit and deposit aggregates continuously declined. From 2010 to 2018, the stock of outstanding loans and deposits fell by 45% and 42% respectively. In the last two years, however, the declining trend in deposits reversed with deposits increasing 21% in 2019. In 2020, due to the pandemic crisis, deposit growth slowed to a 6% annual rate.

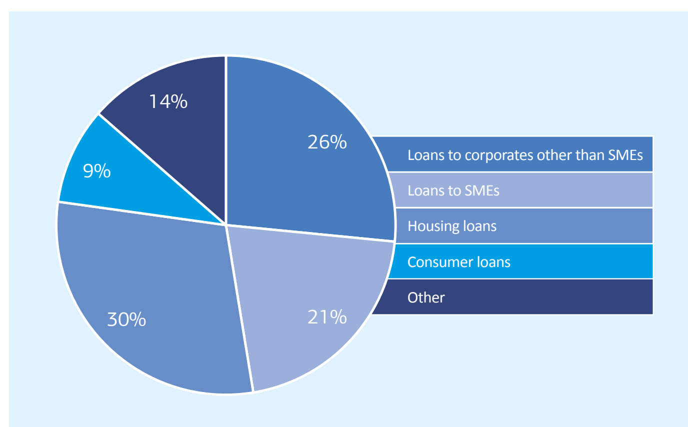
Figure 7. **Growth rates of loans and deposits**



Source: Bank of Greece

Loans to households accounted for 39% of the total credit portfolio of banks in 2020, out of which housing loans have the largest share with 30 percentage points. Exposure to corporates accounts for 59% of the total credit portfolio with loans to SMEs having the most important contribution with 26 percentage points.

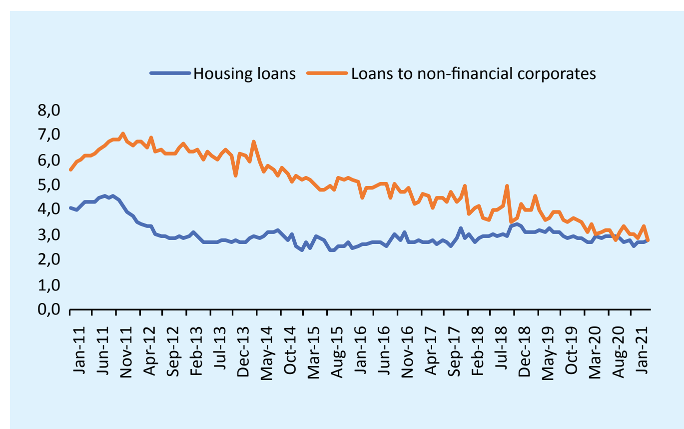
Figure 8. **The structure of the credit portfolio, December 2020**



Source: Bank of Greece

Interest rates on loans to households for housing purposes have not changed much over the last 10 years and by the end of 2020, they stood at close to an annual rate of 3%. In contrast, for loans to corporates interest rates have declined over the last decade, with the annual interest rate down from 7% in 2012 to 3% by the end of 2020.

Figure 9. **Interest rates on loans**



Source: Bank of Greece

Greece went through a large-scale crisis in the period of 2008-2016 that resulted in a massive increase in NPLs, huge losses incurred by the banking sector, a drop in capitalization, a general loss of confidence, and deposit outflows. To overcome the difficulties the banking sector required significant injections of capital. For the period between 2008 and 2018, capital injections by public finances amounted to around EUR 50bn, which corresponded to 30% of GDP[2] in 2020. To clean up the balance sheet of commercial banks, authorities launched a program to securitize and sell bad loans that helped to reduce NPLs in the system significantly. The authorities plan to continue the program further. Even after this clean-up NPLs remain elevated at 27% in 2020. Capital adequacy has recovered in recent years, but the quality of the capital remains concern as a large part of the Tier 1 capital consists of Deferred Tax Credits with limited loss absorbing capacity. A large amount of bad loans has a negative impact on banks profitability with the ROE staying negative or close to zero for the last 7 years. Positive developments were observed in the last 2 years as deposits grew 21% in 2019 and another 6% in 2020. Strong deposit growth supported the accumulation of large liquidity buffers in the system as the share of liquid assets increased to 39% of total assets.

[2] 2019 article IV consultation, staff report, IMF.