Conference of the Hellenic Banks Association and the European Mortgage Federation

on

"Current Developments and Challenges in the Mortgage Market"

Welcome address

by

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1. Introductory remarks

I am very pleased to be with you this evening on the occasion of the meeting of the Executive Committee of the EMF in Athens. As a former member of this Committee, in my capacity as Chairman of the National Mortgage Bank of Greece, I am fully aware of the work of the EMF; efficiently representing the interests of the European mortgage credit market. As President of the Hellenic Bank Association, which is the regular representative of Greece at the EMF, I can assure you that we follow the work of the EMF closely and contribute to its effectiveness.

The conference deals with two crucial financial regulatory initiatives: the new “Basel III” framework and the principle of “responsible lending” in mortgage credit. The importance of the selected topic is significant, since both these initiatives will affect the European mortgage credit market in important ways in the years to come.

However, since we are in Greece and the Greek crisis is one of the major issues affecting the European financial system, allow me to provide you with my insights on the current situation.

2. The recent global financial crisis and its implications on the banking system

An important starting point is that the Greek banking sector did not trigger the economic strains and the fiscal crisis in our country, as has been the case in many other countries. On the contrary, it was the Greek fiscal crisis that has negatively affected the Greek banking system.

Indeed, the initial spill-over effects from the global financial crisis on the Greek banking system were very limited. Greek banks have shown remarkable resilience and were able to overcome those difficulties due to a number of factors:

- they were not exposed to the risks that triggered the causes of the recent financial crisis, e.g. structured products, quasi off-balance sheet exposure, high leverage,
- they had a strong capital base and steadily increased their provisions against unexpected losses,
- they followed prudent credit and market risk management policies,
- the effective micro-prudential supervision exercised by the Bank of Greece ensured the stability of the Greek banking system.

Accordingly, **the activation of a bank rescue programme in Greece in late 2008 was mostly for prudential purposes.** Specifically, the recovery programme adopted by the Greek Government for €28 billion was *mainly* aimed at the enhancement of liquidity conditions in the system and access to this package at that time was extremely limited.

In addition, the level of deposit guarantee was raised to €100,000 (from €20,000) per depositor, immediately after the collapse of Lehman Brothers in order to enhance depositor confidence in the system, a move which proved successful.

Overall, during the global financial crisis of 2008-2009, the Greek banking system remained healthy, adequately capitalized, and quite profitable. The outlook changed when the world recession eventually hit Greece, with output declining sharply in the second half of 2009 and 2010, and exposing underlying fiscal weaknesses, which were compounded by the political cycle. The sharp deterioration in the fiscal accounts and the distrust of markets, resulted in the need for an unprecedented support package from the IMF and the EU, in combination with special terms of access to the ECB liquidity facility.

The adjustment programme has had many successes during its first year -- a fiscal adjustment of over 5 pps of GDP and important structural reforms, such as the pension reform, the labour market reform, and the opening of closed professions. Nevertheless, the revenue shortfalls in early 2011 and delays in implementing other structural reforms has led to the conclusion that the adjustment programme needs more time to be implemented or to be effective. Thus, a new enhanced programme is currently being discussed.

Let me now turn to how these developments are affecting the banking system.

3. The implications on the banking system

The Greek crisis has negatively affected the Greek banking system in the following two ways:

Firstly, bank liquidity remains very tight:

- bank deposits declined by nearly 20% since late 2009, despite the fact that interest rates for new deposits from households with agreed maturity up to 1 year were the 2nd highest within the eurozone (3.73% in March 2011),
- access to the interbank market as well as the money and debt capital markets remains extremely limited,
- borrowing from the ECB represents, currently, nearly 20% of banks' liabilities, albeit on a slowly declining trend (December 2010: €97.7 billion, March 2011: €87.9 billion)

Secondly, due to the recession, non-performing loans increased to 10.4% in December 2010 (from around 5% pre-crisis levels), mostly reflecting developments in the household sector, though corporate delinquencies are now picking up at an accelerating rate. The only good news is that 74% of NPLs regard secured loans, loans to non-financial corporations and mortgage loans.

The initial conditions of the banking system are providing it with important support: low leverage and thus low reliance on wholesale markets, high capital ratios and high profitability. This was attested to by the results of the EU-wide stress-testing exercise – conducted in 2010 by the predecessor of the European Banking Authority (the Committee of European Banking Supervisors), in close cooperation with the European Central Bank. Indeed, the results for the six Greek banks tested were positive [the exception being Agricultural Bank]. In fact, they indicated a net surplus of Tier 1 capital of the order of €3.3 billion above the 6% ratio of Tier 1 capital that was agreed as a benchmark, solely for the purpose of the stress test (the baseline scenario). The upcoming EBA stress test results in July will reconfirm the resilience of the Greek banking sector.

It is important to note that, despite the negative macroeconomic conditions, some banks have managed to carry out successful capital issues: the National Bank of Greece by €1.8 billion, and Piraeus Bank by €800 million.

4. Institutional measures

Apart from the initiatives underway to help preserve sufficient liquidity in the system, two institutional measures have been taken in order to safeguard its resilience:

(a) Government guarantees were issued to be used by Greek banks as collateral in order to obtain funding from the European Central Bank (€30 billion, over and above the original €55 billion). These packages were authorised by the European Commission under State aid rules.

(b) A "*Financial Stability Fund*" (FSF) was established with capital of €10 billion from the support mechanism of the Greek economy, with an aim to enhance the capital adequacy of banks, in the event they would be deemed viable but undercapitalized (in short to provide a safety net to the Greek banking system). So far, it has not been tapped.

5. The way forward

Under current conditions, Greek banks have three main objectives:

(a) The first is to maintain and, to the extent possible, improve their capital adequacy ratios,

(b) The second objective is to restore appropriate liquidity positions. Banks have been requested to submit and implement medium-term funding plans in order to reduce their reliance on Eurosystem refinancing operations over a medium-term horizon. Preliminary drafts and their adequacy will be assessed by the Bank of Greece and the ECB in close cooperation with the European Commission and the IMF,

(c) Finally, in the medium term, banks will have to comply fully with the European regulatory developments underway, such as:

- Basel III regulations, to be implemented in the European Union,
- the Review of the Deposit Guarantee Schemes Directive,
- the banking resolution proposals,
- the proposals on the taxation of the financial sector,
- the additional regulation of SIFIs (since several Greek banks will be considered to be systemically important), and
- the proposal for a Directive on credit agreements relating to residential property.

Banks operating in Greece are ready to address these challenges. Nevertheless, the major task for the Greek banking system is to fully support the national effort for the necessary adjustment of the economy.