Box A

Banking Systems in Greece, Portugal and Spain

Over 2010, concerns about sovereign debt in Greece, Portugal and Spain have been associated with a deterioration in sentiment towards banks in those countries. This Box outlines the structure of their banking systems, recent developments, and the financial sector support mechanisms in place.

In aggregate, the banking systems in Greece, Portugal and Spain share a similar mix of broad asset and liability categories, that is not very different from the euro area average. In these countries, monetary financial institutions' (MFIs) loans are around 70 per cent of assets, with similar splits between household and business loans (Table A1). The balance is in debt securities (around 15 to 20 per cent) and other assets, such as equity holdings and fixed assets. On the liability side, around 70 to 80 per cent of their funding is from deposits, with the remainder from wholesale markets (around 5 to 20 per cent) and other sources.

Banking industry structures show more variation across these countries. In Greece and Portugal the systems are quite concentrated; the largest five banks in each country account for around 70 per cent of banking system assets. In contrast, the banking system in Spain is more fragmented; the five largest institutions hold just over 40 per cent of banking system assets. Just under one half of banking system assets is held by commercial banks,

Table A1: Euro Area MFIs' Balance Sheet

Claims on and liabilities to euro area residents, per cent of total, as at July 2010[(a)]

	Greece	Portugal	Spain	Euro area
Assets				
Loans	74	66	70	65
Household	29	28	27	18
of which:				
Housing	*18*	*22*	*21*	*13*
Other personal	*12*	*5*	*7*	*5*
Business and other[(b)]	45	39	43	47
Securities other than equities	14	21	17	18
Government	10	5	5	6
Other	3	17	12	13
Other assets	12	12	13	16
Liabilities				
Deposits	82	68	70	60
Debt securities	4	18	13	18
Other	6	5	8	15
Equity	9	9	9	7

(a) The data cover consolidated transactions of MFIs' operations within the country
(b) Includes financial corporations and general government
Source: ECB

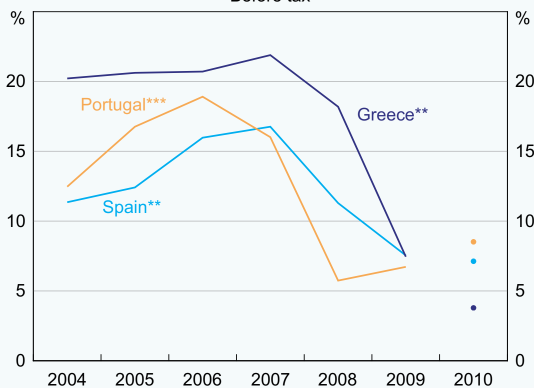
with over 40 cajas or savings banks making up most of the remainder. The largest banks in these countries often also have sizeable offshore operations; for example some of the large Greek banks are active in eastern Europe, and some of the Spanish banks have extensive operations in Latin America and North Atlantic countries.

Banking systems in Greece, Portugal and Spain were quite profitable in the years preceding the crisis. This was particularly the case in Greece, where return on equity of the five largest banks averaged around 20 per cent (Graph A1). The high profitability partly reflected strong economic outcomes; in the five years to 2007, Greek GDP and lending growth averaged around 4 per cent and 14 per cent respectively, compared to around 2 per cent and 7 per cent for the euro area (Graph A2). These strong outcomes partly reflected historically low borrowing rates after entry to the euro system lowered risk spreads.

In the recent period, however, profitability has fallen sharply as financial and macroeconomic conditions have deteriorated. Funding for banks and the economy generally has been negatively affected by the increase in sovereign risk spreads and declining confidence, with concerns including the direct effect on banks' holdings of sovereign debt, and the effect of current and future fiscal tightening on growth and future loan quality. Greek banks' asset quality is among the lowest in the euro area; the non-performing loan ratio stood at 8.2 per cent of total loans as at March 2010, well above the ratio of a year earlier. High unemployment and falling property prices have weighed on asset quality in Spain, bringing the non-performing loan ratio to 3.6 per cent in June 2010, though its rate of increase has slowed in the past six months. Among Portuguese banks, the non-performing loan ratio has increased from 2.7 per cent to 3 per cent in the six months to July 2010, around half a percentage point higher than a year earlier. Nonetheless, to date, banks in these countries have generally maintained profitability despite increased provisions for bad loans.

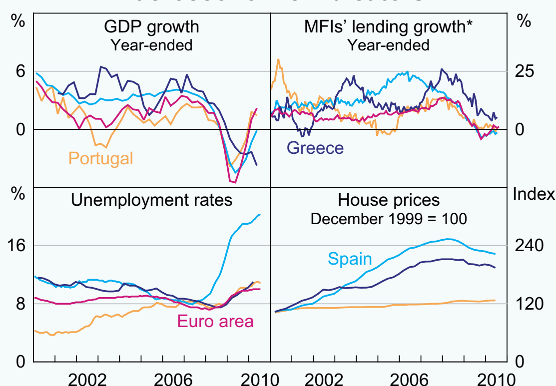
The results of the European bank stress test exercise, released in July, suggest that banking institutions in Spain and Greece were among those that would be most affected by a further deterioration in asset quality: of the seven institutions where capital fell below the 6 per cent Tier 1 capital ratio benchmark

Graph A1
Banks' Return on Equity*
Before tax



* Five largest Greek banks, and all Portuguese and Spanish MFIs
** 2010 data are annualised half year results
*** 2010 data are annualised March quarter results
Sources: Bank of Portugal; Bank of Spain; Bloomberg; banks' annual and interim results

Graph A2
Macroeconomic Indicators



* Securitisations brought onto Greek MFIs' balance sheets from June 2010 are excluded
Sources: BIS; ECB; Thomson Reuters

in the most difficult scenario, five were Spanish cajas and one a large Greek bank (the seventh was German). Twelve Spanish institutions, one Greek and one Portuguese bank were also among the 21 institutions that came relatively close to breaching the benchmark (with a Tier 1 capital ratio of between 6 and 7 per cent inclusive in the scenario). However, Spain had the largest number of banks in the stress test sample, reflecting both the structure of the banking system there and wider participation in the test than in other countries.

Various measures are in place to support both the capital and liquidity of banks in these countries. The Spanish Government has set up the Fund for Orderly Bank Restructuring which has €12 billion available to facilitate restructures and mergers and which can be increased, if necessary, to €99 billion. In addition, the Spanish authorities have relaxed ownership rules to encourage restructuring of the sector, and significant consolidation is already underway. Both Greece and Portugal have recapitalisation funds to enable banks to maintain a Tier 1 capital ratio of at least 8 per cent. Nine Greek banks have received €4 billion out of the €5 billion of funds that have been set aside by the Greek Government and a further €10 billion is available through the Hellenic Financial Stability Fund. No private Portuguese bank has required recapitalisation to date.

The ECB is also supporting banking systems through its monetary policy operations and liquidity facilities. Lending to domestic MFIs by central banks in Greece, Portugal and, to a lesser extent, Spain has increased sharply since 2008 (Graph A3). The European Financial Stability Facility, which became operational in early August, is another potential source of support. These arrangements have helped to support the ongoing operations of the banking systems in these countries.

Graph A3
ECB Monetary Policy Operations