

## THE GREEK BANKING SYSTEM

During the past two decades, the Greek banking and financial system has undergone momentous transformations, amounting to what the *Financial Times* once characterized as no less than a “silent revolution”. Let me sketch for you some of the features of this transformation.

To draw a brief historical background, the Greek banking system evolved in parallel with the modern Greek state. The country’s oldest and largest commercial bank, the National Bank (NBG), was established in 1841, and several banks followed in due course. In 1928, the Bank of Greece was established as the country’s central bank. During the booming 1920s many new commercial banks were established, only a part of which, however, survived the economic crisis of the 1930s.

In the postwar period, the Greek banking system was assigned the pivotal role of financing the country’s economic development and industrialization. As in many other European countries, a detailed framework of financial interventionism gradually developed, through

which banks were required to provide low-cost credit for industrial development. A complex system of quantitative and qualitative credit controls and banking restrictions was established, under the protective umbrella of the Bretton Woods system. For the particular circumstances of a developing country in the postwar era, these interventionist institutions may have had an overall positive role to play in assisting capital accumulation and investment. However, financial interventionism in Greece continued after the collapse of Bretton Woods. Over the 1970s and much of the 1980s, interventionism degenerated into high inflation and large deficits, keeping failed industries artificially alive, and channeling negative real interest-rate credit to various favored socioeconomic groups.

As with other European countries, the liberalization of the financial system in the 1980s was deemed indispensable for the overhaul of the entire economy. The deregulation of interest rates, allowing them to rise to market levels at the end of the 1980s, and the liberalization of the capital account by the first half of the 1990s, paved the way for macroeconomic stabilization. Liberalization ended a whole period of subsidized credit, which had led to an inefficient allocation of scarce capital as well as high inflation. It also

subjected Government to the discipline of international markets, from which it now had to raise financing.

As with many other instances of structural modernization, the European Union provided a crucial external force for financial liberalization. The single market program in the second half of the 1980s offered the first impetus in the arduous process of rendering Greek banks competitive to withstand international competition. The EMU convergence program in the 1990s provided a framework of discipline that allowed conditions of monetary stability to be restored, for the first time since 1973.

In this context, the financial sector has led the way in the transformation of the Greek economy and I think it can claim a large share of the progress achieved. Greek banks are now seen as comprising among the most dynamic part of the Greek economy.

Since the 1990s, Greek banks have taken advantage of liberalization to strengthen their portfolios and capitalization. The boom of the Greek capital market between 1997 and 1999 accelerated financial system development, further strengthening Greek banks, which expanded into a wide range of financial services.

Monetary stabilization since the second half of the 1990s made possible the rapid development of capital and money markets. Activities, such as asset management, insurance, mortgage lending and consumer credit have also experienced considerable growth and diversification. A wide range of products is now made available to Greek consumers who gradually develop new consumption patterns and new investment habits.

Greek banks have invested greatly in their organizational and technological modernization. Between 1990 and 2001, total gross fixed capital investment in the sector reached 2.5 billion euros. Banks expanded and modernized their distribution networks, which apart from the traditional branches and ATMs, now include alternative distribution channels such as the Internet and mobile telephony where the penetration rate is rising at a swift pace. In fact, labor productivity in the Greek banking sector during the past few years has grown faster than that in the Eurozone.

The withdrawal of government from the banking sector was a major development during the 1990s, taking both the form of statutory liberalization and privatization. Smaller and middle-sized state-controlled banks have

been sold to private investors, and the government's share of larger-sized banks has shrunk. Improved structures of corporate governance now allow much more effective shareholder control over the management of Greek banks, the largest of which, NBG, is also listed on the New York Stock Exchange, with all the high transparency requirements that this comprises.

After consecutive bank privatizations, a wave of mergers and acquisitions from the second half of the 1990s raised the degree of concentration in the Greek banking sector. The total number of commercial banks operating in Greece is now 39. This comprises 17 Greek and 22 foreign commercial banks, the number of which has been reduced in the past few years. Greek banks maintain a strong position in the domestic retail market with long-rooted ties to the clientele base, a position, which is difficult for foreign banks to challenge. Apart from the commercial banks operating in the Greek market, there are now also four investment banks (up from two in 1997) and two specialized financial institutions.

As a result of consolidation, the share of the five largest banks in total deposits now exceeds 79%, compared with 60% in 1997. In terms of total assets, the five largest

banks control an approximate 77%: the two largest banks, NBG and Alpha Bank, control 29% and 16% of total assets respectively, followed by EFG Eurobank, Commercial Bank, and Agricultural Bank, each in the area of 10% to 14%.

Despite the relatively higher degree of concentration compared with other EU countries, the five largest Greek banks put together correspond to only a middle-sized bank in the European Union in terms of total capitalization. This is indicative of the need for further consolidation in the Greek banking market; there are consistent efforts in that direction.

The increasing concentration in the Greek banking sector has evolved in parallel with steadily growing competition. As Greek banks seek to enlarge their market share, competition has intensified both in terms of the range and quality of provided services and in pricing policies as well.

After the year 2000, overall bank profits have been declining, following the downward trend of the Greek capital market, and the loss of a traditional source of commission income following the successful transition to the Euro. The profitability structure has improved

significantly as banks now increasingly rely on income from core banking instead of financial operations. Low interest rates have given a boost to private sector and retail lending. I should note that, despite the rapid growth of mortgage and consumer credit in the last few years, their total share of GDP remains notably lower than the Eurozone average. Total outstanding credit to the household sector corresponds to only 22% of GDP, compared with a 47% Eurozone average. Though corporate debt has grown steadily during the recent period, it is relatively low compared with EU benchmarks. Thus, there is significant potential ahead for the further growth of banking credit, which is of course not to discount potential associated risks.

It would be an omission not to refer to the significant expansion of Greek banks in the Balkans since the 1990s, enhancing corporate networks, business growth opportunities, and broader stability in the region. Between 1990 and 2002, Greek banks invested 550 million euros in the Balkans. The NBG, Alpha Bank, EFG Eurobank, Commercial Bank and the Bank of Piraeus now have established significant presence in Bulgaria, Romania, Albania, Serbia, and the Former Yugoslav Republic of

Macedonia, also by having acquired control of major credit institutions in these countries.

The Economic and Monetary Union and the higher degree of integration with international markets have raised the standards across the board in Greece. Size, scale of operations, investment in technology and containment of costs have become key factors for determining competitiveness. It is a natural instinct, of course, that nobody likes the inconvenience of change and readjustment. But it is now clear beyond doubt that these are the sine qua non's for Greek banking and corporate life, and that they will constitute permanent features for our future.