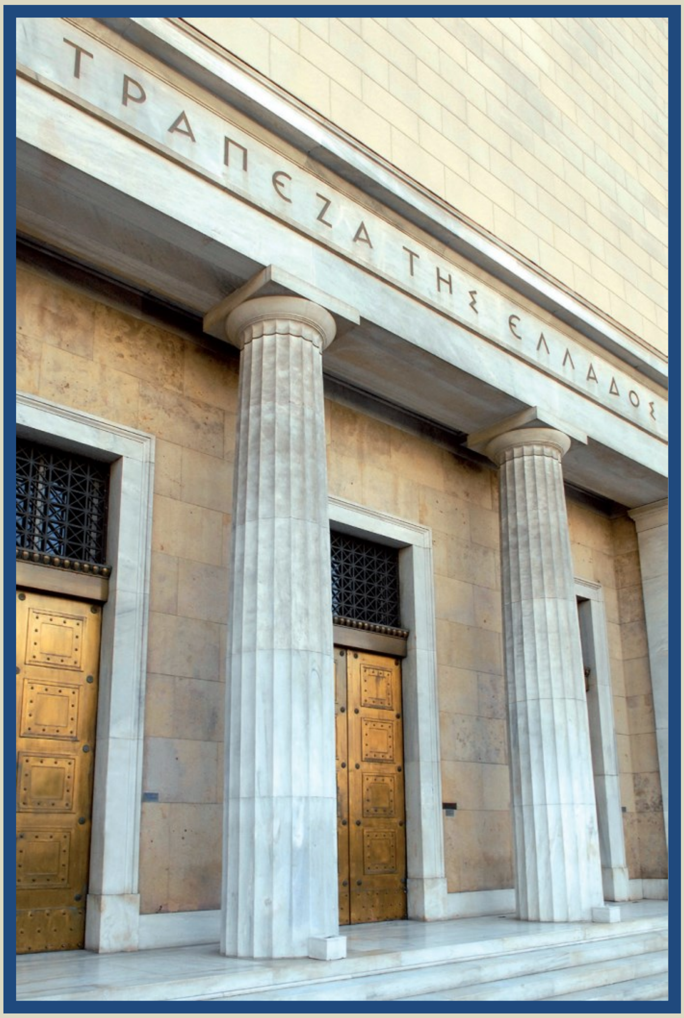
FINANCIAL STABILITY REVIEW

EXECUTIVE SUMMARY



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BANK OF GREECE
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I. EXECUTIVE SUMMARY

Risks to financial stability in Greece are mainly exogenous, due to heightened geopolitical tensions and mounting trade protectionism. Increased volatility in international money and capital markets – triggered by the announcement and partial enactment of tariffs by the US and, in retaliation, by some of its main trading partners – was short-lived and has not yet had any major direct impact on the functioning of the global financial system. However, the risk of an abrupt repricing of financial assets worldwide remains exceptionally high, and the recent market turmoil has once again brought to the fore the high interconnectedness of global markets and the speed of contagion. A potential resurgence of trade tensions would indirectly affect the Greek economy and the domestic banking sector, through a slowdown in global and European economic growth, reduced investment and credit expansion, and a deterioration in asset quality.

In 2024, the Greek economy grew at a satisfactory pace, well above the euro area average for the fourth consecutive year. The real gross domestic product (GDP) growth rate stood at 2.3% in 2024, materially higher than in the euro area. The main drivers of economic growth were private consumption, investment and services exports. More specifically, private consumption growth accelerated, on the back of rising households' real disposable income. Investment – especially in machinery – maintained its upward momentum in 2024. By contrast, the overall contribution of the external sector was negative, as exports declined somewhat, adversely affected by the deteriorating international environment, while imports of goods and services increased significantly. Lower government expenditure also weighed negatively on economic growth. On the fiscal front, tax revenue overperformed in 2024, with the general government primary balance turning out at a surplus of 4.8% of GDP, up from 2.0% in 2023, significantly exceeding the budgeted 2.5%, thanks, to a large extent, to the successful implementation of measures to counter tax evasion.

Banking sector fundamentals improved further in 2024, enhancing its resilience. In more detail, profitability and capital adequacy increased, banks' assets quality improved further and liquidity remained high. This was underpinned by domestic economic growth, credit expansion, successive upgrades of the sovereign and significant Greek banks' credit ratings, and progress in the overhauling of the LSI sector – most notably Attica Bank's merger with Pancreta Bank and their share capital increase, as well as a substantial reduction in the stock of non-performing loans (NPLs).

The liquidity of Greek banking groups improved further in 2024. This improvement was driven by deposit growth in Greece, the expansion of banks' international activities – notably in Cyprus – and the issuance of bank bonds. These factors more than offset the full repayment of the Targeted Longer Term Refinancing Operations (TLTRO III), which materially reduced Eurosystem funding (December 2024: EUR 2.6 billion, December 2023: EUR 14.3 billion). Liquidity ratios remain well above prudential requirements. More specifically, in December 2024 the Liquidity Coverage Ratio (LCR) stood at 218.3% and the Net Stable Funding Ratio (NSFR) at 138.5%. It should be noted that the recent market turmoil has so far not affected banks' liquidity and funding conditions, while the funding gap in foreign currencies is very small and manageable.

Banks' asset quality improved markedly, mainly thanks to NPL securitisation. In particular, 2024 saw a significant improvement in the quality of Greek banks' loan portfolios, with the stock of NPLs declining to EUR 6 billion – down by 39.8% compared to 2023 – mainly due to loan securitisations in the context of the Hellenic Asset Protection Scheme (HAPS – "Hercules"). The ratio of NPLs to total loans dropped significantly to 3.8% in December 2024 (from 6.7% in December 2023), the lowest level since Greece joined the euro area, further converging towards the average in the Banking Union (December 2024: 2.3%).

Greek banking groups' profitability improved significantly. In 2024, Greek banking groups posted profits after tax and discontinued operations amounting to EUR 4.4 billion, compared with profits of EUR 3.8 billion in 2023. This development was underpinned by an increase in net interest and fee income and a decline in loan-loss provisions, while profitability was adversely affected by higher operating costs. In addition, the expansion of international activities contributed significantly, driven primarily by the consolidation of Hellenic Bank (Cyprus) by Eurobank. Banking groups' return on assets (RoA) and return on equity (RoE) stood at 1.3% and 12.2% respectively.

The capital adequacy ratios of Greek banking groups also improved further. Prudential own funds were boosted mainly by internal capital generation and the issuance of capital instruments. In particular, the Common Equity Tier 1 (CET1) ratio on a consolidated basis increased to 15.9% in December 2024 and the Total Capital Ratio (TCR) to 19.7%, now standing at the same level as the average in the Banking Union (CET1: 15.9% and TCR: 20.0% in December 2024). Nonetheless, the quality of Greek banks' prudential own funds remains low: in December 2024, deferred tax credits (DTCs) amounted to EUR 12.2 billion, representing 38.6% of total prudential own funds (down from 44.2% in December 2023).

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In the current macroeconomic and financial environment, implementing an appropriate macroprudential policy to avoid the build-up of systemic risks and to enhance the resilience of the banking sector is all the more important. The Bank of Greece conducts a quarterly assessment of the intensity of cyclical systemic risks and the appropriateness of the Countercyclical Capital Buffer (CCyB) rate for Greece and sets or adjusts it, if necessary. The analysis of the indicators examined by the Bank of Greece confirms that overall, there is no excessive credit growth, however it points to emerging cyclical systemic risks in certain areas, such as credit to non-financial corporations, residential real estate prices and the current account. Furthermore, the banking sector's improved fundamentals and prudential ratios have created favourable conditions for building adequate macroprudential space to safeguard financial stability over the medium term. In this context, the Bank of Greece adopted a framework for a Positive Neutral Countercyclical Capital Buffer (PN CCyB), setting its target rate at 0.5%. In light of the above, the Bank of Greece set the countercyclical capital buffer rate for Greece at 0.25%, applicable from 1 October 2025.

In addition, the Bank of Greece identified Other Systemically Important Institutions (O-SIIs) in Greece for the year 2024, applying the relevant European Banking Authority (EBA) guidelines, and set the O-SII buffer rate for 2025 at 1.25% for Eurobank Ergasias Services and Holdings S.A. on a consolidated basis and at 1.00% for all other O-SIIs.

Finally, the Bank of Greece has enacted macroprudential borrower-based measures (BBMs) for loans and other credit to natural persons secured by residential real estate located in Greece, effective from 1 January 2025. In more detail, a cap was introduced on the loan-to-value ratio at origination (LTV-O) of 90% for first-time buyers and 80% for second and subsequent borrowers, as well as a cap on the debt service-to-income ratio at origination (DSTI-O) of 50% for first-time buyers and 40% for second and subsequent borrowers.

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The Greek insurance market maintained its capital adequacy in 2024, despite challenges associated with the international macroeconomic and financial environment and climate change. Following the mergers and acquisitions of recent years, insurance undertakings continue to actively adapt to the requirements of a rapidly changing environment, addressing both existing and emerging risks. To this end, they review their business models and adjust, where necessary, their pricing and investment policies, confirming the industry's flexibility and resilience over time.

The financial system infrastructures operated smoothly, while the use of electronic means of payment expanded further in 2024. The uninterrupted operation of these infrastructures, i.e. payment, clearing and settlement systems, contributed positively to the stability of the domestic financial system by ensuring the efficient processing of transactions. As for the use of electronic payment instruments and payment cards, transactions rose both in volume and value in 2024. At the same time, the enhancement of card payment security was reflected in a decrease in the fraud-to-transaction ratio both in volume and value terms.

Credit Servicing Firms (CSFs) play a significant role in private debt management in Greece. In December 2024, total exposures under management by CSFs amounted to EUR 87.4 billion, of which 82% referred to exposures serviced by CSFs on behalf of credit acquirers and the remaining 18% to exposures managed on behalf of credit and financial institutions. The portfolio comprised mainly NPLs (83%) and, to a lesser extent, performing exposures (17%).

The activities of Payment Institutions (PIs) and Electronic Money Institutions (EMIs) grew considerably in 2024. The total value of payment transactions carried out in 2024 by PIs stood at EUR 62.3 billion, up by 7% compared to 2023. In the same vein, the total annual value of payment transactions carried out by EMIs stood at EUR 34.4 billion, up by 28.2% year-on-year. These developments had a positive impact on the own funds and profitability of PIs and EMIs.

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The Greek economy is projected to continue growing in 2025 at a satisfactory rate, well above the euro area average. According to the Bank of Greece March 2025 projections, the growth rate of the Greek economy is set to remain at 2.3% in 2025 – well above the euro area average. Private consumption and investment will continue to be the key drivers of growth, while the contribution of the external sector is expected to be neutral. US tariffs on imported EU goods are expected to have a limited direct impact on the Greek economy. The small share of Greek exports to the US (around 5% of total exports in 2024) and the composition of goods' exports suggest only a muted effect on the country's external trade. At the same time, as regards shipping, the impact is anticipated to be limited for most key sectors, except for container transport, where a more pronounced effect is expected. However, US tariffs on EU exports should indirectly weigh on the Greek economy by dampening euro area growth and heighten uncertainty, dragging down exports and investment sentiment. In addition, the potential loss of the safe haven status of US assets could have adverse effects, although the full impact cannot be safely assessed. Conversely, higher capital flows into the EU on the back of trade tensions and a potential redirection of Chinese exports to the EU could act as a tailwind.

The outlook for the Greek banking sector remains favourable. The further upgrade of Greece's credit rating above the investment grade threshold, combined with the resilience of the economy, points to a positive outlook for the banking sector. Net interest income is expected to be affected by recent key interest rate cuts; however, this negative impact should be partly offset by stronger demand for new loans from both firms and households. Co-funded programmes of the National Strategic Reference Framework (NSRF 2021-2027), the Recovery and Resilience Facility (RRF) funds, as well as the financing tools of the European Investment Bank Group and the Hellenic Development Bank, will help in this direction. In addition, recent acquisitions of banks abroad and non-banking operations in Greece are expected to help banking groups diversify their income sources.

The nature of emerging global risks calls for vigilance. Ongoing geopolitical tensions and armed conflicts, as well as the rise of trade protectionism have reshaped the external environment. While the Greek banking sector is now much better placed to address the risks emerging at the current juncture, the nature of these risks differs markedly from conventional risks. This hampers their effective management and calls for the combined application of available microprudential and macroprudential policy tools so that the banking sector remains robust and on a growth trajectory.

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