

# Financial and Macroeconomic Drivers of Bank Profitability: Evidence From Greek Systemic Banks During 2009-2019

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## ABSTRACT

This paper aims at investigating the factors that affected the profitability of Greek systemic banks during the period 2009-2019. The authors initially review the findings of relevant international literature. Then, details of the methodology followed are provided and the variables that constitute the model are explained. Based on those, they investigate econometrically the factors that influenced banks' return on assets. The econometric analysis establishes that the ability of Greek systemic banks to generate profits through the use of their assets, during the period 2009-2019, was shaped under the influence of the debt crisis, which turned into a financial crisis, as well as specific financial and macroeconomic factors.

## KEYWORDS

Debt Crisis, Financial Analysis, Financial Ratios, Greek Systemic Banks, Profitability, ROA

## INTRODUCTION

The 2009-2019 decade has featured prominent changes in the economic landscape of Greece. Among others, the banking sector has undergone structural transformation both through the channel of EU-wide regulatory changes, as well as Greece-specific factors. We primarily cater about the latter set of factors in this paper, those pertaining to Greece. The performance of Greek banks could have not been left unaffected by a series of drastic developments in an economy which aimed to simultaneously tackle fiscal and structural problems, at a time when financing was scarce and the business environment fragile.

In parallel with the crisis unfolding in Greece, systemic banks were asked to continue their operation in an even more competitive EU banking market. Technological advances, new forms of finance, deregulation and increased interlinks shaped the morphology of the Greek banking sector, requiring banks to be open to new opportunities, but also ready to tackle any arising challenges that came along. At the same time, they had to support the resurgence of the Greek economy, distinguish profitable opportunities in a macroeconomic situation with asymmetric information and moral hazard, and continue credit provision to their clients. Besides, the issue of high non-performing loans featured prominently both in the academic and the policy debate.

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As the backbone connecting and fueling economic activity across various sectors of the economy, banks ought to be aware of their dependencies, as well as their links to other economic sectors. As the same time, as firms that not only maximise their own profits, but also constitute the input for other sectors to carry out investment, it is equally important that banks have a clear understanding of the driving factors of their financial performance.

International literature has explored the driving factors of bank profitability during the great recession. In Greece, similar studies are carried out either for previous time periods or in a broader frame, comprising various aspects of bank balance sheets. Yet, the study of Greek bank profitability during the 2009-2019 period remains relatively less studies from an economic perspective. This is the gap that the present paper endeavours to fill through an econometric analysis of key factors often cited in the theoretical and international relevant literature.

The rest of the paper is structured as follows. We first provide a literature review. Then, we present the methodological framework, which is followed by an analysis of the research results. The last two sections discuss the policy implications of findings and conclude.

## **LITERATURE REVIEW**

According to Katsimi and Moutos (2010), the situation that led to the Greek crisis mainly featured bureaucracy, vested interests and relations between private interests and the public sector, which contributed to the mismanagement of public resources, tax evasion and the deterioration of the quality of public services. At the macroeconomic level, governments proved to have been unable to reduce the fiscal deficit. On the side of the Greek statistical authorities, there may have been not only misrepresentation of data, but also significant errors on the side of European partners. The latter revealed the weakness or reluctance in their reactions to the visible signs of Greek failure, such as the chronically large current account deficits. In this regard, Kotios and Roukanas (2013) analysed the Greek financial crisis in light of the functional responsibilities and inadequacies of eurozone governance. Some of the dimensions of the management of the Greek crisis are the weaknesses of the European decision-making mechanism and European leadership, the economic nationalism displayed by some member states, the risks of contagion of the crisis to the Eurozone and the overreactions of markets and credit rating agencies.

### **Causes of the Greek Fiscal Crisis**

Kutter (2014) points out that the high level of public debt in Greece rendered the implementation of austerity measures necessary, while the contagion dynamics of the Greek crisis justify the implementation of similar measures in other European countries. However, the Greek crisis has revealed the systemic flaws of EMU, highlighting the need for deeper economic integration. Provopoulos (2014), claims that the causes of the Greek crisis were the large external and fiscal imbalances. The growing deficit was the result of reduced competitiveness and the expansion of the public sector. Unlike what happened in other countries, the initial crisis in Greece led to a banking crisis. The country made significant progress in addressing the imbalances and the Bank of Greece managed to restructure the banking system. The resulting conditions have improved the outlook for the Greek economy, as assessed by financial markets. Finally, Gourinchas, Philippon and Vayanos (2017) concluded that the depth of the crisis related to the size of the macroeconomic imbalances, while the sudden interruption of capital flows in the economy also played an important role.

The Greek crisis highlighted the failure of the asymmetric institutional framework of EMU, which was due to its exclusive reliance on internal devaluation, economic fragmentation and lack of counter-cyclical policies, and which led to external imbalances. The Greek problem has pushed the Eurozone in the direction of developing strong policies and institutions and avoiding an existential challenge. Yet, it is argued that the EMU is stronger today, but not necessarily adequately equipped to deal with the next major crisis (Pagoulatos, 2020).

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