The Bank of Greece proposes a national “bad bank”

BY ALEXANDER NYE

On July 16, the Bank of Greece (BOG) proposed a public asset management company (AMC) to buy non-performing loans (NPLs) from banks using public funds.

Yannis Stournaras, governor of the BOG, argues that an AMC could help banks clean up their balance sheets and allow them to raise capital.

Unlike the AMCs that governments created during the Global Financial Crisis (GFC) of 2007-09, a Greek AMC would not be able to subsidize banks by acquiring NPLs above market prices. Europe’s Bank Recovery and Resolution Directive (BRRD), passed in 2014, now prohibits European government from providing most forms of the vast majority of state aid to banks outside of the resolution process, including through AMCs. This means the AMC’s purchase of the NPLs would likely subject participating banks to large haircuts, eating into their capital.

The BOG has not put forward a detailed description of the bad bank proposal. In its July 2020 Financial Stability Report (FSR), the BOG said that a new AMC would not fundamentally change the country’s existing banking infrastructure. Third parties would be brought in to help the bad bank, though this could mean anything from contracting with private asset managers to having private-sector entities take an equity stake in the AMC (as they did in Ireland during the GFC).

In its FSR, the BOG also suggested the AMC could have a loss-sharing element; participating banks would solely bear any losses. However, that does not seem to be the case. The Greek proposal would have the banks endure those losses, but would only do so untreaching their minimum capital ratios. If a bank’s capital ratio fell below the minimum allowed level, the Greek taxpayers may help cover the losses. If this is the case, the FSR is contradicting itself. The BOG wrote that this element of the plan was to keep the government from having to put any of the participating banks into resolution.

Greece does have other tools for dealing with NPLs. One is the Hellenic Asset Protection Scheme, better known as “Hercules,” a program approved in late 2019 by the Greek government and the European Commission. The program removes €30 billion in NPLs from bank balance sheets and places it in SPVs owned by the Greek government, which then securitize the debt into tranches and sell it. The government added up to €12 billion in guarantees to the senior tranche as a way to make them more attractive to investors.

However, Stouarans has said that creating a bad bank is the only way to get rid of NPLs quickly. He supported a proposal to create a European AMC or national AMC, explaining either one was acceptable so long as they happened quickly. The European Union spent part of April discussing the prospect of a bad bank, but the idea faced resistance within the European Commission.