

Greek Banks

Initiating coverage on Alpha Bank and Piraeus: top-down concerns, bottom-up opportunities

Greek Banks: Summary of ratings and target prices (EUR)

	Ticker	Price	Target price	Rating	Upside
ACB	ACBr.AT	0.100	0.137	Buy	37.0%
BOP	BOPr.AT	0.060	0.061	Hold	1.7%

Source: Thomson Reuters Datastream, HSBC estimates
Pricing as at close 6 November 2015

13 November 2015

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- ▶ **Profitability should improve markedly for Greek banks as funding, activity and provision levels normalise**
- ▶ **Top-down concerns and potential stock overhang warrant some caution**
- ▶ **Initiate coverage: Alpha (Buy) is our top pick; for Piraeus (Hold), the upcoming recapitalisation looks attractive**

You've come a long way

Greek banks have had a challenging year, facing fears of a Grexit, political uncertainty, capital flight and subsequently mandatory bank holidays, capital controls and a capital injection. Funding, activity and asset quality headwinds have mounted. Crisis, however, has fundamentally transformed the sector, leaving it more concentrated and cost efficient.

We initiate coverage on Alpha Bank and Piraeus as visibility has improved substantially. There are still numerous unknowns given the impending recapitalisation, but pressures appear to have peaked. Greek banks should benefit significantly from a normalisation of interbank funding, an activity-led improvement in fee margins, further rationalisation of their cost base and a normalisation of asset quality. Returns should reach above cost of equity levels by 2018e.

Greece has become accustomed to turbulence, however, and we therefore incorporate some impact on the investment case for the higher potential for negative surprises given the relatively fragile nature of the Greek post crisis recovery. In spite of our conservative stance, we still see value.

Alpha Bank is our preferred play – we believe it will benefit the most from market dynamics, while its business mix is more defensive. As a result, we expect Alpha Bank to see the biggest improvement in ROA and reach a 13.0% ROTE in 2018e post excess capital. We initiate coverage with a Buy rating and a EUR0.137 target price.

Headwinds from corporate loan pricing and asset quality for Piraeus imply less upside for existing shareholders based on our estimates. But we think the upcoming recapitalisation also looks attractive for Piraeus (Hold, EUR0.061).

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Investment summary

- ▶ Greek banks should see a marked improvement in profitability and reach excess capital positions in 2018e, we believe
- ▶ However, top-down concerns lead us to take a conservative stance on valuation
- ▶ We see upside in Alpha Bank (Buy, TP EUR0.137); the upcoming recapitalisation also looks attractive for Piraeus (Hold, EUR0.061), but our estimates imply less upside

Following an unprecedented period of stress for the Greek economy, we think the banking system has ample room to improve profitability. Given that Greek banks are unlikely to face a normalised environment for a number of years, we look through to our 2018 estimates. On that basis and adjusted for any excess capital, we think Alpha Bank will be able to post above cost of equity ROTEs, with Piraeus Bank somewhat lagging due to a relatively greater drag from the domestic corporate portfolio, both in terms of loan pricing and asset quality.

The upcoming recapitalisation that aims to fill capital needs from the recent ECB stress test means that there are numerous known unknowns. At the same time, given the relatively fragile nature of the Greek post crisis recovery, top-down considerations warrant some caution. For the recapitalisation process, we assume that all share issuance is made at a 30% discount to the closing price on 6 November and that:

- ▶ Alpha is able to cover its full capital requirements through book building and the Liability Management Exercise (LME), with no need to resort to state funds.
- ▶ Piraeus is able to cover up to the AQR and baseline scenario capital needs through the book building, LME and EUR200m of asset sales. Any remaining capital needs are then met with state funds.

Additionally, we incorporate a common 10% valuation discount to reflect near-term uncertainties relating to the successful conclusion of the first programme review and the reestablishment of the ECB waiver on Greek collateral as well as a 300bp higher cost of equity than European peers (half of the average GGBs spread to European peer countries) to incorporate longer-term top-down concerns on the macro and political front. We also adjust our valuation for bank-specific stock overhang that would arise from (a) state ownership and (b) stock ownership from holders of debt that either participated in the LMEs or were converted to equity through burden-sharing. In each case we use a negative multiplier of ownership and adjust our valuation accordingly. Last, our target capital ratios reflect: (1) systemic risk, given the level of concentration in the sector; (2) impending changes in regulatory requirements; and (3) a prudential buffer for future stress tests.

Greek Banks: Summary of main valuation assumptions (EURm)

	ACB	BOP
Capital Need from AQR/stress test:	2,743	4,933
Assumed actions:		
Book building	1,658	1,420
LME	1,086	593
Burden sharing	0	0
Public sector shares	0	680
share issuance discount to closing price:	30%	30%
Public sector CoCos	0	2,040
Other actions	0	200
Ownership structure:		
Public sector	16%	29%
Private sector	84%	71%
o/w previously debt holders	29%	20%
Overhang multipliers:		
state ownership	0.30	0.30
debt investor ownership	0.05	0.05
Ownership structure discount	6%	10%
Common discount	10%	10%
Base Year	2018	2018
Long-term growth rate	1%	1%
Cost of Equity	12%	12%
Capital requirement	12.3%	12.5%
o/w Basel III minimum	7.0%	7.0%
o/w Supervisory buffer	2.5%	2.5%
o/w Management buffer	2.8%	3.0%

Source: HSBC estimates

Based on the above, we think there is still significant upside in Alpha Bank shares and initiate coverage with a Buy rating and a EUR0.137 target price. The upcoming recapitalisation also looks attractive for Piraeus, but our estimates imply there is little upside for existing shareholders. We initiate with a Hold rating and a EUR0.061 target price.

A marked improvement in profitability...

Despite the high level of concentration in the market and the resulting improvement in cost efficiency, the crisis has significantly hampered Greek bank profitability. In 2015 alone, Greek banks have had to face fears of a Grexit, political uncertainty, capital flight and subsequently mandatory bank holidays, capital controls and a capital injection. Funding and asset quality headwinds as well as low levels of economic activity have reduced returns on assets (ROA) significantly. From here, we believe Greeks banks will see a steady and significant improvement in ROA over the next few years, from the negative levels seen in the crisis years to an ROA in excess of 100bp by 2018e based on the following levers:

- ▶ A return of domestic deposits and the reinstatement of the ECB's waiver on Greek government bonds should help to normalise interbank funding costs. Falling time deposit costs should also provide room for re-pricing. These should be somewhat offset by continuing deleveraging and, eventually, pricing pressure on loans.
- ▶ A substantial improvement in fee margins given the very low starting base. By 2018e, we expect Alpha Bank and Piraeus to cover close to half the distance between Q3 2015 levels and 2008, with 2008 reflecting healthy levels of activity and near peak system level fees.

- ▶ We believe there is also further room to reduce costs by optimising the domestic network.
- ▶ Asset quality normalisation will undoubtedly be the biggest swing factor and early signs appear to be positive.

This shift would leave Greek banks' ROA well below our emerging market banks coverage universe but somewhat above our European banks coverage universe. For the two banks, the normalisation of provisions is by far the biggest swing factor in our estimates followed by NII (c28bp of ROA on average) and other revenue (c15bp).

It is important to note that, on our 2018 estimates, Greek banks' average ROA would be at par with 2008 levels of 1.05% on better cost performance (worth c52bp on average) and a more benign asset quality environment (c17bp) as we expect NII (-23bp) and other revenue (-29bp) to remain well below 2008 levels due to lower interest rate levels and lower levels of economic activity.

...and excess capital in 2018e

We think that Greek banks will be able to meet the capital needs that arose from the recent AQR/stress test process through: (1) asset sales and other actions; (2) an increase in share capital from Liability Management Exercises (LMEs), private sector book-building, private or state burden sharing as well as state participation, all at the same price; (3) capital gains on the LMEs; and (4) state-funded CoCos. Ownership and recapitalisation should change markedly as a result. On a simple measure of leverage (Assets / Equity), Greek banks would stand at relatively low levels, with the average of the two recapitalised banks at c9x as of 2015e.

Longer term, we also believe that capital requirements should ease. In theory, if the adverse scenario of the ECB's recent stress test does not materialise, that additional capital would no longer be necessary. In practice, however, we think Greek banks should target capital ratios above those of their European peers due to the sensitivity of their capital positions to changes in the value of their impaired assets portfolios, whether actual or stress test scenario related.

Despite our relatively conservative take on both capital accumulation (returns) and capital requirements, our estimates still suggest that Alpha Bank and Piraeus would have excess capital as of 2018e post repayment of non-equity state-aid instruments. In comparable terms, excess capital against our target capital ratios of c12.4% would be highest for Piraeus, with Alpha Bank at somewhat lower levels.

But top-down concerns suggest some caution is warranted

Although the recent turmoil is expected to put another dent in the Greek economy's recovery, the outlook longer term is positive. Having already lost over a quarter of the country's GDP in real terms, the economy appears to have bottomed out and, after a forecast contraction in H2 2015, quarterly growth rates should start to stabilise. Overall, HSBC economists expect GDP to contract significantly in Q3, and fall by 1.3% in 2015 as a whole. Thereafter, we expect Greece's GDP to contract by another 1.2% in 2016, even if quarterly growth rates should return to positive ground, and then grow by 2.4% in 2017.

With an overwhelming majority of the electorate and MPs supporting the third adjustment programme, there is reason to believe that stability and implementation have finally arrived for Greece. However, the country has become accustomed to turbulence and we thus think it appropriate to incorporate some

probability of a more negative outcome in the investment case for the higher potential for negative surprises given the relatively fragile nature of the Greek post crisis recovery. We include:

- ▶ A 300bp higher cost of equity than European peers (half of the average GGBs spread to European peer countries) to incorporate longer-term top-down concerns on the macro and political front.
- ▶ A common 10% discount to reflect near-term uncertainties relating to the successful conclusion of the first programme review and the re-establishment of the ECB waiver on Greek collateral.
- ▶ A 0.30x multiplier on % state ownership given that the Hellenic Financial Stability Fund (HFSF) would eventually need to sell down its position longer term and a 0.05x multiplier on % debt investor ownership as a discount as some would not have a mandate that allows them to hold equity in order to reflect stock overhang.

Alpha Bank is our preferred play

Alpha Bank is poised to benefit the most from a normalisation in interbank funding. Given its lower exposure to domestic small corporates, we also think that loan pricing and asset quality headwinds are likely to be relatively less. Benefits from fees should be in line with the market, while we think there is still room to reduce the domestic footprint. Asset quality trends have traditionally been stronger than peers, providing us with more confidence on the outlook for provisions and the rundown of the doubtful loans portfolio, albeit uncertainty remains high. As a result, we expect Alpha Bank to see the biggest improvement in ROA, with 2018e ROA jumping to 1.30% from -0.47% in 2014.

Near term, we see headwinds from stock overhang, as both state and debt-investor ownership would be significant based on our recapitalisation assumptions. But the bank should remain in private hands, with over 50% private-sector ownership. Coupled with an above cost of equity 13.0% ROTE in 2018e post excess capital, we see upside for existing shares. We initiate coverage with a Buy rating and a EUR0.137 target price.

The upcoming recapitalisation also looks attractive for Piraeus

Piraeus should also have significant room to improve profitability from a funding and cost perspective, we believe. However, we think that headwinds from corporate loan pricing and asset quality will eventually bite. We also see Piraeus as the most leveraged play on recovery values for the banks' doubtful portfolios. With 71% of ownership in private hands, based on our assumptions, Piraeus will also suffer the least from stock overhang. However, we see little upside left for existing shares. We initiate coverage with a Hold rating and a EUR0.061 target price. However, we think the upcoming recapitalisation should look attractive given our assumed 30% discount in the issuance.

Ample scope to improve profits

- ▶ Asset quality will be the driving force behind the expected improvement in profitability for Greek banks, we think
- ▶ We also see significant upside from revenues and costs, but prefer to err on the side of caution given current uncertainties
- ▶ ROA should improve markedly over the next few years, bringing Greek banks above European peers but below emerging markets

A new beginning, but not a clean slate

The Greek banking system has transformed profoundly over the course of the Greek crisis. From 2009 to 2014, over 30% of the workforce has left the industry, 34% of branches have been closed and foreign ownership of assets has nearly disappeared. Following consolidation¹, the top 4 domestic players in the market command a c90% combined share, with the remainder effectively split between one smaller institution and a group of co-operative banks. The Herfindahl-Hirschman Index has jumped from 12% to 22% over 5 years and Greece is now one of the most concentrated banking markets in Europe. Based on a recent study by the ECB (Report on financial structures, October 2015), as of 2014 the share of total assets of the five largest credit institutions was highest in Greece among EU countries, while Greece also had the third highest HH index behind Finland (33%) and Estonia (24%).

Sector trends

	Employees	Branches	HH Index*	Top 5 market share	Foreign owned assets (EURm)	Total assets (EURm)	Domestic credit (EURm)	Top 4 average NPL ratio
2009	65,682	4,117	12%	69%	103,422	490,831	312,673	6%
2014	45,654	2,711	22%	94%	9,845	397,027	247,887	33%
Change	-30%	-34%	10%	25%	-90%	-19%	-21%	27%

*The Herfindahl-Hirschman Index measures concentration in a market. It is defined as the sum of squares of market shares and can range from 0 (large number of very small firms) to 1 (monopoly), presented here as a percentage.
Source: Bank of Greece, HSBC calculations

However, during the same period, domestic credit institutions have seen their asset base shrink by c19%, credit to the domestic economy has shrunk by c21% and the average (group-level) NPL ratio for the top 4 banking institutions has jumped from 6% to 33%, with provisions effectively wiping out all pre-provision profits. As of 2014, deposit balances were down 29% from 2009 levels, with Greek banks thus having to

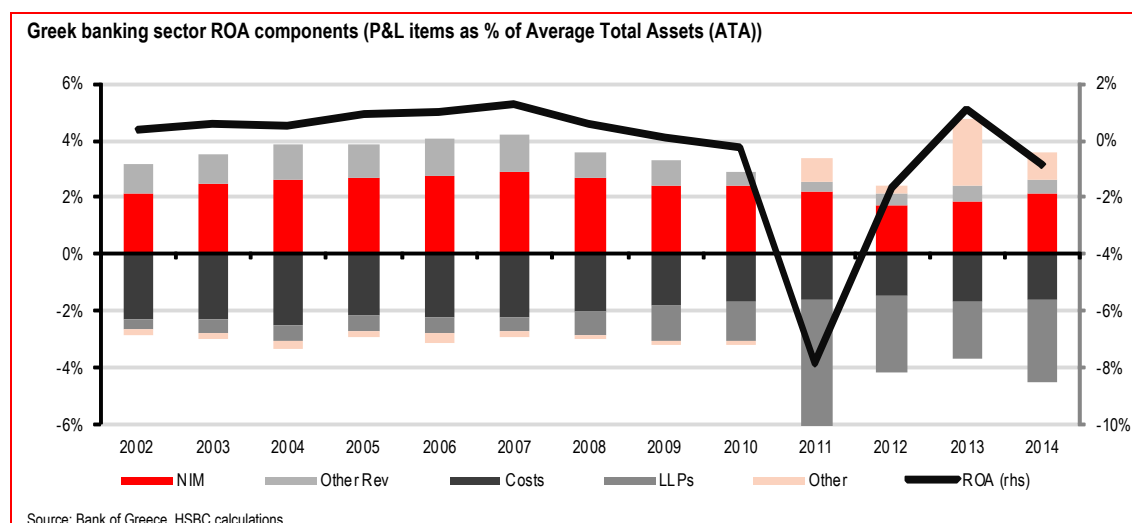
¹ Main acquisitions include: Alpha Bank (Emporiki Bank, Citi Greece), Piraeus (ATEbank, Geniki, Greek subsidiaries of Bank of Cyprus, Hellenic Bank, Cyprus Popular Bank, Millennium BCP, Panellinia Bank).

deal with the consequences, either in the form of higher retail funding costs or emergency central bank funding, putting pressure on the top line. The recent turmoil during 2015 has exacerbated trends; the total deposit outflow from 2009 levels has reached c48.8% (September data) and NPL ratios have increased further following the latest Asset Quality Review (AQR) from the ECB.

Things could hardly be worse. The question thus appears to be if profitability can only get better for Greek banks from here and, if so, to what extent. At its peak, based on central bank data, the banking sector was able to post high teen ROEs on high revenue margins (c4%), despite high cost and risk intensity (cost-income ratios >50%, cost of risk c95bp, leverage c14x). However, given the vast sector restructuring and fundamental changes in the regulatory environment, it is questionable whether history can serve as a guide.

- ▶ In this section, we examine the bottom-up opportunities that exist for Greek banks' profits, assuming that a mild recovery occurs as planned and widely expected by the Greek government, the European Commission, the ECB and the IMF and in line with our economists' forecasts. This forms our base case for profitability going forward and can in many ways be thought of as an "if all goes according to plan" scenario for ROA. We should note that we base our analysis on conservative assumptions so this should not be viewed as a best-case or blue-sky scenario.
- ▶ Given the intricacies of the latest recapitalisation, we believe more commentary is warranted; hence we address capital (and leverage) in the next section.
- ▶ Top-down concerns and consequences for the investment case (if things don't go according to plan) are then explored in the following section.

Based on Bank of Greece data (see graph below), by far the biggest driver of the change in ROA for Greek banks over the past few years has been the pick-up in provisions. As of 2014, the deterioration in provisions versus an average of the 2002-2007 period removed some 237bp from ROA. Admittedly, 2014 provisions were also affected by the ECB's Asset Quality Review (AQR) and banks have had a similar experience so far in 2015 given that the AQR process was repeated. We believe the deterioration in asset quality has been very much outside the banks' control and due to the adverse and persistent deterioration

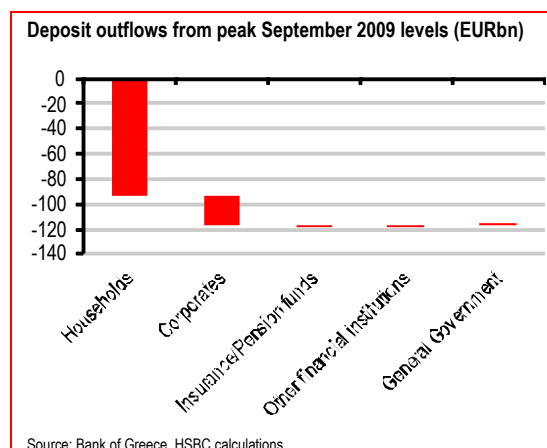
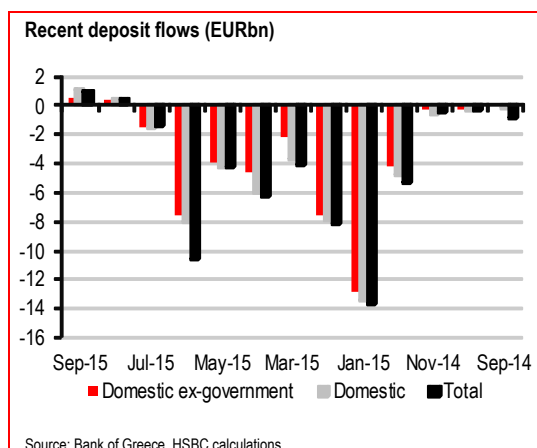


in the Greek economy. Fee income has also seen a significant deterioration on the back of lower activity (-71bp on ROA 2014 vs an average of the 2002-2007 period). For their part, banks have significantly improved their cost efficiency, with the improvement contributing c66bp to the change in 2014 ROA versus the 2002-2007 period average. Some other elements, which are relatively one-off in nature (creation of badwill, tax gains), have also contributed positively to ROA.

We think little has changed during 2015, with the challenging environment being prolonged rather than improving as previously anticipated. Peak to trough (2007-2012) though, the second biggest deterioration (after asset quality) had been in net interest margins (NIM). The 2012 to 2014 period saw an improvement as liquidity improved for the system. But the significant deterioration during 2015 has made net interest income (NII) possibly one of the most important drivers going forward.

Funding cost normalisation to drive NII higher

With deposits down 48.8% from peak levels as of September 2015, including cEUR44bn of cumulative outflows of domestic non-government deposits over the past 12 months due to the recent turmoil, it is not surprising that Greek banks have turned to expensive central bank assistance for liquidity. The imposition of capital controls during the summer halted the outflow, but the likelihood of deposits flowing back into the banks is hard to assess. We do, however, think there are reasons to be optimistic, as we discuss below.



Double-digit NII impact from interbank funding cost normalisation

Most of the deposit outflow over the past 12 months appears not to have been reinvested elsewhere. As evidenced by central bank data, currency in circulation has increased by cEUR20bn to cEUR50bn during the turmoil. Piraeus estimates suggest that 80% of private sector deposit outflows up to June 2015 remained in the country in cash, either as bank notes or in the form of short-term investments. That would suggest that deposits have not necessarily left the country or been converted to mutual funds, making an eventual return more likely. Withdrawals were arguably caused by fears of redenomination on a potential Grexit as well as doubts over the health of the banking system. The recapitalisation process as well as the gradual removal of capital controls should alleviate concerns on the latter, while, with a programme already in place, fears of a potential Grexit should increasingly subside.

On the return of deposits, Greek banks would most likely choose to reduce their dependence on expensive ELA funding. Banks pay 1.55% for the cash they receive from the ELA, but the most expensive form of ELA is backed by issues guaranteed by the Greek state (Pillar II bonds) where banks pay an additional

1.15% on the nominal value of the bonds they post as collateral that are then subject to significant haircuts. The effective cost thus for the most expensive portion of ELA funding can be above 3.5%.

In order to make an assessment of the potential impact, we assume that 50% of domestic time deposits that have left the banks over the past 12 months as well as 100% of all other domestic deposits return over the next five quarters, so that banks see the full benefit in 2017. We also include all the funds from the (impending) capital increases. Banks do not treat Pillar II costs homogeneously from a P&L perspective but, although our P&L estimates are adjusted for this difference, below we present the total impact on a like-for-like basis. The impact would be 9% of annualised Q3 NII for Alpha and 15% for Piraeus.

Gain from ELA reduction assuming 50% of time deposits and 100% of other domestic deposits that have left over the past 12 months return (EURm)

	ACB	BOP
ELA reduction from deposit return & capital increase	7,081	10,937
NII gain from ELA reduction	110	170
% of Q3 2015 annualised NII	6%	9%
Gain from Pillar II guarantee reduction	68	120
Total % of Q3 2015 annualised NII	9%	15%

Source: HSBC estimates

A successful conclusion of the first review of the new adjustment programme for Greece could also allow the ECB to reinstate the waiver for Greek government bonds, allowing banks to switch their central bank dependence from expensive ELA funding to the ECB's main facilities. In practice, however, in a scenario where ECB liquidity is reinstated, we think banks would also regain access to the interbank market, as was the case in 2014, and, despite its higher cost, banks would opt to reduce their structural dependence on the ECB to Q3 2014 levels in line with their previous strategy. If we assume a repo market cost of 50bp, the total impact including any additional reduction in Pillar II costs would be 9% for Alpha and 4% for Piraeus.

Impact for switching central bank funding from ELA to repo/ECB (EURm)

	ACB	BOP
NII gain from switching ELA to repo	159	80
NII gain from switching ELA to ECB	18	0
Total gain from switch in Interbank	176	80
% of Q3 2015 annualised NII	9%	4%
Gain from Pillar II guarantee reduction	0	0
Total % of Q3 2015 annualised NII	9%	4%

Source: HSBC estimates

Even if all of the above were to materialise, dependence on the interbank market would remain high. But the structural dependence on the ECB (excluding funding for the EFSF bonds) would fall significantly as can be seen in the next table.

Greek banks' dependence on the interbank market following our assumed deposit influx

	ACB	BOP
Total % of Assets	30%	29%
o/w repo	21%	19%
o/w ECB	9%	10%
o/w ECB ex-EFSF bonds	3%	0%

Source: HSBC estimates

The total impact from a normalisation in interbank funding would be significant. Even once we include a cost for the influx of deposits (assumed to be 0.8% here), banks would see a double-digit increase in NII from Q3 levels. The impact on bottom-line profitability would also be significant, with the contribution to ROA improvement at 32bp for Alpha and 25bp for Piraeus.

Total estimated impact from normalisation in interbank funding after influx of deposits (EURm)		
	ACB	BOP
Total NII Gain	237	184
% of Q3 2015 annualised NII	12%	10%
Total gain from Pillar II guarantee reduction	68	120
Total % of Q3 2015 annualised NII	16%	16%
ROA contribution (bp)	32	25

Source: HSBC estimates

Ample room to re-price deposits

Rates on time deposits have been steadily falling for a number of years in Greece. The process was somewhat halted but not reversed during the first half of 2015. The imposition of capital controls caused a further significant step down in deposit rates, with rates on new time deposits of up to 1 year dropping 50bp in July alone, with a further 12bp drop in August, according to central bank data. New production rates as of the end of September stood at 1.18%, suggesting there is still room for improvement if compared with rates in other euro-area countries.

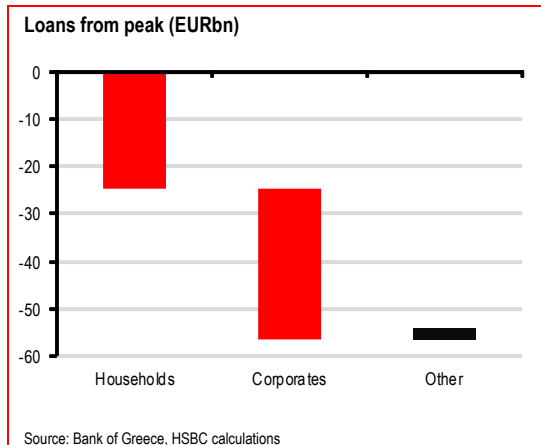
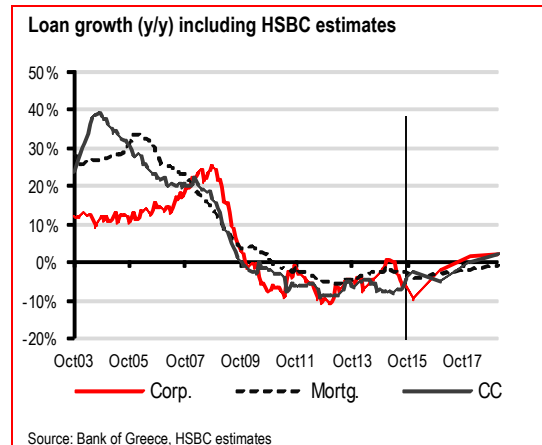
However, given the relative volatility that the Greek deposit market has witnessed in recent years, we think it is unlikely that deposit rates will reach levels seen in, for example, Spain (c0.4%). The impact on NII would still be significant. Assuming the whole book of domestic time deposits is re-priced to 0.8% would increase NII by 3% for Alpha and 5% for Piraeus and contribute 6bp and 10bp to ROA respectively, with every additional 10bp of reduction in the cost of time deposits adding a further 1%.

Impact from deposit re-pricing (EURm)		
	ACB	BOP
Total gain on stock	60	97
% of Q3 2015 annualised NII	3%	5%
Every 10bp more	17	21
% of Q3 2015 annualised NII	0.9%	1.1%
ROA contribution (bp)	6	10

Source: HSBC estimates

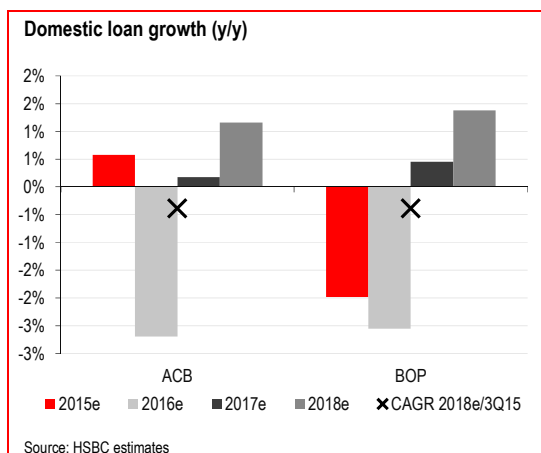
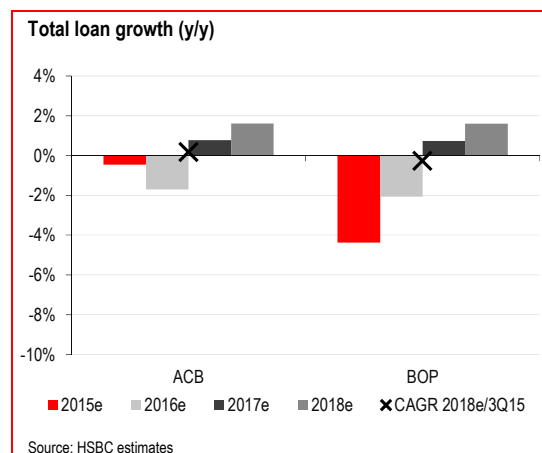
Loan pricing pressure unlikely for now but deleveraging pressure still mounting

The Greek banking system has shrunk its loan book significantly during the crisis; domestic loan balances have fallen by cEUR54bn or 21% from peak levels, with corporates down cEUR32bn, mortgages down cEUR13bn and other household lending down cEUR11bn. New production trends offer little to suggest optimism is warranted, with current levels at their lowest level on available data since 2002.

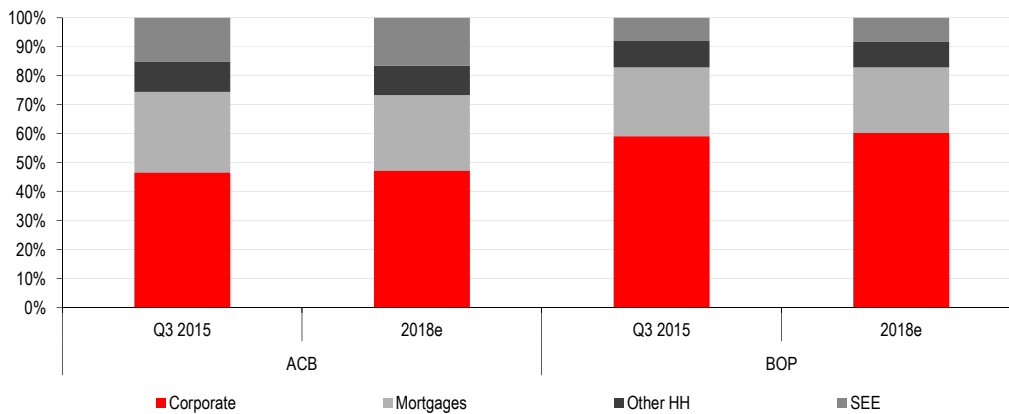


Data from the Bank of Greece, however, suggests that, with GDP growth returning in late 2014, negative loan flows (adjusted for write-offs, exchange rate valuations and reclassifications) became minimal in early 2015. In fact, some months saw positive flows for Corporates and Consumer Credit. This suggests that, if the Greek economy begins to recover, loan growth could recover rapidly given the prolonged period of deleverage.

Given that 2015 and 2016 are widely expected to be another two years of recession, our forecasts incorporate system level loan growth recovering only in 2018, with growth in corporates already in 2016e but declines in mortgages even in 2018e, as can be seen in the previous right-hand chart.



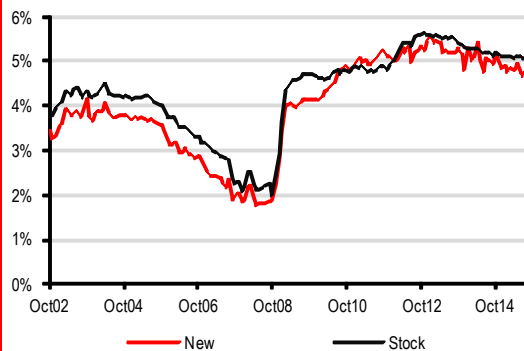
Loan book mix by bank



Source: HSBC estimates

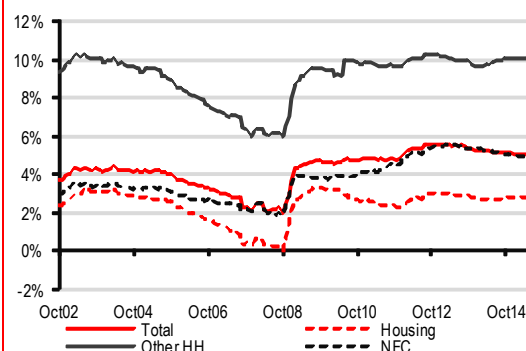
We expect no major market share shifts among banks for their domestic loan books, with individual domestic loan growth estimates reflecting the loan book mix between corporates, mortgages and other household lending and total loan growth reflecting their relative exposure to higher-growth, foreign operations.

Spreads on loans



Source: Bank of Greece, HSBC estimates

Stock spreads on loans



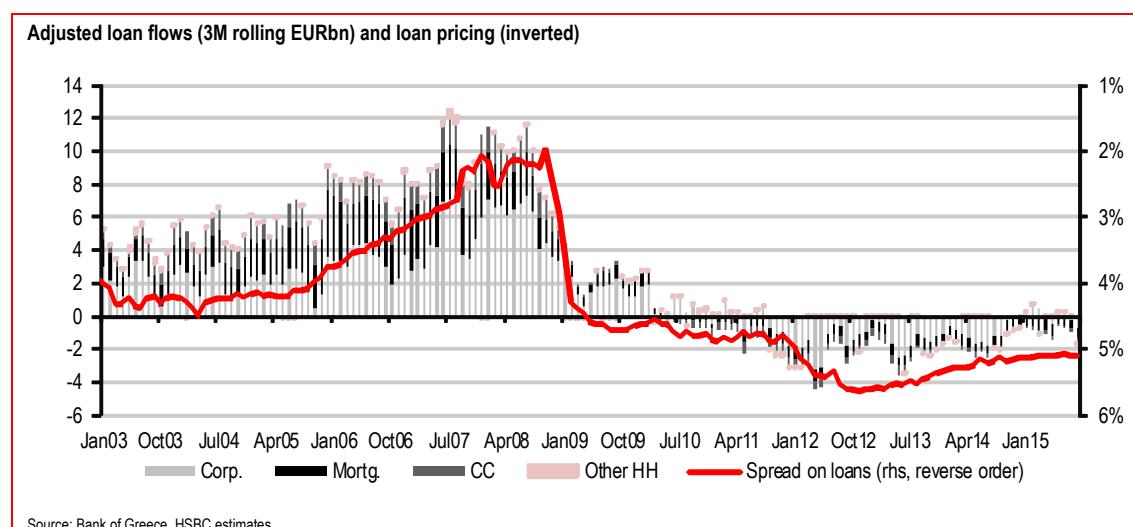
Source: Bank of Greece, HSBC estimates

Sector level data suggests there has been close to no change in stock spreads by product. The fall in overall loan pricing thus appears to be due to a change in the loan book mix (see graphs above).

Loan growth assumptions and assumed changes in loan pricing for domestic loans

	Corporate	Mortgages	Other HH
Assumed net loan growth			
2016e	-2.0%	-3.0%	-5.0%
2017e	1.5%	-2.0%	0.0%
2018e	2.2%	-1.0%	2.0%
Assumed change in loan pricing			
2016e	0.0%	0.0%	0.0%
2017e	-0.1%	0.0%	-0.2%
2018e	-0.4%	0.0%	-0.2%

Source: HSBC estimates



Pricing, however, has in the past proven to be very sensitive to loan flows. As can be seen in the previous chart, loan spreads steadily declined throughout the period of increased loan flows up to 2008 and subsequently spiked at the onset of deleveraging. On the basis of our loan forecasts, we assume no change in mortgage pricing for our forecast horizon. We do, however, assume some pressure on other household lending from 2017e, when we expect some loan growth to emerge, and mounting pressure on corporates from 2017 where we are most bullish on loan growth (see previous table).

The resulting headwind from shrinking loan books in 2016e and pricing pressures thereafter would be significant based on our estimates at c10% of annualised Q3 NII for Alpha and 18% for Piraeus and with a negative contribution to ROA of 20bp and 28bp respectively. The headwind would be most pronounced on our estimates for Piraeus due to its significantly larger relative exposure to domestic corporates, where we expect pressure on margins, and also due to its relatively smaller exposure to higher-growth foreign operations.

Headwinds from continuing deleverage would be significant based on our estimates (EURm)

	ACB	BOP
Total NII loss on loans (spread & volume)	-196	-331
% of Q3 2015 annualised NII	-10%	-18%
ROA contribution (bp)	-20	-28

Source: HSBC estimates

If, however, we bring all of the above together, including the improvement in interbank funding (Pillar 2 fee included), deposit growth and re-pricing as well as loan growth headwinds and loan pricing, the overall impact on NII would be positive, based on our estimates. It would represent a 9% increase from Q3 NII levels for Alpha and 3% for Piraeus and would account for 7% and 4% respectively of our expected improvement in net profit between 2015e and 2018e. It would also account for a c17bp and 5bp improvement in ROA respectively. Given that, at the sector level, as of 2014 the NII contribution to ROA was c43bp below the average 2002-2007 level and 2015 has so far seen a significant deterioration, we would consider our assumed improvement in NII as relatively conservative, leaving room for positive surprises.

Total improvement from NII

	ACB	BOP
NII gain % of Q3 NII	9%	3%
NII gain % of 2015e-2018e net profit improvement	7%	4%
NII gain % of 2018e Average Total Assets (bp of ROA)	17	5

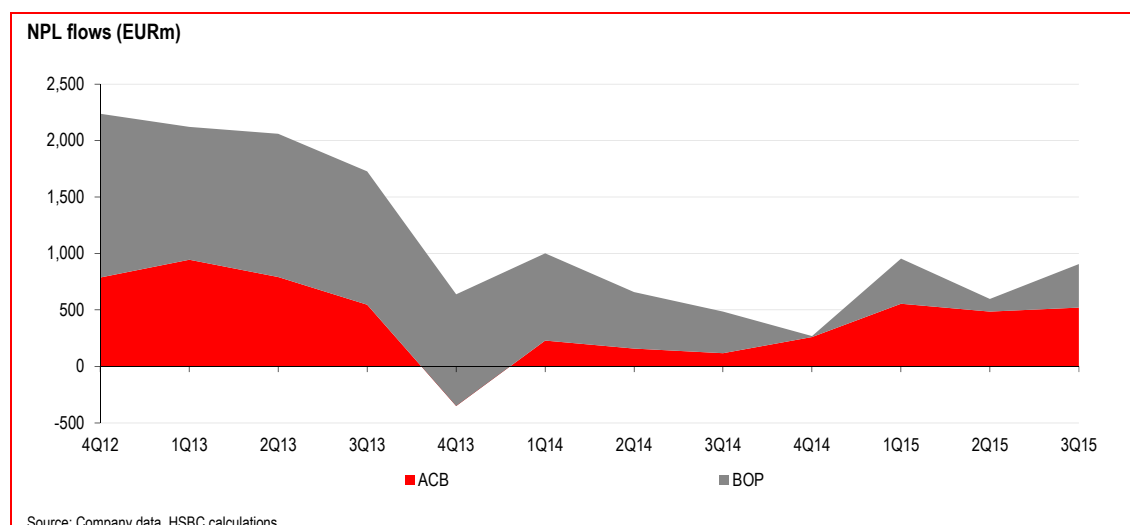
Source: HSBC estimates

Rundown of NPLs could provide additional funding relief

Admittedly, the above analysis would appear to lack consideration of future trends on asset quality.

We believe that there are two distinct elements to consider:

- **NPL flows:** Given that the consensus view suggests a further year of recession for Greece, one would expect a continuing deterioration of asset quality, with the resulting impact on NII from the increase of non-performing loans. Given the size of the correction in the Greek economy already and impending austerity measures, it could be argued that the average performing borrower in Greece is closer to default than in a normal environment. As a result, in such a scenario, inflows to NPLs would spike again, creating additional headwinds to NII.



Recent experience, however, has shown that the (remaining) loan book has proved to be resilient to further shocks. As can be seen in the previous graph, the recent turmoil caused an increase in NPL flows but it was by no means pronounced. We discuss the outlook for asset quality in some more detail later in the chapter, but, as far as NII is concerned, we have included headwinds to NII from deteriorating asset quality in our loan forecasts and they are thus already reflected in the above estimates.

- **Rundown of the NPL stock:** The flip side of the above is that a large part of banks' funding is tied up in a very large portfolio of (non-performing) loans, creating a significant drag to NII. We analyse our views on the rundown of the portfolio later in the chapter, but, in order to give an indication of the potential benefit, we present in the table below the estimated impact on our 2018e NII, net profit and ROA from carrying our 2018e estimated NPL book per bank. We estimate that eliminating the NPL portfolio would lead NII 3.6% higher for Alpha and 5.8% for Piraeus, adding some 8bp and 10bp to ROA, respectively.

Impact from carrying the NPL stock (EURm)

	ACB	BOP
Cost of liabilities (bp)	-103	-107
NPL stock	7,467	10,860
Estimated Interest Expense	-77	-116
% of 2018e NII	3.6%	5.8%
% of 2018e Net profit	6.2%	13.1%
% of 2018e Average Total Assets (bp of ROA)	8	10

Source: HSBC estimates

CoCo & wholesale funding: longer-term opportunities

Following the impending liability management actions, Greek banks will have little left in terms of wholesale funding. It is not entirely clear when they will regain access to the credit market, but we think there are some reasons to believe this may not be a factor near term as: (a) negative trends in loans and positive trends in deposits are likely to mean that banks have little need for extra funding; and (b) if pricing is in any way driven by Greek sovereign spreads, the cost of wholesale issuance would currently be prohibitive as it would be well above the cost of other funding sources.

Longer term, however, we think that Greek banks would aim to reinstate their access to the market in order to diversify their funding sources. It could also be argued that wholesale funding provides a more stable source of funding than the interbank market. One could assume that Greek banks could use wholesale funding to disengage from central bank funding that is, at least in theory, temporary in nature. However, as we have shown previously, by 2018e we expect most of the ECB dependence will be in place in order to fund low-yielding EFSF bonds. As a result, we would not think of it as structural and would see little stigma attached to it and, as a result, see no reason why Greek banks would create a negative carry just to remove ECB dependence. Replacing repos in the interbank market would have some benefits in terms of stable funding (assuming maturities of issued securities extend beyond 1 year) and/or releasing collateral, but we think the incremental cost would reduce banks' propensity to replace repos with wholesale funding.

One interesting possibility would be to replace the newly issued government CoCos with wholesale funding. We discuss capitalisation and capital requirements in the next chapter, but, simplistically, if the CoCos were put in place to provide capital in an adverse scenario and an adverse scenario does not materialise (as we envisage in our base case), they would in principle eventually cease to have a purpose and banks would be able to reimburse them.

Impact from removing CoCos (EURm)

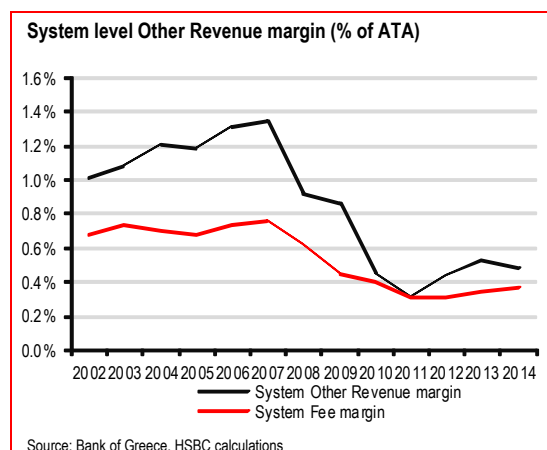
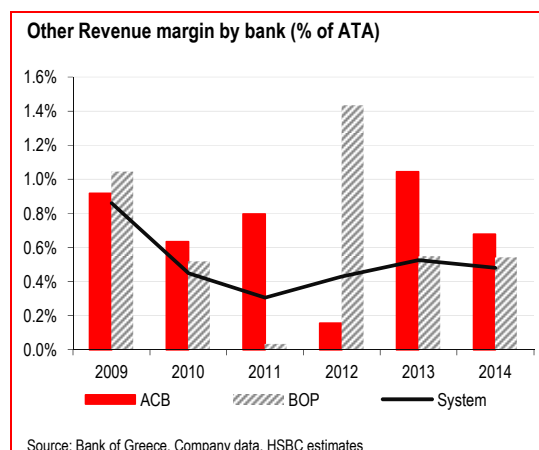
	ACB	BOP
Benefit	-73	33
% of 2018e NII	-3.4%	1.7%
% of 2018e Net profit	-5.9%	3.8%
% of 2018e Average Total Assets (bp of ROA)	-8	3

Source: HSBC estimates

In order to provide an estimate of the impact, we simplistically assume that CoCos and all other wholesale funding instruments left over after the Liability Management Exercises (LME) are replaced by two types of instruments: sufficient Additional Tier 1 (AT1) to satisfy regulatory requirements (1.5% of

2018e RWAs) at an assumed cost of 9%, and senior bonds at an assumed cost of 4.5% for the balance. Based on our estimates, the actual impact would be small positive for Piraeus and negative for Alpha as we do not expect any take-up of CoCos. The reason is that most of the government-funded CoCos would have to be replaced with similarly expensive AT1 instruments in order to satisfy regulatory requirements.

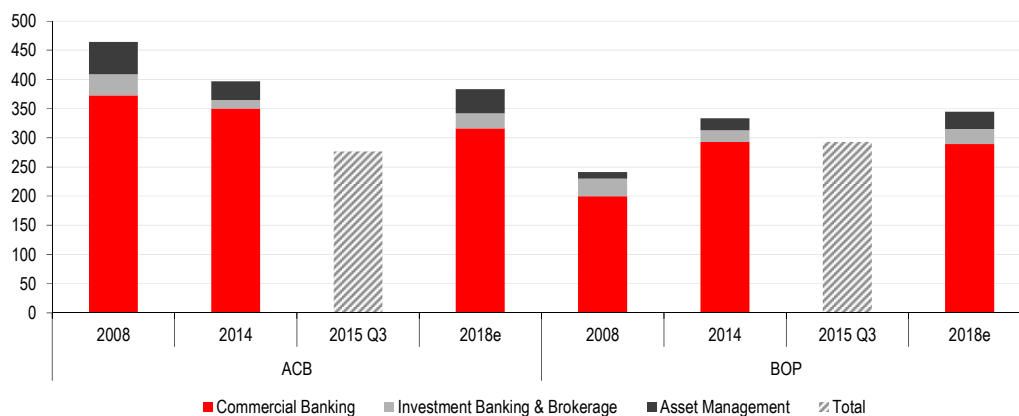
Longer-term opportunities for fee margin & activity pick-up



Historically, Greek banks have enjoyed healthy non-NII margins. Other revenue margins peaked at 1.35% of average total assets (ATA) in 2007 and have since been declining, reaching a low of 0.31% in 2011. From the 2007 peak in other revenue to 2014, system level fees have dropped by 44%, while trading profits have turned into losses, bringing total revenue down by c59%. Individual banks have seen similar trends, with low levels of activity putting pressure on both fees and trading, while in some instances fees have also been penalised by high government guarantee costs for emergency funding.

The first three quarters of 2015 have seen a further significant deterioration due to the recent turmoil and the resulting negative effect on overall activity. This should provide Greek banks with ample upside to improve the contribution of non-interest income to profitability. In absolute terms, banks should also see the benefits of consolidation coming through as balance sheets have been concentrated to a few players. It is thus not unimaginable that, over the next few years, the contribution of other revenue to the P&L could return to pre-crisis levels.

Breakdown of fees by type of activity and by bank* (EURm)

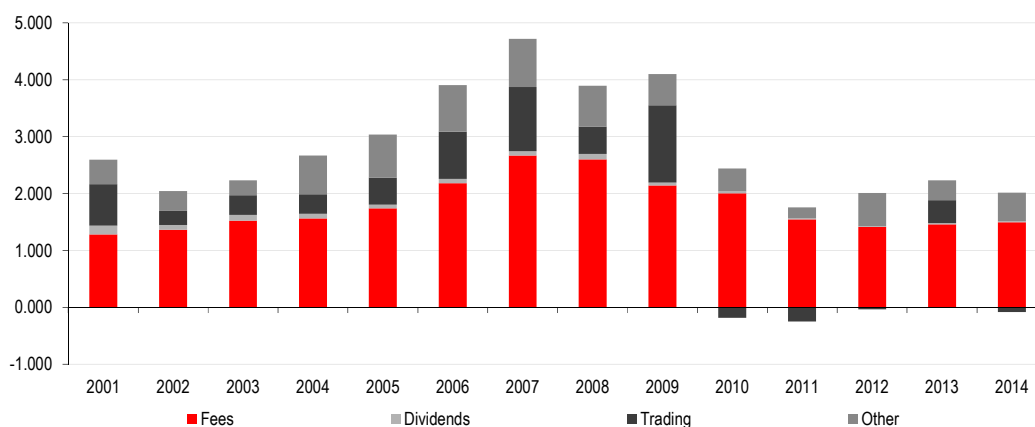


Source: HSBC estimates

* Q3 2015 levels are annualised.

Although the improvement should be significant in absolute terms, on a like-for-like basis we are somewhat more sceptical on margins. We believe that trading profits will remain depressed as long as the securities portfolio is constrained due to commitments from restructuring plans. Activity is also unlikely to return to peak 2008 levels given the correction in the economy, both on the commercial banking front as well as in brokerage and asset management. The only area where we see upside from 2008 levels within our horizon is in fees from POS terminals given the recent increase in the use of credit and debit cards, itself a consequence of legal limits on cash transactions as well as an improvement in consumers' familiarity with cards as a direct result of the capital controls. We don't, however, envisage that to be a game-changer.

System level evolution in other revenue (EURm)



Source: Bank of Greece, HSBC calculations

Improvement from other revenues

	ACB	BOP
Other revenue gain % of Q3 other revenue	38%	7%
Other revenue gain % of 2015e-2018e net profit improvement	6%	3%
Other revenue gain % of 2018e Average Total Assets (bp of ROA)	14	4

Source: HSBC estimates

It is however hard to make an accurate assessment of the upside for fees for individual banks. As previously stated, history is not necessarily a good guide for their future performance due to consolidation. The improvement, however, should still be substantial: we expect a c14bp improvement in ROA for Alpha and 4bp for Piraeus from 2015 levels due to the improvement in other revenue, below the improvement coming from NII that also comprises a much bigger (c80%) part of revenues. The improvement in other revenue would also justify about 6% and 3% of the improvement in net profits respectively.

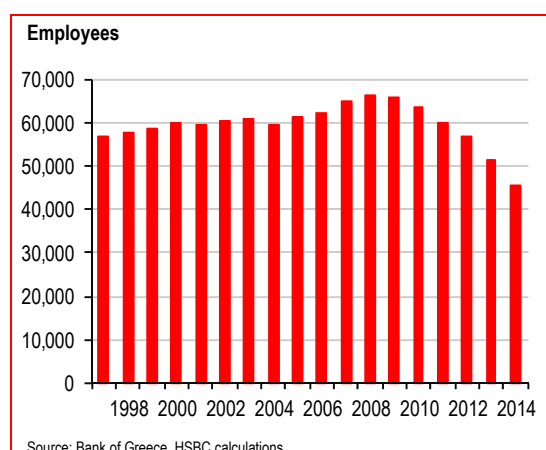
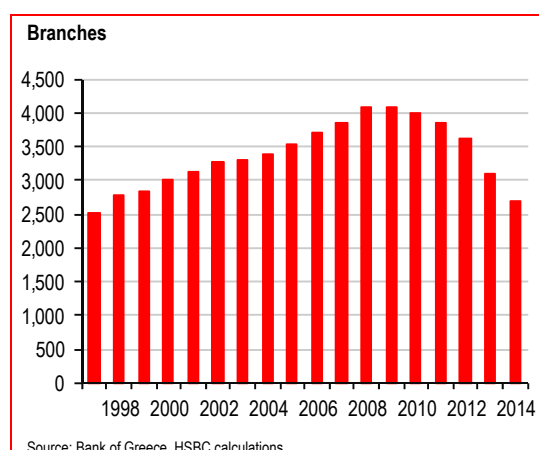
Fee margin (% of ATA)

	ACB	BOP
2008	0.77%	0.48%
2014	0.54%	0.37%
2015 Q3	0.39%	0.34%
2018e	0.56%	0.41%
Distance covered	43.34%	48.92%

Source: HSBC estimates

More specifically in terms of fee margins, by 2018e we expect Alpha to cover 43% and Piraeus 49% of distance between Q3 2015 levels and 2008, with 2008 reflecting healthy levels of activity and near peak system level fees. When considering additional upside potential, we think it is important to remember that, based on our economists' forecasts, Greece's GDP is expected to still be below 2000 levels in 2017.

Further room for structural reduction in costs



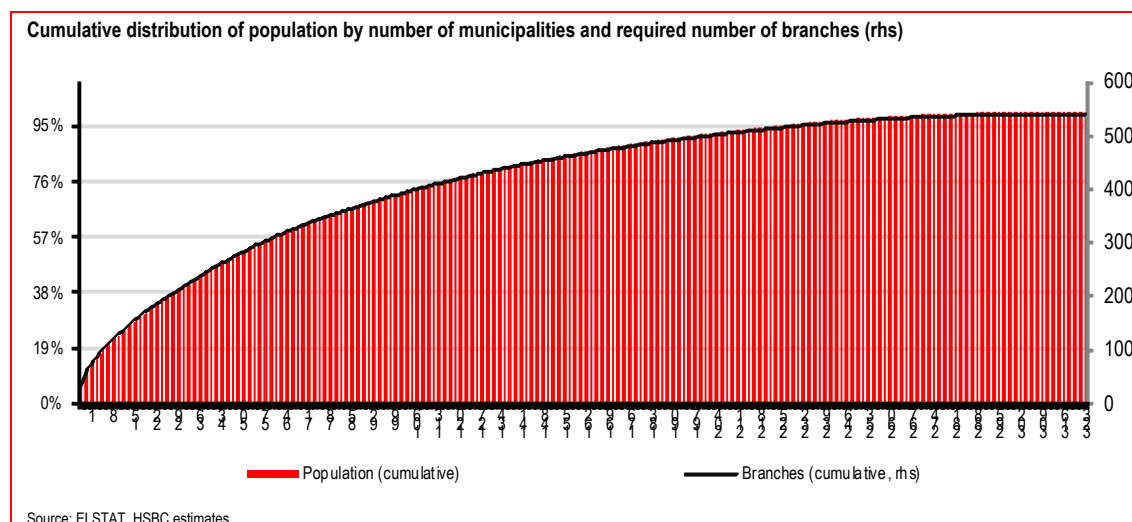
Greek banks have significantly improved their cost efficiency throughout the crisis, with the improvement contributing c66bp to the change in 2014 ROA versus the 2002-2007 period average. At the system level, from 2009 to 2014, over 30% of the workforce has left the industry and 34% of branches have been closed. Given that activity is expected to remain low for a number of years, we think it is important to know if there is structurally further room to reduce costs or if cost discipline is the best that can be expected.

Banking sector cost metrics (2014): Greece versus eurozone countries

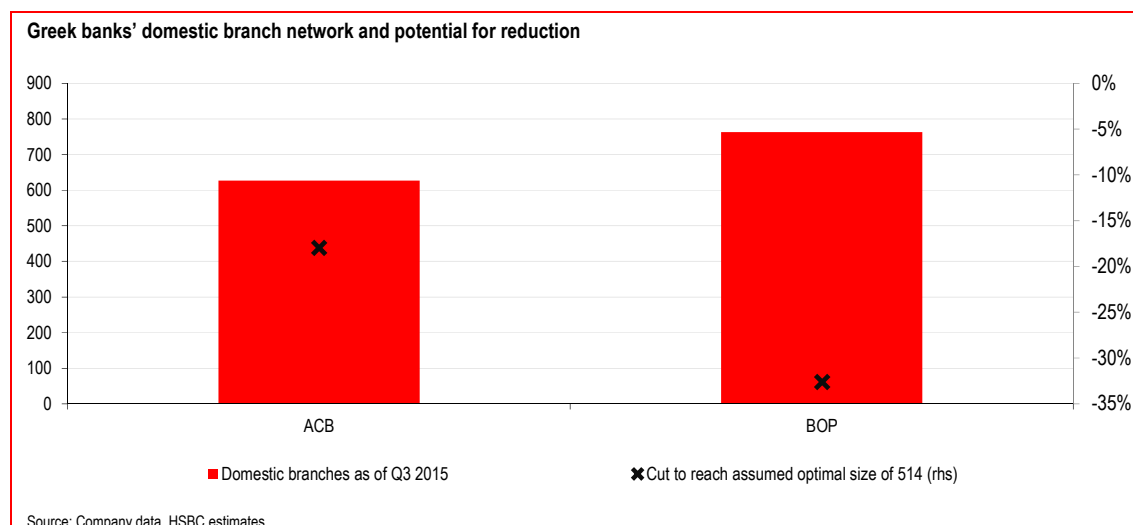
	Greece	Rank	Euro-area	No.1	No.2	No.3
Population per branch	4,090	8	2,111	10,785 Estonia	9,096 Netherlands	6,254 Latvia
Population per employee	241	5	166	327 Lithuania	290 Slovakia	271 Estonia
Employees per branch	17	12	13	117 Luxembourg	51 Netherlands	40 Malta
Assets per person (EUR'000)	36	14	90	1,301 Luxembourg	148 Ireland	146 Netherlands
Assets per employee (EUR'000)	8,696	12	14,932	28,630 Luxembourg	26,153 Finland	26,055 Netherlands

Source: ECB, HSBC calculations

As of 2014, Greece ranked 8th among euro area countries in terms of population per branch based on ECB data and was well below the top performers in the region, suggesting there is still upside from optimising the network post consolidation. Population density and other socioeconomic metrics would in principle affect how a bank positions its network. In order to make an assessment of what the optimal network size would be, we start by looking at population density.



We have looked at the distribution of the population at a municipality level as a proxy of a geographical region that would likely be within a branch's reach, although we accept that it is by no means a perfect measure. On this basis, 95% of the Greek population lives within 226 municipalities (out of a total of 326). If additionally we assume that each branch can at most service a population of 20,000 (given that its actual customer base will be significantly less simply due to competition), we can conclude that Greek banks would need 514 branches each to reach about 95% of the population.



The potential room for improvement differs among banks. We think Alpha Bank and Piraeus could reduce their networks by 19% and 33%, respectively, before they reach assumed optimal size, creating ample room for cost-cutting.

Things get a bit more complicated on the employee front. The total numbers of bank employees in the country is relatively small: one in 241 people, with Greece ranking 5th in the eurozone. Branch intensity (employees per branch) is above the euro-area average but well below the best-in-class countries. And we would caution against using branch reduction estimates to imply employee reduction numbers as many employees are tied up in central functions, including the in-house problematic asset management units, c6% of Piraeus's Group FTEs, for example.

Cost metrics for Greek banks and peers

	ACB (Q3 2015)	BOP (Q3 2015)	Average	Europe (2014)	CEEMEA (2014)	Domestic Spain (2014)	Italy (2014)	Nordics (2014)	Greek system (2014)
Cost Margin	1.82%	1.51%	1.66%	1.34%	2.16%	1.22%	1.90%	0.79%	1.62%
Cost-Income Ratio	55%	50%	53%	59%	43%	49%	68%	47%	61%
Staff costs/ FTE (EUR000)	37	34	35			75	73	97	71
Opex/ FTE (EUR000)	88	66	77			133	127	163	134
Loans/FTE (EURm)	4.4	3.5	3.9			7.3	4.3	12.1	5.0
Opex/ Branch (EURm)	1.3	1.2	1.3			1.0	1.6	4.7	1.2
Loans/Branch (EURm)	67	64	66			53	53	359	85
FTEs/ Branch (no.)	15	18	17			7	13	30	17

Source: HSBC estimates

We think the latter point is significant. The average number of loans per branch (branch intensity), both at a bank and at a system level, compares favourably with peers in Spain and Italy. Greek banks also compare favourably to European peers when we look at the average personnel cost (staff costs per employee), even if we look at system level numbers to exclude distortions from their South Eastern Europe (SEE) operations. However, there is an apparent lack of employee intensity (loans per employee).

This would suggest that many employees are tied up in non-productive functions. However, we believe that this is directly related to: (a) the low level of lending activity in the economy; and (b) the need for NPL resolution due to large non-performing balances. As a result, we do not think that staff numbers can

fall significantly from here as employees will be tied up in the work-out of non-performing assets until activity returns. The alternative would be for banks to adjust their headcount aggressively, maintaining it at low levels for a few years and then building up capacity again if and when activity returns. Given the cost of redundancies, we believe banks would instead simply restrict hiring, allowing headcount to slip.

Impact on profitability from costs

	ACB	BOP
Cost gain % of Q3 Cost	-16%	-21%
Cost gain % of 2015e-2018e net profit improvement	4%	7%
Cost gain % of 2018e Average Total Assets (bp of ROA)	9	10

Source: HSBC estimates

Our less aggressive stance on cost cutting, however, does not mean that we do not expect strict cost discipline from Greek banks. After all, activity is and is likely to remain low, making cost discipline a priority. But, as can be seen from the table below, we expect little in terms of further improvements in profitability arising from costs. At the same time, though, we expect little to no pressure from the cost line.

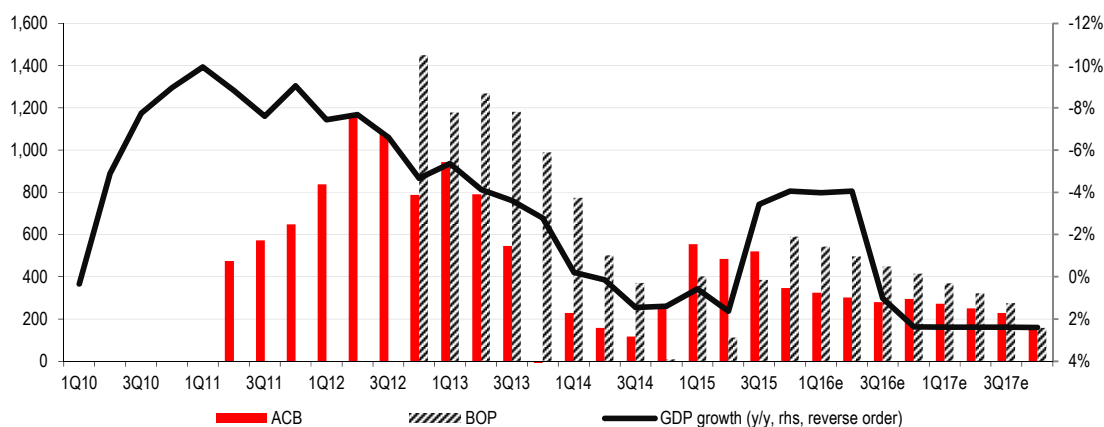
Asset quality – a surmountable hurdle

Greek banks have faced an unprecedented deterioration in asset quality over the course of the Greek crisis years, with the average (group-level) NPL ratio for the top 4 banking institutions jumping from 6% in 2009 to 33% in 2014 and provisions effectively wiping out all pre-provision profits. The recent turmoil during 2015 has exacerbated trends and NPL ratios have increased further following the latest Asset Quality Review (AQR) from the ECB. Things could hardly be worse.

NPL flows could surprise positively

Given that the consensus view suggests a further year of recession for Greece, one would expect a continuing deterioration of asset quality, with the resulting impact on provisions from the increase of non-performing loans. Given the size of the correction in the Greek economy and impending austerity measures, it could be argued that the average performing borrower in Greece is closer to default than in a normal environment. As a result, in such a scenario, inflows to NPLs would spike again, creating additional headwinds to profitability.

Domestic NPL flows (EURm, adjusted for one-off AQR effects) have generally tracked GDP growth and we expect this to continue



Source: Company data, HSBC estimates

Recent experience, however, has shown that the (remaining) loan book has proved to be resilient to further shocks, while the economy is performing better than originally feared, with the EC recently increasing its 2015 GDP growth forecasts to -1.4% from -2.3% previously. As can be seen in the previous graph, the recent turmoil caused an increase in NPL flows, even excluding one-off AQR effects, but, it was by no means pronounced. Part of the reason why NPL flows were elevated in Q3 was arguably the two-week long bank holiday in July and the administrative hurdles that it created, with banks suggesting that the situation had already improved in August and September.

Additionally, recent and impending legislative changes reduce the protection enjoyed by borrowers, potentially reducing the propensity of mortgage holders to strategically default on their loans. It is also important to remember that recognition of problematic exposure is very high among Greek banks following two subsequent AQRs from the ECB (2014 and 2015) and two diagnostic studies of their loan portfolios conducted by BlackRock for the Bank of Greece (2011 and 2013). After all, a significant level of provisions has already been set aside for exposures that are still performing, effectively front-loading the required effort on asset quality.

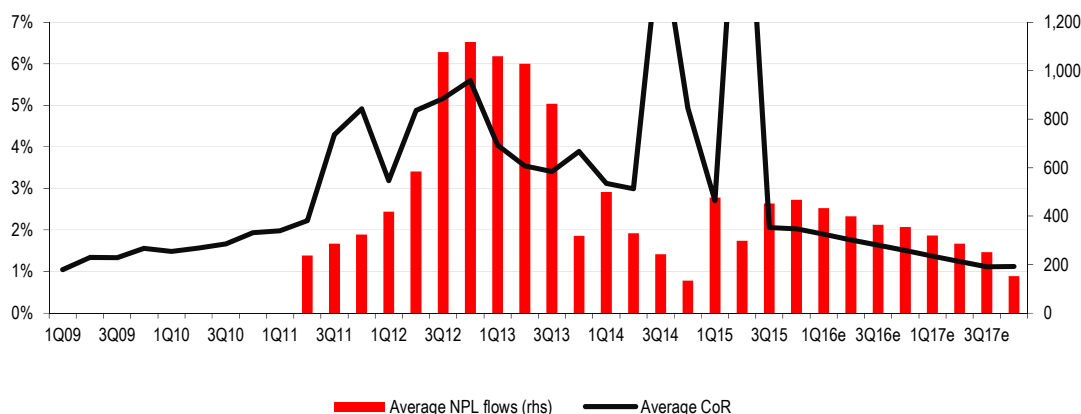
Expected improvement in provisions and contribution to profitability

	ACB	BOP
3Q15	259	253
4Q18e	94	112
Change	-64%	-56%
LLP gain % of 2018e Average Total Assets (bp of ROA)	68	47

Source: HSBC estimates

In that context, our estimates are rather conservative: we expect NPL flows in the next four quarters to reach c51% of 2013 levels, with the cost of risk returning to a more normalised c85bp level only in 2018e. The impact on profitability, however, should not be underestimated: we expect LLPs to fall by c64% from Q3 2015 levels to Q4 2018e for Alpha and 56% for Piraeus, contributing c68bp and 47bp to ROA respectively.

Average domestic NPL flows (EURm, adjusted for one-off AQR effects) and actual average cost of risk (including AQR effects)



Source: Company data, HSBC estimates

Significant uncertainty on rundown of doubtful portfolios

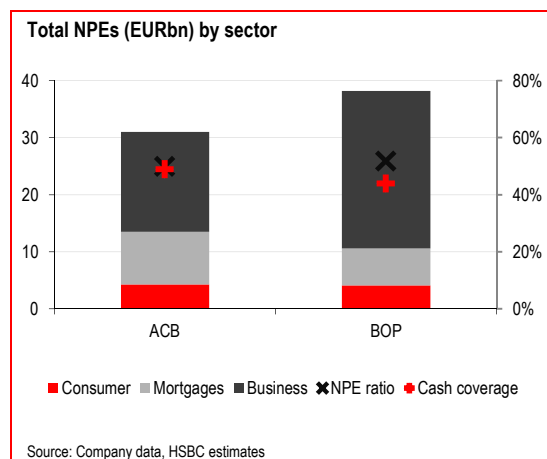
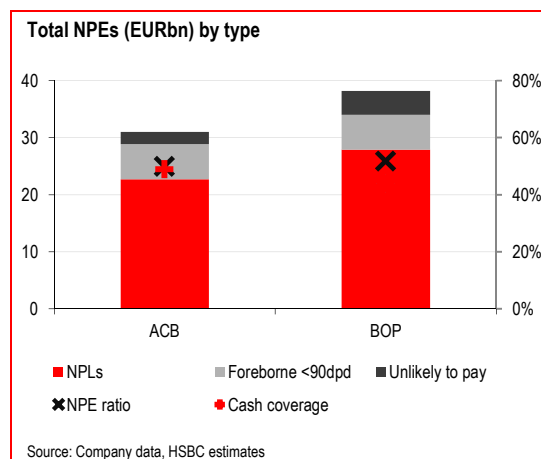
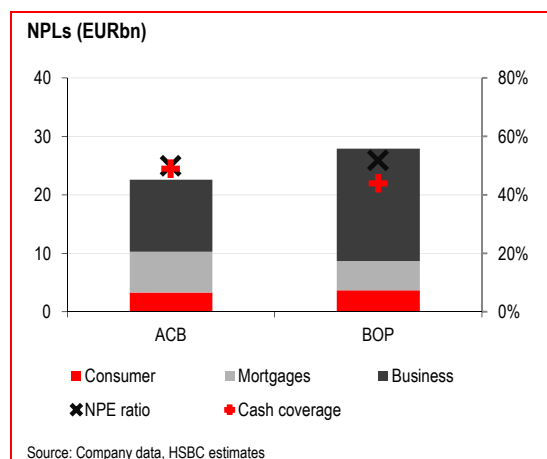
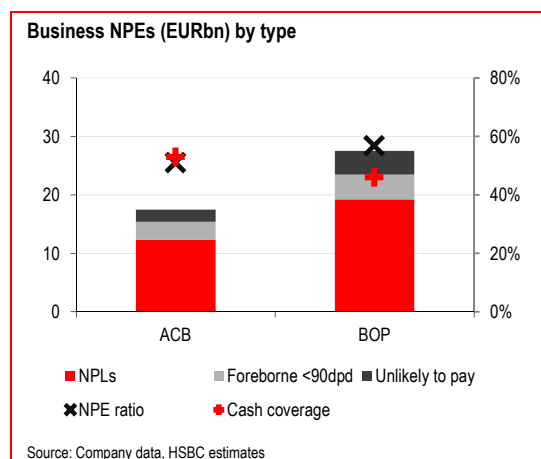
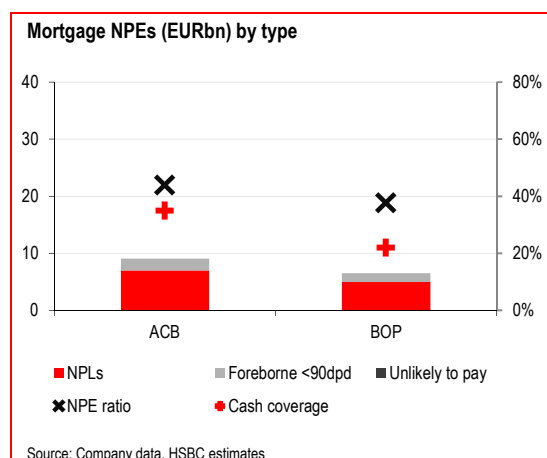
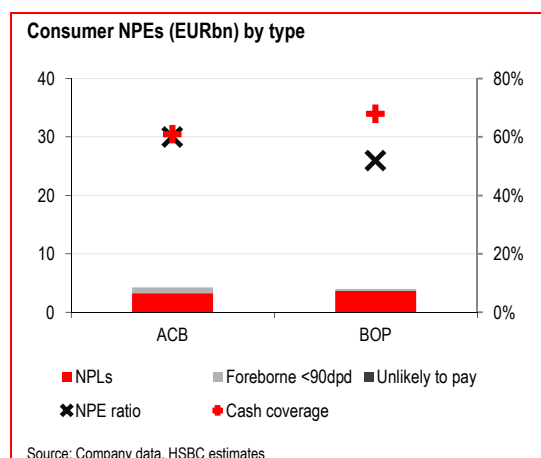
Following the recent AQR adjustments, Greek banks have about 48% of their loans classified as non-performing exposures (NPEs) as per the EBA definition, with about 73% of those classified as non-performing loans (NPLs). As we have noted previously, the sheer size of the portfolios creates a drag on profitability as funding and costs are tied up in a non-core activity. It should thus not be surprising that we believe the management of doubtful assets can be a great source of risk or value going forward.

We present the size and characteristics of the two banks' doubtful portfolios in a series of graphs on the next page. By far the biggest exposure is to business loans (62% of the net portfolio), followed by mortgages (30%) and consumer credit (8%). Additionally, our understanding is that there is little if any concentration within the doubtful business loans portfolio among different industries. However, that makes it harder to assess the true value of the portfolio from an outsider's perspective. Although there is a significant amount of collateral attached to business loans, the value of that collateral is usually directly linked to the outlook for the specific industry, unless the collateral can easily be re-purposed. As a result, it would appear that the true value of a large part of the portfolios depends heavily on the outlook (and industrial composition) of the Greek economy.

At the one extreme, one could assume that following four separate reviews, the doubtful portfolios of banks are adequately provisioned and no further effort will be required from the banks. For their part, in their business plans banks appear to rely very little on proceeds from liquidation of exposures and believe that restructuring and recoveries will offset any required write-offs. Given the additional top-up in provisions that we have assumed for 2016e and 2017e, we tend to subscribe to this view.

At the other end of the spectrum, one could assume that current coverage levels are deeply insufficient as the correction in the economy has been so severe that borrowers have been permanently impaired and there is little to no hope of recovering any value from the exposures. In order to make an assessment, we run a scenario (Scenario 1 in the next table) where we assume that the recovery rate for doubtful exposures is 10% for business and 6% for consumer loans (both 20% of the current system-level coverage-implied recovery rate) and 50% for mortgages that, based on the sector-level average LTV of c70%, would imply a cumulative fall in the value of the collateral of c65%. Simplistically, we also assume that the required rate of return (RRR) is 15% and that the portfolio is run down over the course of 10 years.

NPE portfolio breakdown



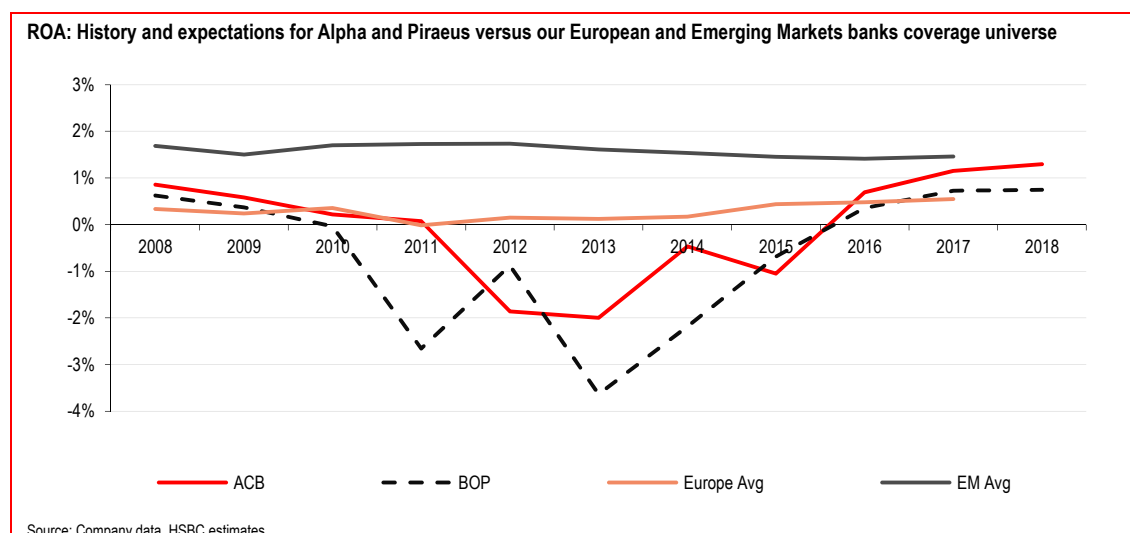
Punitive assessment of the value of the doubtful assets portfolio of Greek banks

	ACB	BOP
Coverage-implied recovery rate	51%	56%
Business	47%	54%
Mortgages	65%	78%
Consumer	39%	32%
Scenario 1:		
Recovery assumptions:	22%	17%
Business	10%	10%
Mortgages	50%	50%
Consumer	7%	7%
NPV at 15% RRR	-4.6	-7.5
Business	-3.2	-6.1
Mortgages	-0.7	-0.9
Consumer	-0.7	-0.5
NPV as % of 2015e TBV	49%	83%
Business	34%	67%
Mortgages	7%	10%
Consumer	7%	6%
Scenario 2: 5pp higher recovery		
NPV as % of 2015e TBV	41%	72%
Business	30%	60%
Mortgages	5%	8%
Consumer	6%	5%
<i>NPV as % of 2015e TBV @ 10pp higher recovery</i>	<i>38%</i>	<i>59%</i>
<i>NPV as % of 2015e TBV @ 20pp higher recovery</i>	<i>19%</i>	<i>39%</i>
<i>NPV as % of 2015e TBV @ 30pp higher recovery</i>	<i>0%</i>	<i>19%</i>

Source: HSBC estimates

If such a scenario were to materialise, Alpha could lose 49% of its 2015e tangible book value (TBV), while Piraeus could lose 83%. We would expect institutions with a domestic and/or business focus or lower levels of coverage currently would be more heavily affected. The results of the scenario, however, are highly sensitive to our assumptions on recovery rates. A 5pp increase in the recovery rate (see Scenario 2 above) would reduce the impact on TBV by c10pp. To make things worse, it is more likely than not that the starting coverage ratios are reflective of the quality of the portfolio rather than the adequacy of provisioning. Thus, using the same recovery rate across banks is likely inadequate. But the analysis still highlights the exceptionally high sensitivity of Greek banks' value to the recovery value of their doubtful portfolios.

ROA back between emerging and developed markets



What it all boils down to is that we expect Alpha and Piraeus to see a steady and significant improvement in ROA over the next few years, from the negative levels seen over the past few years to an ROA in excess of 100bp by 2018e. This shift would bring them well below our emerging market banks coverage universe but somewhat above our European banks coverage universe. A normalisation of provisions is by far the biggest swing factor in our estimates, followed by NII (c39bp of ROA on average) and other revenue (c21bp).

Disaggregation of profits into underlying components (2018e)

	ACB	BOP	Average
Net Interest Income	3.14%	2.36%	2.75%
Other Revenue	0.81%	0.66%	0.73%
Total Revenue	3.95%	3.02%	3.48%
Costs	-1.57%	-1.44%	-1.51%
Cost-Income	40%	48%	44%
Operating profit	2.38%	1.58%	1.98%
LLPs	-0.54%	-0.52%	-0.53%
Loans % of Assets	68%	58%	63%
CoR	80	90	85
Other	-0.54%	-0.31%	-0.42%
ROA	1.30%	0.74%	1.02%

Source: HSBC estimates

It is important to note that, on our 2018 estimates, the average ROA would be above 2008 levels on a better cost performance (worth c37bp on average), a more benign asset quality environment (c31bp) and a better NIM (10bp), with other revenue (-23bp) below 2008 levels due to lower levels of economic activity.

Prospective leverage: down but not out?

- ▶ We believe both banks will be able to cover their AQR and baseline scenario capital needs, avoiding resolution
- ▶ Beyond that, however, the make-up of capital on the other side of the recapitalisation will vary
- ▶ Capital requirements are also not entirely clear, we believe, offering reasons to be cautious; but upside for leverage exists

Decomposing the Rubik cube of recapitalisation

In order to avoid recapitalising banks under the stricter BRRD requirements that could bring depositor bail-in, the recapitalisation process has been expedited by all relevant parties in order to take advantage of the legal framework that was recently voted into law and is binding until year-end. Since Piraeus kicked off proceedings with the announcement of its Liability Management Exercise (LME) on 15 October, events around the Greek banks' recapitalisation have unfolded at an unprecedented pace. In summary:

- ▶ All banks announced LMEs for most of their outstanding senior, subordinated and hybrid debt instruments.
- ▶ The new legislation that governs the recapitalisation of Greek banks for 2015 before BRRD becomes active on 1 January 2016 as well as rules governing the Hellenic Financial Stability Fund was voted into law by the Greek parliament.
- ▶ The Ministry of Finance has issued a decree specifying the details of state participation in banks.
- ▶ The ECB and the Single Supervisory Mechanism (SSM) have announced the results of the AQR exercise and the accompanying stress test as well as the capital requirements that arise from them.
- ▶ Banks have submitted their capital plans to the SSM in order to cover their capital needs and have set dates for EGMs to approve the necessary capital actions.

The direct consequence of the expedited schedule is that various processes of the recapitalisation are occurring at the same time. Once disentangled, however, the ordering of what needs to happen is relevantly simple:

EGMs need to be called to approve any of the below as they result in an actual (shares) or potential (CoCos) change in the share capital of the institution.

Banks have launched LMEs for most of their outstanding senior, subordinated and hybrid debt instruments, allowing holders to exchange in full or at a discount the nominal value of the securities for shares in the upcoming capitalisation at a price equal to that of the book-building process. Some banks have also presented holders with the option of receiving cash, albeit at bigger discounts to nominal value. Banks create capital due to the capital gain that is booked if the exchange (for shares or cash) is below par and due to the creation of new equity if debt is exchanged for shares.

Book-building processes are conducted in order to attract private sector investment into new shares. Existing shareholders can participate, but there are no rights attached to the issue.

Banks have submitted various mitigating actions to the SSM for approval. These include asset sales as well as developments during recent months that were not included in the calculation of capital needs arising from the recent stress test (movements in the AFS reserve, pre-provision profits above stress test expectations, DTC creation, changes in the tax law, etc). If approved, these are included in the bank's capital plan.

The total of the above is defined as the total private sector participation. If the total sector participation is above the maximum capital needs arising from the AQR and the baseline scenario of the stress test, the institution avoids resolution. We expect all banks to avoid resolution, so we do not investigate that scenario.

If the total of the above is also enough to cover the institution's total capital needs (ie including the capital needs under the adverse case scenario), then the institution avoids the burden sharing that would have to precede any injection of state funds.

If private sector participation is not sufficient to cover the total capital needs, then burden sharing is activated. In this case, any outstanding hybrid, subordinated and senior debt instruments (including state preference shares) are converted to equity with haircuts based on a valuation (that will be done by the Bank of Greece using independent valuers) until sufficient capital is present or until all available funds are exhausted. The conversion price will be the same as that used in the LME and book-building processes. If state preference shares are converted into equity, they carry full voting rights and their ownership is transferred from the state to the HFSF.

Once all of the above is completed, the state can meet any remaining capital needs via (a) shares with full voting rights for 25% of the remaining capital needs, and (b) 8% coupon CoCos for the remaining 75%.

Pre-existing shares owned by the HFSF will continue to have restricted rights if the resulting private sector ownership of the institution is above 50%. The HFSF will prioritise selling shares with restricted rights, while all HFSF shares rank senior to other shares in liquidation.

Total capital needs could thus be met by: (1) asset sales and other actions; (2) an increase in share capital from LMEs, private sector book-building, private or state burden sharing as well as state participation, all at the same price; (3) capital gains on the LMEs; and (4) state-funded CoCos.

Although the process is known, many details are still to be determined. Most deadlines for participation in the LMEs have now passed and early indications on participation are positive, although bondholder meetings will define the final result. However, private sector participation in the book-building exercises as well as the Bank of Greece valuations for any burden-sharing are yet to be determined. This has a direct impact on state participation and the calculation of the free float. For lack of a better alternative, for our base case we assume that management expectations are largely fulfilled. Namely, we assume that:

- ▶ Alpha is able to cover the full capital need through the book building and the LME, with no need to resort to state funds.
- ▶ Piraeus is able to cover up to the AQR and baseline scenario capital needs through the book building, LME and EUR200m of other actions. Any remaining capital needs are then met with state funds.

Recapitalisation breakdown by institution (EURm)

	ACB	BOP
Comprehensive Assessment Outcome:		
Capital Need (1)	2,743	4,933
under AQR	0	2,188
under Baseline	263	2,213
under Adverse	2,743	4,933
Capital Plan:		
Other actions (a)	1,086	793
LME	1,086	593
Asset Sales		200
Other (incl. DTAs)		
Private Sector book building (b)	1,658	1,420
Total private sector participation (incl LME)	2,743	2,013
% of Baseline & AQR	1045%	100%
% of Total capital need ex-non LME actions	100%	43%
Burden sharing required?		YES
Burden sharing at LME terms (c)	0	0
o/w private sector for share issuance	0	0
o/w state preference shares for share issuance	0	0
Public sector injection = (1) - (a) - (b) - (c)	0	2,720
o/w shares	0	680
o/w Cocos	0	2,040

Source: HSBC estimates

On the basis of the above, as a result of the recapitalisation the two banks would increase their equity base by c42%, with the HFSF holding additional subordinated instruments of c23% of the resulting TBV in the case of Piraeus. On a simple measure of leverage (Assets / Equity), both would stand at relatively low levels, with Alpha at c7x as of 2015e and Piraeus at c10bp.

Assumed increase in equity (EURm) and resulting state ownership of subordinated debt instruments

	ACB	BOP
Equity increase	2,718	2,685
% of Q3 2015 TBV	41%	43%
Resulting equity	9,314	8,976
CoCos and state prefs as % of resulting equity	0%	23%
Assets / Equity	7	10

Source: HSBC estimates

This begs the question: if all goes according to plan and Greek banks conclude their restructuring plans without facing an adverse scenario and normal regulatory supervision is reinstated, will they be overcapitalised? In order to make an adequate assessment, we look at long-term capital requirements.

A take on long-term capital requirements for Greek banks

In principle, Greek banks are relatively simple, domestically focused retail banking institutions. It would thus at first appear that capital requirements should be among the lowest in the eurozone. From a regulatory perspective, minimum capital requirements would be set at a relatively low level. Based on the status quo, banks that are directly supervised by the SSM need to abide by an 8% capital requirement (4.5% minimum Common Equity Tier 1 (CET1), a 2.5% capital conservation buffer and a 1.0% surcharge) by the ECB as they are considered significant institutions (a kind of blanket approach to systemic importance). However, we believe there are number of reason to doubt that approach.

In the recent stress tests, the SSM imposed a 9.5% minimum capital requirement on Greek banks under the baseline scenario. That would imply that the supervisor sees some common need for banks to have higher capital requirements. Admittedly, the Greek banking market is now highly concentrated. That would arguably call for a higher charge for systemic importance of institutions from a domestic perspective than that implied by the ECB's blanket 1% requirement. We treat this additional 1.5% as a Pillar 2 requirement for systemic risk, bringing the total systemic risk charge to 2.5% and the regulatory requirement to 9.5%.

In practice, individual bank capital requirements are effectively defined by the Supervisory Review and Evaluation Process (SREP). The SREP can result in capital requirements above the common regulatory minima to reflect risks specific to the institution. We think management needs to take this into account when doing its capital planning and prudentially keep capital levels above regulatory requirements to avoid nasty surprises, ie use a management buffer. We see two main areas in need of attention:

- ▶ **Impending changes in regulatory requirements:** Given that the SREP looks at capital with a 12-month-forward view, banks would need to take into account any impending regulatory changes that can affect the supervisor's view on the need for the bank to hold extra capital. Rules that are being phased out would be the obvious thing to mention here, but, given that we're using fully loaded ratios, this has little bearing on our estimates. The list of other pending regulatory hurdles is (still) long and timing for implementation is (still) uncertain, but we would mention MREL and all measures related to RWA inflation (Fundamental Review of the Trading Book, revision of standardised risk weights, BIS and ECB reviews of risk weightings, operational RWAs, sovereign risk-weights, etc) as the most relevant here. Changes to the treatment of insurance holdings (Danish compromise) and the debate on deferred tax assets (DTAs) would also be relevant, but the former is less of an issue for Greek banks, while fully loaded ratios and the apparent resolution of the debate on Deferred Tax Credits (DTC) means there is little threat on this side. Liquidity (LCR) and funding (NSFR) are also worth noting.
- ▶ **Prudential requirements from further stress tests.** In practice, the SSM already requires Greek banks to be well above the base-case regulatory requirements for prudential reasons by asking banks to also satisfy (lower, 8% CET1) capital requirements under an adverse forward-looking economic scenario. In theory, if the adverse scenario does not materialise, that additional capital would no longer be necessary. In practice, however, we fear that stress tests have become a recurring feature

for European banks. And although their scope and reach as well as the severity of the assumptions in the adverse scenario might be limited somewhat in the future, as recent announcements by the EBA would suggest, we still think it would inform the SREP. Given Greek banks' capital sensitivity to movements in the value of their problematic portfolios as seen in the previous chapter, we would think managements should err on the side of caution and aim to hold more capital.

We assume a common 1.0% add-on for impending changes in regulatory requirements. In line with the 2014 experience for Greek banks, where macroeconomic assumptions were less severe in the face of recovery, we think that using the recent 2015 stress tests as a guide for long-term additional capital requirements would be unwise. Instead, we weight the impact on capital from the 'baseline' and 'adverse' case scenarios of the recent ECB exercise equally and assume a 40% haircut. What that means in practice is that we expect the adverse case scenario in future stress tests to have an impact that is 40% less than half-way between the baseline and adverse case scenario of the 2015 stress test. After all, the 2015 baseline scenario included a recession. As visibility improves, this buffer could eventually fall.

HSBC target CET1 ratios		
	ACB	BOP
Minimum common equity Tier 1	4.5%	4.5%
Capital conservation buffer	2.5%	2.5%
Basel III minimum	7.0%	7.0%
SIFI buffer	1.0%	1.0%
Systemic risks in Pillar 2	1.5%	1.5%
Total Regulatory Requirement (a)	9.5%	9.5%
Future stress tests buffer	1.8%	2.0%
Regulatory change buffer	1.0%	1.0%
Management Buffer (b)	2.8%	3.0%
<i>pro-memoria: 2015 stress test impact</i>		
Baseline	-0.10%	-0.30%
Adverse	-7.50%	-7.80%
Target CET1 % (a) + (b)	12.3%	12.5%

Source: HSBC estimates

Unsurprisingly, capital requirements are pretty similar for the two banks. They are also somewhat above management targets for other European banks, but we believe this is justified by the need to take a prudential approach to capital needs in order to reflect the risk inherent in Greek banks' doubtful loan books.

Looking through to excess capital

Despite our relatively conservative take on both capital accumulation (returns) and capital requirements, our estimates still suggest that both banks would have excess capital as of 2018e. However, given the rules governing the two different outstanding non-equity state-aid instruments, namely CoCos from the 2015 recapitalisation and preference shares dating back to 2008, we think that, from a shareholder's perspective, excess capital should be viewed on a net basis assuming that those instruments are paid back first as a matter of priority.

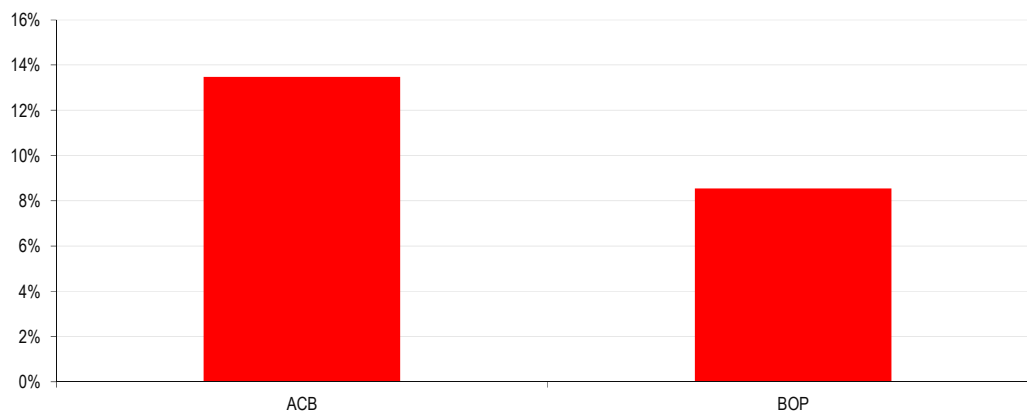
Excess capital versus our target CET1% (2018e)

	ACB	BOP
2018e Target CET1%	12.3%	12.5%
2018e CET1%	20.3%	20.2%
o/w Outstanding CoCos/ Prefs %	0.0%	3.6%
Excess capital incl. CoCos/ Prefs (%)	8.0%	7.7%
Excess capital net of CoCos/ Prefs (%)	8.0%	4.1%
Excess capital net of CoCos/ Prefs (EURm)	4,308	2,336

Source: HSBC estimates

The capital position net of any CoCos and preference shares would still be in excess of our target capital ratios. In comparable terms, excess capital as a percentage of RWAs would be slightly higher for Alpha than Piraeus, but at significant levels for both. If we combine the above analysis with our views from the previous chapter on ROA, we conclude that returns would reach 13.5% for Alpha and 8.5% for Piraeus based on our estimates (see below) after any excess capital is paid out. We would argue that Piraeus ranks lower as its focus on corporates creates the biggest drag on profitability as of 2018e due to both the higher volume of non-performing exposures and the impact from loan pricing.

2018e ROTE excluding excess capital



Source: HSBC estimates

Top-down considerations

- ▶ Although the recent turmoil is expected to put another dent in the Greek economy's recovery, the outlook longer term is positive
- ▶ With programme execution front-loaded, the first review pending and issues with IMF participation and debt restructuring unresolved, near-term uncertainties remain
- ▶ Together with recent experience on timing slippage as well as the likelihood of another 'accident', we think caution is warranted

Macro backdrop positive longer term

By Fabio Balboni

In H1 2015, the economy surprised on the upside, narrowly escaping another recession thanks to 0.1% q-o-q GDP growth in Q1 (after having fallen by 0.2% q-o-q in Q4 2014), and then posting 0.9% q-o-q growth in Q2 2015. Growth in Q2, however, was helped by some temporary factors: the public sector expanded by 3.8% q-o-q, while net trade contributed positively to growth because of the collapse in imports (-4.9%) and despite flat exports growth. With capital controls in place since the end of June, we expect the economy to go back into recession in H2 2015. Economic confidence has plunged since the end of 2014, and manufacturing PMIs reached an all-time low of 30.2 in July, only slightly recovering in the following months, but still averaging 37.5 over the third quarter. This is close to the previous low in Q1 2009 (39 monthly average), when GDP contracted 4.7% q-o-q. Overall, we expect GDP to contract significantly in Q3, and fall by 1.3% in 2015 as a whole.

Despite that, having already lost over a quarter of the country's GDP in real terms since 2008, the economy appears to have bottomed out and, after the contraction in H2 2015, quarterly growth rates should start to stabilise. The unemployment rate continues to fall, albeit slowly (25.2% in Q2 2015). Manufacturing PMIs recovered in October to 47.3, which is broadly in line with the Q2 average. Industrial production in August was 4.5% higher than the previous year's level, near the peak reached in November 2014 in terms of yearly growth. However, credit conditions have deteriorated due to the liquidity squeeze affecting the banking sector, and, in particular, loans to firms reverted deeply into negative territory in September (-5.8% y-o-y) after being in positive territory in the first half of the year – and it is unlikely the situation will improve until banks have been fully recapitalised. This should continue to weigh on the domestic recovery. Exports so far have performed poorly (-3.5% in the year to August), but the even bigger contraction in imports (-10.4%) has led to a small improvement in the trade balance, while tourism has been performing strongly. As imports recover, we do not see a significant high contribution from net exports to GDP growth in the future. All in all,

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due to the base effect from weak growth in H2 2015, we expect Greece's GDP to contract by another 1.2% in 2016, even if quarterly growth rates should return to positive ground, and then grow by 2.4% in 2017.

On the fiscal front, the budget execution figures up to September show a slightly higher deficit than in 2014 (EUR1.8bn vs EUR1.1bn). Revenues are 8% lower than last year (and 5.6% below target). However, public spending was also 8.5% below last year, but, as acknowledged by the Ministry of Finance, much is due to the build-up of arrears and "after the gradual stabilisation of cash flow conditions, the expenditure will gradually revert to the levels of budget targets". This should leave a significant shortfall due to weak revenues. In light of this, in the new programme of financial assistance the targets for the primary surplus targets were revised down to -0.25% of GDP in 2015 (vs 3% in the previous programme), 0.5% in 2016, 1.75% in 2017 and 3.5% in 2018. This is still a substantial fiscal tightening, particularly if the economy were to underperform. The lower-than-expected contraction in GDP should make it easier to meet the primary deficit target for 2015 (-0.25% of GDP) but more austerity will be needed in the following years to meet the subsequent deficit targets (0.5% in 2016, 1.75% in 2017, and 3.5% in 2018), which could have a negative drag on growth.

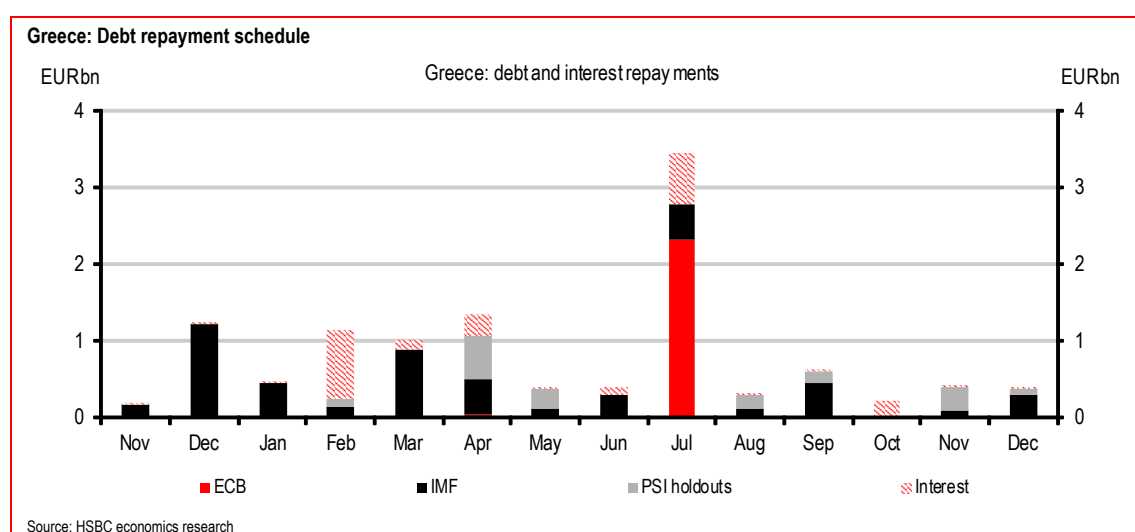
Of the EUR86bn of financial assistance agreed by the Eurogroup on 14 August, only EUR13bn was disbursed immediately to allow Greece to meet imminent payment obligations (and another EUR10bn was made available to the HFSF for the initial phase of the bank recapitalisation). Another EUR3bn could be made available before the first review is completed, provided Greece has carried out a series of actions agreed by the Eurogroup. The European Commission said recently that it was satisfied with the progress made so far, but no further disbursement has been made yet.

The first review was expected to be completed by the autumn, but there are still many challenges ahead and delays are likely. The government is expected to make sufficient progress on the medium-term budgetary plan, labour market and pension reforms, and the establishment of a privatisation fund with a target of assets to be privatised of EUR50bn (almost 30% of GDP). At the time of the first review, we also expect some

Key economic forecasts									
	2015	2016	2017	Q2 15	Q3 15	Q4 15	Q1 16	Q2 16	Q3 16
GDP	-1.3	-1.2	2.4	1.6	-3.4	-4.0	-4.0	-4.1	1.0
GDP (% quarter)	-	-	-	0.9	-4.2	-0.8	0.1	0.8	0.9
Consumer spending	-0.3	-1.3	1.7	2.5	-2.3	-3.0	-2.8	-3.6	0.2
Government consumption	2.3	-0.2	-0.9	2.3	3.5	4.5	2.2	-1.8	-0.1
Investment	-11.9	-6.5	11.3	-3.3	-19.1	-33.9	-26.4	-13.5	6.8
Stockbuilding (% GDP)	-0.1	0.0	0.1	-0.8	-1.1	-0.9	-0.9	-0.7	-0.4
Domestic demand	-0.9	-1.4	2.0	1.0	-2.4	-5.1	-4.6	-3.4	0.7
Exports	-1.3	4.6	6.1	-1.8	-4.0	-0.3	2.0	3.5	6.7
Imports	-1.3	3.3	6.4	-3.5	-4.1	-6.5	-3.1	3.1	7.6
Industrial production	-1.8	1.5	4.1	-2.9	-5.0	-1.1	-2.7	-0.8	0.7
Unemployment (%)	25.5	24.7	23.5	-	-	-	-	-	-
Wage growth	2.4	1.5	1.5	3.5	2.0	1.5	1.5	1.5	1.5
Consumer prices	-1.0	0.4	-0.3	-1.4	-0.6	0.1	1.0	0.4	0.0
Current account (USDbn)	1.5	1.8	1.8	-	-	-	-	-	-
Current account (% GDP)	0.8	1.0	1.0	-	-	-	-	-	-
Budget balance (% GDP)	-3.9	-3.2	-2.9	-	-	-	-	-	-
Gross external debt (% GDP)	252	248	243	-	-	-	-	-	-
Gross government debt (% GDP)	184	195	193	-	-	-	-	-	-
USD/EUR*	1.1	1.2	1.2	-	-	-	-	-	-
3-month money (%)*	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
10-year bond (%)*	-	-	-	-	-	-	-	-	-

Source: Thomson Reuters Datastream, HSBC estimates

difficult discussions on debt restructuring, a key precondition for the IMF to take part in the programme. A combination of extension of maturities and longer grace periods on all EU loans could be enough for the IMF to be on board, while also avoiding an upfront haircut on the debt, which is opposed by the Eurogroup. Greece does not face imminent debt repayments, other than the monthly repayments to the IMF, and there is no hard deadline until, possibly, a EUR3bn debt and interest repayment to the ECB in July 2016. Until the first review, we also won't see any payment to Greece beyond what is strictly needed to repay the debt, which will make it difficult to clear public sector arrears or go back to invest (public investment is down 40% in the year to September from 2014) which could help re-start the economy.



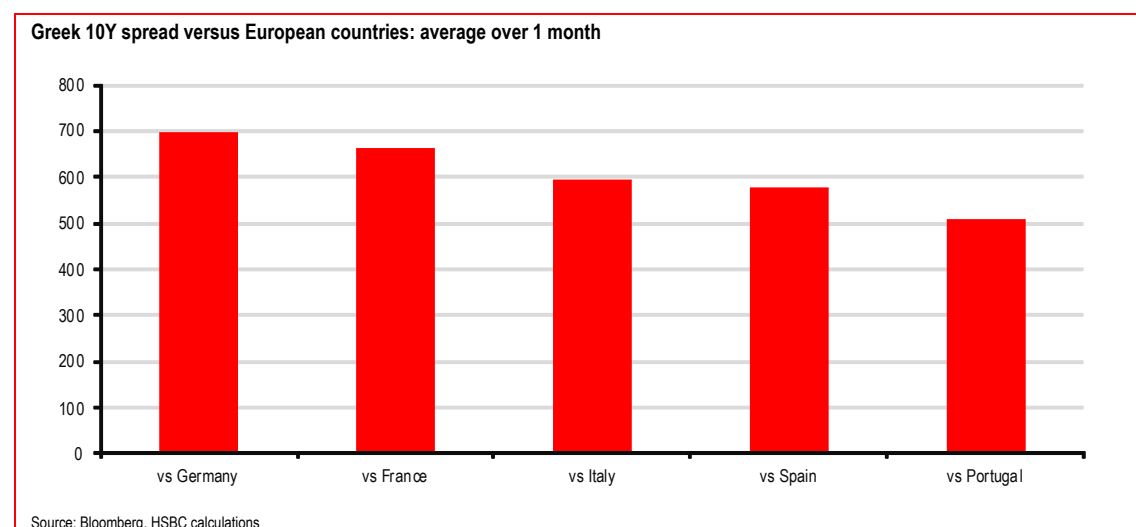
On the political front, the leftist party Syriza won a clear victory in the Greek snap general election on 20 September, but fell just short of an outright majority, obtaining 145 seats in the 300-seat parliament. Alexis Tsipras was re-elected Prime Minister, and Syriza was joined again by the right-wing party ANEL (Independent Greeks), with 10 MPs, to form a coalition government. Euclid Tsakalotos was confirmed as finance minister. The government has a very thin parliamentary majority of 5 MPs. Syriza should be more cohesive, with the dissident MPs having left the party to form a new, anti-euro formation, which failed to meet the 3% threshold for entering parliament. But with a dense list of structural reforms to be approved, including on sensitive issues such as the pension and labour market, divergences within the party could re-emerge. The Independent Greek party differs from Syriza on many aspects of domestic politics, from immigration to religion, which could cause difficulties.

Recent experience, however, would warrant some caution

Similarly to our ROA analysis, much of the above discussion by Fabio Balboni forms our base case for the economic outlook and can in many ways be thought of as a “if all goes according to plan” scenario. From a top-down perspective, however, recent experience would warrant some caution. Since the onset of the crisis, Greece has gone through four sets of elections, one referendum, three economic adjustment programmes (one still ongoing), numerous reshuffles of the government cabinet and passed more deadlines than we would wish to list here. Given the socioeconomic adjustment that has been required, we would not think that any of the above should necessarily be surprising.

With an overwhelming majority of the electorate and MPs supporting the third adjustment programme, there is reason to believe that stability and implementation has finally arrived in Greece. After all, our base case is that it all goes according to plan, with deposits returning to the system, a successful conclusion of the first programme review, allowing the ECB to reinstate the eligibility of collateral for normal operations, and the economy steadily improving. The simple fact of life though is that, over the past few years, the timing of implementation has generally slipped and a potential Grexit² has been a market concern more than once. We thus think it appropriate to incorporate some impact on the investment case for the higher potential for negative surprises given the relatively fragile nature of the Greek post crisis recovery.

The problem, however, is how to quantify an impact. One approach would be to turn to the debt markets for assistance. From a probability of default perspective, current bond prices seem to imply a very low level. If, instead we look at yields, 10-year Greek government bonds (GGBs) are trading at an average spread of c600bp above other European countries (see graph below). Even when compared with arguably its closest peer, the spread of Greek 10Y GGBs versus the equivalent Portuguese has averaged 507bp over the past month and is, at the time of writing, at c477bp. We could use this as a proxy for the spread to the risk-free rate and increase the cost of equity.



² See [Unfinished business](#), 16 July 2015 page 26, for a discussion of how we think Greece would fare outside of the eurozone.

There are, however, a number of issues with this approach, in our view. The bond market is very quick to incorporate developments and we thus fear that it is not reflective of very long-term risks and opportunities. After all, equity duration is much longer than for bonds. More importantly, though, any adjustment we make to the investment case would have to be made versus the base case of everything going according to plan. We doubt that the 10Y GGBs spread versus Portugal is simply reflective of the higher risk versus baseline implementation, as it might also for example incorporate the probability of a further orderly debt restructuring that could actually be beneficial for the economy and thus the investment case.

An alternative would be to create an elaborate bear case scenario where Greek banks are impacted by further turmoil in the Greek economy. We would argue that part of that is already reflected in the individual capital requirements we use. The buffer we incorporate for future stress tests could very well be thought of as a buffer for future stress. In part, however, the real question would not be how severe the outcome of a bear case would be for Greek banks (we might as well attach a zero value), but how likely it is in the long term. And, from an analytical standpoint, that question remains unanswered.

For lack of a better alternative, we include:

- ▶ A common 10% discount to reflect near-term uncertainties relating to the successful conclusion of the first programme review and the reestablishment of the ECB waiver on Greek collateral.
- ▶ A 300bp higher cost of equity than European peers (half of the average GGBs spread to European peer countries) to incorporate longer-term top-down concerns on the macro and political front.

The above, however, fails to capture the bank-specific stock overhang that would arise from: (a) state ownership, as the HFSF would eventually need to sell down its position longer term; and potentially (b) near term, the sell-down of stock ownership from holders of debt that either participated in the LMEs or was converted to equity through burden-sharing, and do not have a mandate that allows them to hold equity. We have discussed the recapitalisation structure in the previous section, while ownership structure post the capital increases is assessed in the next chapter as it involves assumptions about the issuance price for new shares. It is important to note, however, that we believe that banks with larger long-term positions from holders with a mandate to sell (ie the HFSF) should carry a discount proportionate to the size of that holding. The near-term stock overhang from debt investors' holdings should also be relevant but, given its short-term nature, we believe it should carry less weight. We incorporate both in the discount we use in our valuation by using a 0.30x multiplier on state ownership and a 0.05x multiplier on debt investor ownership. The exact methodology is set out in the next chapter.

Valuation in the face of recapitalisation

- ▶ We take a conservative view on valuation and include discounts for top-down uncertainties and stock overhang
- ▶ The upcoming recapitalisation will apportion value between existing and prospective shareholders; we assume a 30% discount and provide sensitivities
- ▶ We see upside in Alpha Bank shares; the upcoming recapitalisation also looks attractive for Piraeus, but our estimates imply little room for upside for current shares

The basic structure of our valuation methodology is similar to that which we use for other European banks. However, this is adjusted for (a) the complexities caused by the upcoming recapitalisation and (b) the view we take on top-down concerns, as explained in the previous section. Given that Greek banks are unlikely to face a normalised environment for a number of years, we also look through to our 2018e estimates for valuation purposes. We use a 1% long-term growth rate and a 12% cost of equity, 300bp above the 9% we use for other domestically focused European banks, as previously explained.

Greek banks: Basic valuation assumptions

	ACB	BOP
Base Year	2018	2018
Long-term growth rate	1%	1%
Cost of Equity	12%	12%

Source: HSBC estimates

We estimate excess capital as of 2018e. Our required CET1 ratios are based on our previous analysis of capital requirements and target capital ratios. We also exclude any government-owned hybrids (a “required capital buffer” for CoCos, preference shares) from our estimates of excess capital as we assume those would need to be paid first before any excess capital is distributed.

Excess capital calculation (EURm)

	ACB	BOP
CET1% 2018e	20.3%	20.2%
Required CET1%	12.3%	12.5%
RWAs 2018e	54,000	56,502
Excess Capital 2018e	4,308	4,376
minus CoCos and state Prefs. 2018e	0	2,040
Net Excess Capital 2018e (A)	4,308	2,336

Source: HSBC estimates

We then adjust our 2018e tangible book estimates for excess capital and value the remainder based on a warranted equity valuation (WEV) model and our 2018 net profit estimates. The fair value on WEV is then added to our excess capital estimated and discounted back to today. To that we add the net present value of any dividends within our forecast horizon to reach a target market capitalisation before any discount. It is important to note that this target market capitalisation includes the funds of the upcoming capital increases and should not be compared with the current market capitalisation.

Target market capitalisation before discount (EURm)

	ACB	BOP
TBV 2018e	11,136	9,805
TBV post excess capital 2018e	6,829	7,469
Net Income 2018e	885	629
ROTE 2018e	13.0%	8.4%
WEV	1.1	0.7
Fair value on WEV (B)	7,422	5,040
Total 2018e Fair value (A) + (B)	11,730	7,376
Discount years	3.1	3.1
Total fair value discounted to today	8,221	5,170
NPV dividends	252	179
Target market cap before discount	8,473	5,349

Source: HSBC estimates

To the above target market capitalisation we apply:

- ▶ A common 10% discount to reflect near-term uncertainties relating to the successful conclusion of the first programme review and the re-establishment of the ECB waiver on Greek collateral.
- ▶ A discount for stock overhang based on: (a) our assumed overhang multipliers as discussed in the previous section (0.30x negative multiplier on state ownership and 0.05x negative multiplier on debt investor ownership); and (b) the ownership structure post the capital increases.

Common and ownership structure discounts		
	ACB	BOP
Common discount (1)	10%	10%
Ownership structure:		
Public sector	16%	29%
Private sector	84%	71%
o/w previously debt holders	29%	20%
Overhang multipliers:		
state ownership	0.30	0.30
debt investor ownership	0.05	0.05
Ownership structure discount (2)	6%	10%
Total Discount (1) + (2)	16.4%	19.7%

Source: HSBC estimates

The ownership structure, however, will evidently depend on the subscription price for the upcoming capital increases. We have assumed a common 30% discount to the current share price for all banks based on recent experience in capital increases from European banks. We present a sensitivity to our assumptions of a 30% capital increase discount, a 10% common discount, a 0.30x state ownership multiplier and a 0.05x debt investor multiplier in a series of tables at the end of this chapter.

Once we adjust the target market capitalisation before the discount by the above estimated discount, we reach a total target market capitalisation. Based on our estimated ownership structure, we estimate what portion of that total target market capitalisation is attributable to existing shareholders (private and HFSF). We then divide the target market capitalisation that is attributable to existing shareholders by the current number of shares outstanding to derive our target price.

Greek banks: Estimated target price (EUR)		
	ACB	BOP
Total target Market Cap	7,085	4,296
Target PTBV	0.64	0.44
% owned by current shareholders	25%	9%
Owned by current shareholders	1,753	374
Target Price	0.137	0.061
Upside / Downside vs current price (close 6 November)	37%	2%
Assumed capital increase discount	30%	30%
Assumed issuance price	0.070	0.042
Upside to target price for prospective investors	96%	45%

Source: HSBC estimates

The above also gives rise to an estimated target market capitalisation attributable to those that will participate in the upcoming capital increase, either through the LMEs, the book-building process, burden sharing or the state. This can be compared with our assumed issuance price in order to estimate potential upside/ downside for prospective investors. Evidently, given the embedded discount, there is more value in participating in the upcoming capital increases than investing in existing shares. Our target prices, however, are obviously set against the publicly traded shares.

Based on the above, we see upside for current shareholders of Alpha Bank, whereas the upcoming recapitalisation also looks attractive for Piraeus.

Target price sensitivity to discount assumptions (EUR)

ACB													
Common discount	0.137	Capital increase discount						0.137	State ownership discount multiplier				
		20%	25%	30%	35%	40%			0.10	0.20	0.30	0.40	0.50
	0%	0.169	0.161	0.154	0.146	0.137	Debt	0.00	0.145	0.142	0.140	0.137	0.134
	5%	0.160	0.153	0.145	0.138	0.130	investor	0.05	0.143	0.140	0.137	0.135	0.132
	10%	0.151	0.144	0.137	0.130	0.123	ownership	0.10	0.140	0.138	0.135	0.132	0.129
	15%	0.142	0.135	0.129	0.122	0.115	discount	0.15	0.138	0.135	0.132	0.130	0.127
	20%	0.133	0.127	0.121	0.115	0.108	multiplier	0.20	0.135	0.133	0.130	0.127	0.125

BOP													
	0.061	Capital increase discount						0.061	State ownership discount multiplier				
		20%	25%	30%	35%	40%			0.10	0.20	0.30	0.40	0.50
Common discount	0%	0.078	0.073	0.069	0.064	0.060	Debt	0.00	0.067	0.064	0.062	0.060	0.058
	5%	0.073	0.069	0.065	0.061	0.057	investor	0.05	0.066	0.064	0.061	0.059	0.057
	10%	0.069	0.065	0.061	0.057	0.053	ownership	0.10	0.065	0.063	0.061	0.058	0.056
	15%	0.065	0.061	0.058	0.054	0.050	discount	0.15	0.064	0.062	0.060	0.058	0.055
	20%	0.061	0.057	0.054	0.050	0.047	multiplier	0.20	0.063	0.061	0.059	0.057	0.055

Source: HSBC estimates

Company profiles

Alpha Bank

- ▶ Alpha Bank should see the biggest improvement in ROA, with 2018e ROA jumping to 1.30% based on our estimates
- ▶ Coupled with an above cost of equity 13.0% ROTE in 2018e post excess capital, we see upside for existing shares
- ▶ We initiate coverage with a Buy rating and a EUR0.137 target price

Following the acquisition of Emporiki Bank from Credit Agricole and Citi banks operations in Greece, Alpha Bank has become the second largest bank domestically behind Piraeus. Its domestic loan book is biased towards larger corporates, with a relatively smaller exposure to SMEs and mortgages. It also has significant exposure to Romania (5.8% loan market share), Albania (8.6%), Serbia (4.6%), and Cyprus (4.6%).

We believe Alpha Bank is poised to benefit the most from a normalisation in interbank funding. Given its lower exposure to domestic small corporates, we also think that loan pricing and asset quality headwinds are likely to be relatively less. Benefits from fees should be in line with the market, while we think there is still room to reduce the domestic footprint. Asset quality trends have traditionally been stronger than peers, providing us with more confidence on the outlook for provisions and the rundown of the doubtful loans portfolio, albeit uncertainty remains high. Alpha has also concluded an agreement on NPL servicing with a dedicated international player, Spain's Aktua, which could accelerate the work-out of the doubtful portfolio. As a result, we expect Alpha Bank to see the biggest improvement in ROA, with 2018e ROA jumping to 1.30%.

Alpha Bank: Disaggregation of returns and comparison with current and historical levels (% of ATA)

	2018	vs 2015	vs 2008
Net Interest Income	3.14%	+0.39%	+0.14%
Other Revenue	0.81%	+0.21%	-0.11%
Total Revenue	3.95%	+0.61%	+0.03%
Costs	-1.57%	+0.08%	+0.40%
Operating profit	2.38%	+0.68%	+0.43%
LLPs	-0.54%	+3.14%	+0.36%
Other	-0.54%	-1.48%	-0.35%
ROA	1.30%	+2.35%	+0.44%

Source: HSBC estimates

Near term, we see headwinds from stock overhang, as both state and debt-investor ownership would be high based on our recapitalisation assumptions. But the bank should remain in private hands, with over 80% private-sector ownership. Coupled with an above cost of equity 13.0% ROTE in 2018e post excess capital, we see upside for the existing shares. Our EUR0.137 target price implies 37% upside to the current share price and we initiate coverage with a Buy rating. Based on the assumption of a 30% discount in the upcoming capital increase, we think the upcoming recapitalisation should look attractive.

Downside risks include (1) size, pricing and participation in the upcoming capital increase; (2) a further significant deterioration in the economy, leading to a reduction in the value of the doubtful assets portfolio; and (3) a lower than expected improvement in cost efficiency

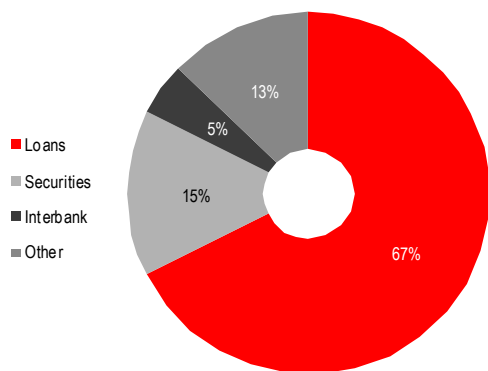
Alpha Bank: Main valuation metrics

EUR	2011	2012	2013	2014	2015e	2016e	2017e	2018e
EPS	-7.13	-2.04	0.45	-0.03	-0.02	0.01	0.01	0.02
EPS core	-0.86	-2.04	0.10	-0.03	-0.02	0.01	0.01	0.02
BVPS	2.65	1.10	0.76	0.60	0.19	0.20	0.21	0.22
TBVPS	2.31	0.84	0.74	0.57	0.18	0.19	0.21	0.22
DPS	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.01
P/E x	0.0	0.0	0.2	-3.7	-4.1	11.0	6.7	5.8
P/E Core x	-0.1	0.0	1.0	-3.4	-4.4	11.0	6.7	5.8
P/BV	0.0	0.1	0.1	0.2	0.5	0.5	0.5	0.4
P/TBV	0.0	0.1	0.1	0.2	0.6	0.5	0.5	0.5
Yield	0%	0%	0%	0%	0%	0%	0%	7%

Source: HSBC estimates

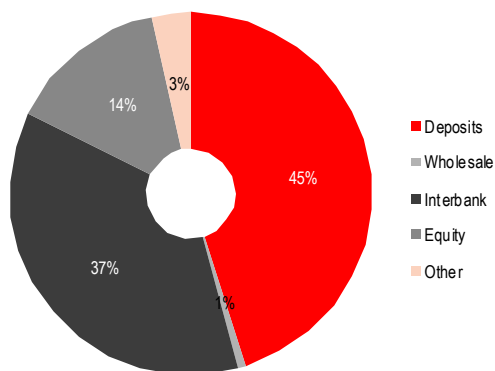
Alpha Bank in figures

Asset mix (2015e)



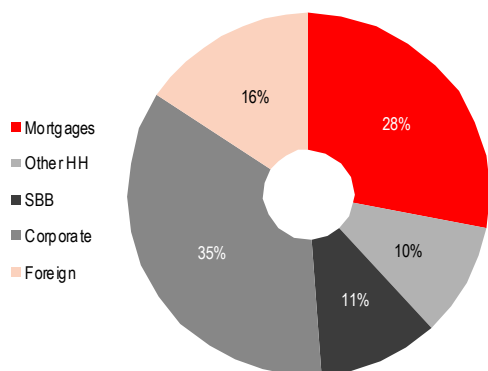
Source: HSBC estimates

Liability mix (2015e)



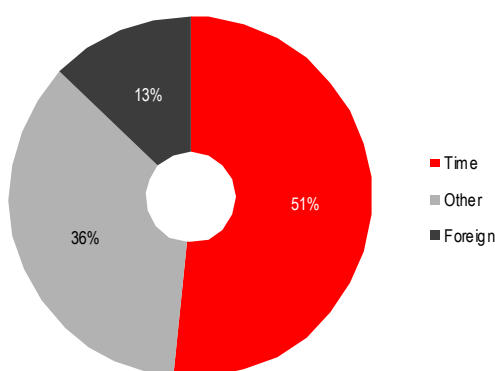
Source: HSBC estimates

Loan split (2014a)



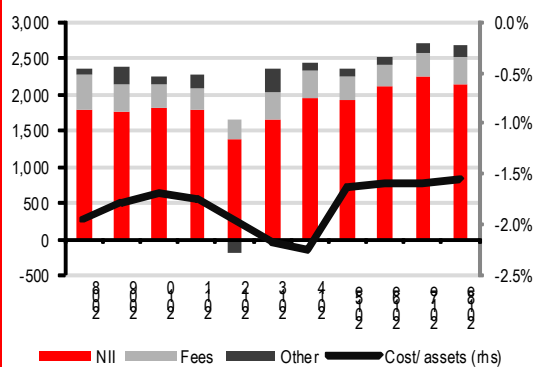
Source: Company data, HSBC calculations

Deposit split (2014a)



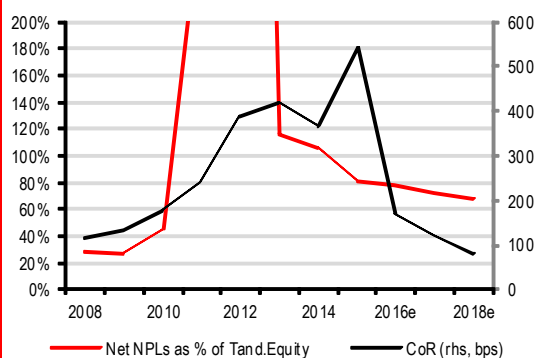
Source: Company data, HSBC calculations

Revenue structure (EURm) and cost efficiency



Source: Company data, HSBC estimates

Asset quality



Source: Company data, HSBC estimates

Financials & valuation: Alpha Bank

Buy

Financial statements				
Year to	12/2014a	12/2015e	12/2016e	12/2017e
P&L summary (EURm)				
Net interest income	1,939	1,936	2,117	2,237
Net fees/commissions	397	312	299	346
Trading profits	41	54	59	83
Other income	56	51	48	45
Total income	2,433	2,352	2,523	2,711
Operating expense	-1,645	-1,157	-1,084	-1,071
Bad debt charge	-1,853	-2,596	-777	-545
Other	0	0	0	0
HSBC PBT	-1,066	-1,401	661	1,095
Exceptionals	40	-89	0	0
PBT	-1,025	-1,490	661	1,095
Taxation	696	702	-192	-317
Minorities + preferences	0	0	-3	-4
Attributable profit	-330	-787	467	773
HSBC attributable profit	-358	-725	467	773
Balance sheet summary (EURm)				
Ordinary equity	7,652	9,697	10,164	10,937
HSBC ordinary equity	7,652	9,697	10,164	10,937
Customer loans	49,557	46,413	45,057	45,699
Debt securities holdings	10,298	10,143	10,143	10,143
Customer deposits	42,901	30,888	36,139	36,862
Interest earning assets	66,591	63,249	60,022	59,665
Total assets	72,935	68,591	67,245	67,905
Capital (%)				
RWA (EURm)	52,800	51,786	51,106	52,966
Core tier 1	14.3	17.8	18.9	19.7
Total tier 1	14.3	17.8	18.9	19.7
Total capital	14.6	17.8	18.9	19.7
Ratio, growth & per share analysis				
Year to	12/2014a	12/2015e	12/2016e	12/2017e
Year-on-year % change				
Total income	3.8	-3.3	7.3	7.4
Operating expense	15.4	-29.7	-6.3	-1.2
Pre-provision profit	-14.2	51.8	20.4	13.9
EPS	-106.0	-8.5	-137.0	65.5
HSBC EPS	-128.3			65.5
DPS				
NAV (including goodwill)	-21.3	-68.6	4.8	7.6
Ratios (%)				
Cost/income ratio	67.6	49.2	43.0	39.5
Bad debt charge	3.7	5.4	1.7	1.2
Customer loans/deposits	115.5	150.3	124.7	124.0
NPL/loan	33.0	37.0	38.4	37.7
NPL/RWA	39.0	44.2	45.6	43.6
Provision to risk assets/RWA	24.2	29.6	30.6	29.2
Net write-off/RWA	0.0	0.0	0.0	0.0
Coverage	62.1	67.0	67.0	67.0
ROE (including goodwill)	-4.5	-8.4	4.7	7.3
Per share data (EUR)				
EPS reported (diluted)	-0.03	-0.02	0.01	0.01
HSBC EPS (diluted)	-0.03	-0.02	0.01	0.01
DPS	0.00	0.00	0.00	0.00
NAV	0.57	0.18	0.19	0.21
NAV (including goodwill)	0.60	0.19	0.20	0.21

Core profitability (% RWAs) and leverage				
Year to	12/2014a	12/2015e	12/2016e	12/2017e
Net interest income	3.7	3.7	4.1	4.3
Trading profits	0.1	0.1	0.1	0.2
Other income	0.1	0.1	0.1	0.1
Operating expense	-3.2	-2.2	-2.1	-2.1
Pre-provision profit	1.5	2.3	2.8	3.2
Bad debt charge	-3.6	-5.0	-1.5	-1.0
HSBC attributable profit	-0.7	-1.4	0.9	1.5
Leverage (x)	6.5	6.0	5.2	4.9
Return on average tier 1	-4.7	-7.9	4.8	7.4

Valuation data				
Year to	12/2014a	12/2015e	12/2016e	12/2017e
PE*			10.7	6.5
Pre-provision multiple	1.5	2.6	3.5	3.1
P/NAV	0.2	0.5	0.5	0.5
Dividend yield (%)	0.0	0.0	0.0	0.0

* Based on HSBC EPS (diluted)

Issuer information			
Share price (EUR)0.10		Target price (EUR)0.14	
Reuters (Equity)	ACBr.AT	Bloomberg (Equity)	ALPHA GA
Market cap (USDm)	1,330	Market cap (EURm)	1,239
Free float (%)	34%		
Country	Greece	Sector	Commercial Banks
Analyst	Jason Kepaptsoglou	Contact	+44 20 7991 6722

Notes: Priced at close of 06 Nov 2015

Piraeus Bank

- ▶ Headwinds from corporate loan pricing and asset quality will eventually bite, leaving Piraeus behind peers, we believe
- ▶ With 71% of ownership in private hands based on our assumptions, Piraeus will suffer less from stock overhang
- ▶ We initiate coverage with a Hold rating and a EUR0.061 target price and think the upcoming recapitalisation should look attractive

Following a series of acquisitions throughout the crisis – ATEbank, Geniki, Greek operations of Cypriot banks and Millennium Bank Greece – Piraeus has become the biggest bank in Greece, with a c30% share of gross loans. The bank is also present in various SEE countries, with an over 5% market share only in Albania. As such, it is also the most domestically focused Greek bank.

We expect Piraeus to have a better cost performance than domestic peers due to efficiencies arising from the concentrated nature of its exposure. We also think that cost of risk will not be dissimilar to peers. The lower profitability that we forecast is thus purely attributable to revenue margins. On the net interest income side, we think that headwinds from corporate loan pricing will penalise net interest margins. We also think that a relatively larger exposure to doubtful assets creates a bigger drag from funding costs. Given the sensitivity of returns and equity to movements in the doubtful loans portfolio, we also see Piraeus as the most leveraged play on recovery values for the banks' doubtful assets.

Piraeus Bank: Disaggregation of returns and comparison with current and historical levels (% of ATA)

	2018	vs 2015	vs 2008
Net Interest Income	2.36%	+0.16%	+0.05%
Other Revenue	0.66%	+0.08%	-0.35%
Total Revenue	3.02%	+0.24%	-0.30%
Costs	-1.44%	+0.08%	+0.34%
Operating profit	1.58%	+0.32%	+0.04%
LLPs	-0.52%	+2.19%	+0.25%
Other	-0.31%	-1.08%	-0.17%
ROA	0.74%	+1.43%	+0.12%

Source: HSBC estimates

This view is reinforced when we look at why our estimates are well below management's targets: we expect a bigger drag on the P&L from the doubtful assets portfolio both on the top line and on costs. On the top line, we expect pricing pressures on corporate loans and the funding cost of the doubtful assets portfolio to depress margins, with NIM standing at 2.36% in 2018, well below management's target of >3%. We are also well below management's 0.90% fee margin target but still expect Piraeus to cover c49% of the distance between

Q3 2015 margins and 2008 levels. Based on our 2018 estimates, Piraeus also ends up with the best cost-to-assets ratio at 1.44%, but that is still worse than management's <1.40% target. The absolute cost base is also c20% higher than management's estimates due to the drag from the doubtful loans portfolio.

Our EUR0.061 target price implies 1.7% upside to the current share price and we initiate coverage with a Hold rating. Based on the assumption of a 30% discount in the upcoming capital increase, we think the upcoming recapitalisation should look attractive.

Upside risks include (1) significant recoveries arising from the doubtful assets portfolio; (2) a stronger than expected recovery in fees given the enhanced footprint post-consolidation; (3) a faster rundown of doubtful assets reducing the drag on profitability.

Downside risks include (1) size, pricing and participation in the upcoming capital increase; (2) a further significant deterioration in the economy, leading to a reduction in the value of the doubtful assets portfolio; and (3) a lower than expected improvement in cost efficiency.

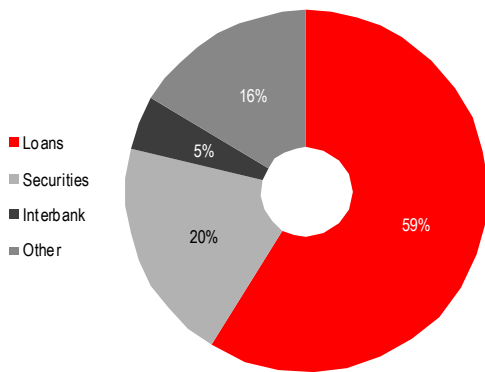
Piraeus Bank: Main valuation metrics

EUR	2011	2012	2013	2014	2015e	2016e	2017e	2018e
EPS	-6.11	-0.44	0.93	-0.34	-0.02	0.00	0.01	0.01
EPS Core	-2.29	-0.47	-0.05	-0.34	-0.02	0.00	0.01	0.01
BVPS	-2.47	-2.80	1.51	1.18	0.13	0.14	0.14	0.14
TBVPS	-2.75	-3.15	1.45	1.13	0.13	0.13	0.14	0.14
DPS	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
P/E x	0.0	-0.1	0.1	-0.2	-3.8	13.8	6.9	6.7
P/E core x	0.0	-0.1	-1.3	-0.2	-3.8	13.8	6.9	6.7
P/BV	0.0	0.0	0.0	0.1	0.5	0.4	0.4	0.4
P/TBV	0.0	0.0	0.0	0.1	0.5	0.5	0.4	0.4
Yield	0%	0%	0%	0%	0%	0%	0%	0%

Source: HSBC estimates

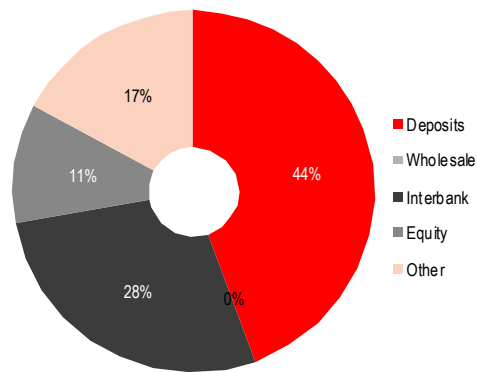
Piraeus Bank in figures

Asset mix (2015e)



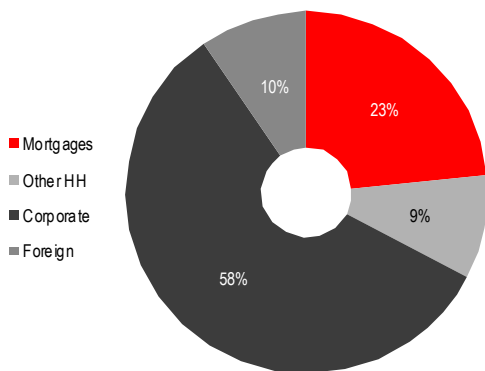
Source: HSBC estimates

Liability mix (2015e)



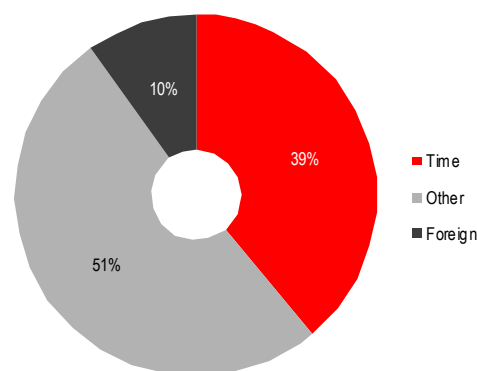
Source: HSBC estimates

Loan split (2014a)



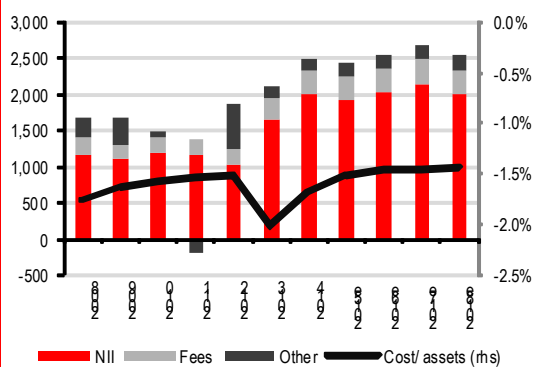
Source: Company data, HSBC calculations

Deposit split (2014a)



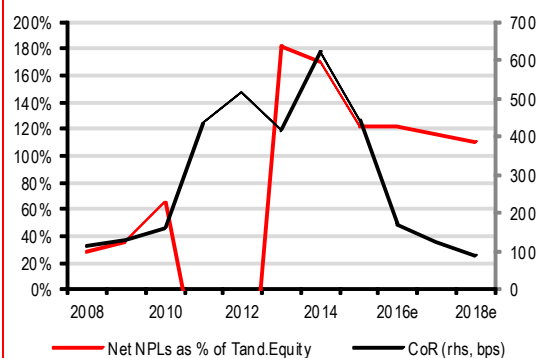
Source: Company data, HSBC calculations

Revenue structure (EURm) and cost efficiency



Source: Company data, HSBC estimates

Asset quality



Source: Company data, HSBC estimates

Financials & valuation: Piraeus Bank SA

Hold

Financial statements				
Year to	12/2014a	12/2015e	12/2016e	12/2017e
P&L summary (EURm)				
Net interest income	2,000	1,926	2,027	2,133
Net fees/commissions	333	312	323	362
Trading profits	-29	88	101	117
Other income	185	111	84	81
Total income	2,490	2,437	2,535	2,692
Operating expense	-1,533	-1,337	-1,252	-1,232
Bad debt charge	-3,718	-2,377	-851	-595
Other	-286	-90	0	0
HSBC PBT	-3,047	-1,368	432	864
Exceptionals	9	11	0	0
PBT	-3,038	-1,356	432	864
Taxation	1,068	758	-125	-251
Minorities + preferences	7	1	-2	-3
Attributable profit	-1,963	-597	305	610
HSBC attributable profit	-1,969	-605	305	610
Balance sheet summary (EURm)				
Ordinary equity	7,210	9,327	9,469	9,916
HSBC ordinary equity	7,210	9,327	9,469	9,916
Customer loans	57,143	50,908	49,159	48,438
Debt securities holdings	16,961	17,217	17,217	17,217
Customer deposits	54,831	38,382	43,909	44,787
Interest earning assets	81,092	76,548	73,175	71,940
Total assets	89,290	86,499	84,828	84,160
Capital (%)				
RWA (EURm)	55,720	57,089	55,986	55,546
Core tier 1	12.4	18.6	19.2	20.2
Total tier 1	12.4	18.6	19.2	20.2
Total capital	12.5	18.6	19.2	20.2
Ratio, growth & per share analysis				
Year to	12/2014a	12/2015e	12/2016e	12/2017e
Year-on-year % change				
Total income	18.2	-2.1	4.0	6.2
Operating expense	-6.4	-12.8	-6.4	-1.7
Pre-provision profit	104.0	14.9	16.7	13.8
EPS	-136.1	-95.3	-127.8	99.9
HSBC EPS				99.9
DPS				
NAV (including goodwill)	-22.0	-88.7	1.5	4.7
Ratios (%)				
Cost/income ratio	61.6	54.9	49.4	45.8
Bad debt charge	6.2	4.4	1.7	1.2
Customer loans/deposits	104.2	132.6	112.0	108.2
NPL/loan	37.8	41.3	43.1	43.2
NPL/RWA	49.5	49.3	51.3	51.2
Provision to risk assets/RWA	28.4	30.1	31.3	31.2
Net write-off/RWA	0.0	0.0	0.0	0.0
Coverage	57.4	61.0	61.0	61.0
ROE (including goodwill)	-26.4	-7.3	3.2	6.3
Per share data (EUR)				
EPS reported (diluted)	-0.34	-0.02	0.00	0.01
HSBC EPS (diluted)	-0.34	-0.02	0.00	0.01
DPS	0.00	0.00	0.00	0.00
NAV	1.13	0.13	0.13	0.14
NAV (including goodwill)	1.18	0.13	0.14	0.14

Core profitability (% RWAs) and leverage				
Year to	12/2014a	12/2015e	12/2016e	12/2017e
Net interest income	3.5	3.4	3.6	3.8
Trading profits	-0.1	0.2	0.2	0.2
Other income	0.3	0.2	0.1	0.1
Operating expense	-2.7	-2.4	-2.2	-2.2
Pre-provision profit	1.7	1.9	2.3	2.6
Bad debt charge	-6.5	-4.2	-1.5	-1.1
HSBC attributable profit	-3.4	-1.1	0.5	1.1
Leverage (x)	7.7	6.8	6.0	5.8
Return on average tier 1	-28.5	-5.7	2.8	5.4
Valuation data				
Year to	12/2014a	12/2015e	12/2016e	12/2017e
PE*			12.8	6.4
Pre-provision multiple	0.3	1.9	3.1	2.7
P/NAV	0.0	0.4	0.4	0.4
Dividend yield (%)	0.0	0.0	0.0	0.0
* Based on HSBC EPS (diluted)				
Issuer information				
Share price	(EUR)0.06	Target price	(EUR)0.06	
Reuters (Equity)	BOPr.AT	Bloomberg (Equity)	TPEIR GA	
Market cap (USDm)	367	Market cap (EURm)	342	
Free float (%)	33%			
Country	Greece	Sector	Commercial Banks	
Analyst	Jason Kepaptsoglou	Contact	+44 20 7991 6722	
Notes: Priced at close of 06 Nov 2015				

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Banks' monitor

Du Pont analysis

Disaggregation of returns into underlying drivers: sector

Profit drivers (% of average tangible assets 2010-2014 average)			Leverage drivers and resulting profitability 2010-2014 average		
	ACB	BOP		ACB	BOP
Net Interest Income	2.61%	2.08%	ROA	-0.81%	-1.88%
Other Revenue	0.66%	0.62%	RWAs % Assets	78%	69%
Total Revenue	3.27%	2.69%	Core Tier 1 %	10.3%	7.3%
Costs	-1.96%	-1.68%	Core Tier 1 / Equity	188%	85%
Operating profit	1.31%	1.01%	Leverage	26	-14
LLPs	-2.28%	-2.86%			
Other	0.17%	-0.03%	RoTE	-32.1%	35.3%
2015e-2017e average			2015e-2017e average		
	ACB	BOP		ACB	BOP
Net Interest Income	3.07%	2.37%	ROA	0.26%	0.13%
Other Revenue	0.63%	0.61%	RWAs % Assets	76%	66%
Total Revenue	3.70%	2.98%	Core Tier 1 %	17.8%	18.1%
Costs	-1.61%	-1.49%	Core Tier 1 / Equity	111%	109%
Operating profit	2.09%	1.50%	Leverage	8	9
LLPs	-1.88%	-1.47%			
Other	0.06%	0.11%	RoTE	1.6%	0.6%
2018e			2018e		
	ACB	BOP		ACB	BOP
Net Interest Income	3.14%	2.36%	ROA	1.30%	0.74%
Other Revenue	0.81%	0.66%	RWAs % Assets	78%	66%
Total Revenue	3.95%	3.02%	Core Tier 1 %	19.5%	20.4%
Costs	-1.57%	-1.44%	Core Tier 1 / Equity	112%	110%
Operating profit	2.38%	1.58%	Leverage	7	8
LLPs	-0.54%	-0.52%			
Other	-0.54%	-0.31%	RoTE	9.4%	6.0%

Source: Company data, HSBC estimates

Disaggregation of returns into underlying drivers: by bank

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
ACB										
Profit drivers (% of average tangible assets)										
Net Interest Income	2.62%	2.67%	2.84%	2.36%	2.52%	2.65%	2.75%	3.13%	3.33%	3.14%
Other Revenue	0.92%	0.63%	0.80%	0.16%	1.04%	0.68%	0.59%	0.60%	0.70%	0.81%
Total Revenue	3.54%	3.31%	3.64%	2.52%	3.56%	3.33%	3.34%	3.73%	4.03%	3.95%
Costs	-1.79%	-1.69%	-1.75%	-1.97%	-2.17%	-2.25%	-1.64%	-1.60%	-1.59%	-1.57%
Operating profit	1.75%	1.62%	1.89%	0.55%	1.40%	1.08%	1.70%	2.13%	2.44%	2.38%
LLPs	-1.01%	-1.30%	-1.80%	-2.85%	-2.92%	-2.54%	-3.69%	-1.15%	-0.81%	-0.54%
Other	-0.16%	-0.10%	-0.02%	0.44%	-0.47%	0.99%	0.94%	-0.29%	-0.48%	-0.54%
Leverage drivers and resulting profitability										
ROA	0.58%	0.22%	0.07%	-1.86%	-2.00%	-0.47%	-1.05%	0.69%	1.15%	1.30%
RWAs % Assets	75%	74%	74%	87%	83%	71%	74%	76%	77%	78%
Core Tier 1 %	7.8%	8.1%	8.2%	8.0%	12.1%	15.2%	16.0%	18.3%	19.3%	20.0%
Core Tier 1 / Equity	98%	80%	122%	484%	154%	102%	100%	98%	98%	98%
Leverage	17	13	20	70	15	9	8	7	7	6
RoTE	9.7%	2.9%	1.5%	-129.4%	-30.9%	-4.5%	-8.9%	4.9%	7.6%	8.1%
BOP										
Profit drivers (% of average tangible assets)										
Net Interest Income	2.04%	2.17%	2.21%	1.73%	2.06%	2.21%	2.20%	2.38%	2.53%	2.36%
Other Revenue	1.05%	0.52%	0.03%	1.43%	0.55%	0.54%	0.58%	0.60%	0.66%	0.66%
Total Revenue	3.08%	2.69%	2.24%	3.16%	2.61%	2.76%	2.78%	2.97%	3.20%	3.02%
Costs	-1.65%	-1.59%	-1.55%	-1.53%	-2.03%	-1.70%	-1.53%	-1.47%	-1.46%	-1.44%
Operating profit	1.44%	1.10%	0.69%	1.63%	0.58%	1.06%	1.26%	1.50%	1.73%	1.58%
LLPs	-0.91%	-1.08%	-2.93%	-3.43%	-2.74%	-4.12%	-2.71%	-1.00%	-0.71%	-0.52%
Other	-0.16%	-0.06%	-0.42%	0.92%	-1.47%	0.88%	0.77%	-0.15%	-0.30%	-0.31%
Leverage drivers and resulting profitability										
ROA	0.37%	-0.04%	-2.65%	-0.88%	-3.63%	-2.18%	-0.69%	0.36%	0.73%	0.74%
RWAs % Assets	69%	68%	77%	73%	63%	64%	64%	66%	66%	66%
Core Tier 1 %	8.0%	8.3%	1.0%	2.0%	11.9%	13.1%	15.5%	18.9%	19.7%	20.2%
Core Tier 1 / Equity	116%	124%	-99%	-26%	322%	106%	110%	118%	117%	117%
Leverage	21	22	-130	-18	43	13	11	9	9	9
RoTE	7.8%	-0.8%	345.4%	15.5%	-155.8%	-27.6%	-7.6%	3.4%	6.5%	6.5%

Source: Company data, HSBC estimates

Quarterly monitor

Main P&L items

Net interest margin (bp)						Net interest income growth y/y					
	3Q14	4Q14	1Q15	2Q15	3Q15		3Q14	4Q14	1Q15	2Q15	3Q15
ACB	273	273	264	265	278	ACB	12%	2%	2%	-1%	-1%
BOP	233	233	221	215	217	BOP	12%	8%	3%	-6%	-7%
Revenue growth y/y						Operating costs growth y/y					
	3Q14	4Q14	1Q15	2Q15	3Q15		3Q14	4Q14	1Q15	2Q15	3Q15
ACB	13%	-8%	0%	-9%	-8%	ACB	56%	2%	-11%	-21%	-39%
BOP	1%	-2%	3%	-26%	10%	BOP	-12%	-23%	-5%	-8%	-9%
Credit costs annualized (bp)						Net income growth y/y					
	3Q14	4Q14	1Q15	2Q15	3Q15		3Q14	4Q14	1Q15	2Q15	3Q15
ACB	269	620	344	1372	219	ACB	-32%	122%	23%	-414%	-364%
BOP	1560	366	197	1169	192	BOP	457%	-53%	-69%	-731%	-132%

Source: Company data, HSBC estimates

Main balance sheet items

Loans (Y-o-Y growth rate)						Deposits (Y-o-Y growth rate)					
	3Q14	4Q14	1Q15	2Q15	3Q15		3Q14	4Q14	1Q15	2Q15	3Q15
ACB	-5%	-4%	-2%	-5%	-6%	ACB	4%	1%	-14%	-26%	-30%
BOP	-9%	-8%	-6%	-10%	-8%	BOP	1%	1%	-15%	-29%	-31%
Loan-to-Deposit ratio (%)						Funding Gap as a % of total assets					
	3Q14	4Q14	1Q15	2Q15	3Q15		3Q14	4Q14	1Q15	2Q15	3Q15
ACB	115%	116%	138%	153%	154%	ACB	9%	9%	19%	24%	24%
BOP	102%	104%	120%	137%	136%	BOP	1%	3%	10%	16%	16%
Loans (Q-o-Q growth rate)						Deposits (Q-o-Q growth rate)					
	3Q14	4Q14	1Q15	2Q15	3Q15		3Q14	4Q14	1Q15	2Q15	3Q15
ACB	0%	-1%	0%	-4%	-2%	ACB	3%	-1%	-16%	-14%	-2%
BOP	-4%	2%	-3%	-5%	-2%	BOP	1%	0%	-15%	-16%	-2%
Total assets growth y/y						Total assets growth q/q					
	3Q14	4Q14	1Q15	2Q15	3Q15		3Q14	4Q14	1Q15	2Q15	3Q15
ACB	-1%	-1%	0%	-2%	-4%	ACB	1%	1%	0%	-3%	-1%
BOP	-7%	-3%	-1%	-1%	-1%	BOP	-2%	3%	-1%	-1%	-2%

Source: Company data, HSBC estimates

Main credit quality and capital items

	NPL growth y/y						Coverage				
	3Q14	4Q14	1Q15	2Q15	3Q15		3Q14	4Q14	1Q15	2Q15	3Q15
ACB			3%	5%	8%	ACB	60%	62%	63%	65%	67%
BOP	8%	2%	-1%	-2%	-2%	BOP	58%	57%	56%	61%	61%

	Core Tier 1						Change in Core Tier 1 q/q (bp)				
	3Q14	4Q14	1Q15	2Q15	3Q15		3Q14	4Q14	1Q15	2Q15	3Q15
ACB	15.9%	14.3%	13.1%	11.1%	12.5%	ACB	-40	-160	-120	-200	140
BOP	13.1%	12.4%	11.6%	9.9%	10.9%	BOP	-189	-70	-76	-173	102

	Risk weighted assets/Total assets (%)						Risk weighted assets growth y/y				
	3Q14	4Q14	1Q15	2Q15	3Q15		3Q14	4Q14	1Q15	2Q15	3Q15
ACB	74%	72%	75%	75%	75%	ACB		4%	1%	-2%	-1%
BOP	65%	62%	65%	65%	65%	BOP	-5%	-6%	-6%	-6%	0%

Source: Company data, HSBC estimates

Annual monitor

Main P&L items

Net interest margin (bp)						Net interest income growth y/y					
	2014	2015e	2016e	2017e	2018e		2014	2015e	2016e	2017e	2018e
ACB	264	274	312	331	313	ACB	17%	0%	9%	6%	-4%
BOP	221	219	237	252	235	BOP	20%	-4%	5%	5%	-6%
Revenue growth y/y						Operating costs growth y/y					
	2014	2015e	2016e	2017e	2018e		2014	2015e	2016e	2017e	2018e
ACB	4%	-3%	7%	7%	-1%	ACB	15%	-30%	-6%	-1%	0%
BOP	18%	-2%	4%	6%	-5%	BOP	-6%	-13%	-6%	-2%	-1%
Credit costs annualised (bp)						Net income growth y/y					
	2014	2015e	2016e	2017e	2018e		2014	2015e	2016e	2017e	2018e
ACB	366	541	170	120	80	ACB	-111%	139%	-159%	66%	14%
BOP	622	440	170	122	90	BOP	-177%	-70%	-151%	100%	3%

Source: Company data, HSBC estimates

Main balance sheet items

Loans (Y-o-Y growth rate)						Deposits (Y-o-Y growth rate)					
	2014	2015e	2016e	2017e	2018e		2014	2015e	2016e	2017e	2018e
ACB	-4%	-6%	-3%	1%	3%	ACB	1%	-28%	17%	2%	2%
BOP	-8%	-11%	-3%	-1%	3%	BOP	1%	-30%	14%	2%	2%
Loan-to-Deposit ratio (%)						Funding gap as a % of total assets					
	2014	2015e	2016e	2017e	2018e		2014	2015e	2016e	2017e	2018e
ACB	116%	150%	125%	124%	125%	ACB	9%	23%	13%	13%	14%
BOP	104%	133%	112%	108%	109%	BOP	3%	14%	6%	4%	5%
Total assets growth y/y											
	2014	2015e	2016e	2017e	2018e						
ACB	-1%	-6%	-2%	1%	2%						
BOP	-3%	-3%	-2%	-1%	2%						

Source: Company data, HSBC estimates

Main credit quality and capital items

NPL growth y/y						Coverage					
	2014	2015e	2016e	2017e	2018e		2014	2015e	2016e	2017e	2018e
ACB	0%	11%	2%	-1%	-2%	ACB	62%	67%	67%	67%	67%
BOP	2%	2%	2%	-1%	-2%	BOP	57%	61%	61%	61%	61%

Core Tier 1						Change in Core Tier 1 q/q (bp)					
	2014	2015e	2016e	2017e	2018e		2014	2015e	2016e	2017e	2018e
ACB	14.3%	17.8%	18.9%	19.7%	20.3%	ACB	-180	346	115	80	61
BOP	12.4%	18.6%	19.2%	20.2%	20.2%	BOP	-152	625	62	96	4

Risk weighted assets/Total assets (%)						Risk weighted assets growth y/y					
	2014	2015e	2016e	2017e	2018e		2014	2015e	2016e	2017e	2018e
ACB	72%	76%	76%	78%	78%	ACB	4%	-2%	-1%	4%	2%
BOP	62%	66%	66%	66%	66%	BOP	-6%	2%	-2%	-1%	2%

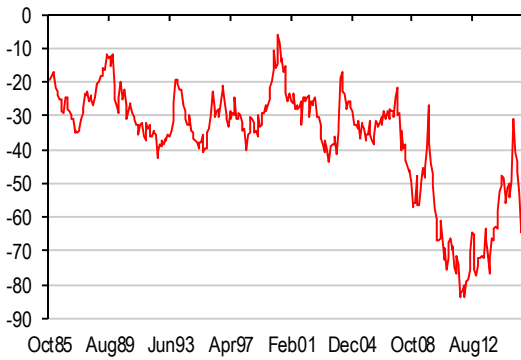
Source: Company data, HSBC estimates

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Sector appendix

Economics

Consumer confidence



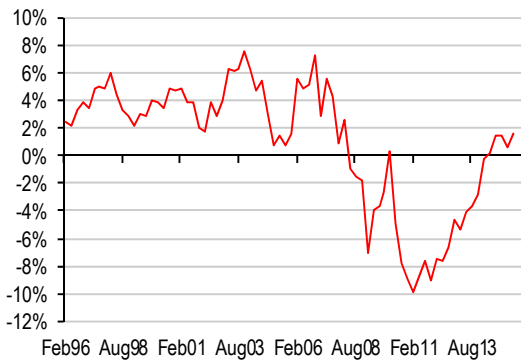
Source: Thomson Reuters Datastream, HSBC calculations

Economic Sentiment



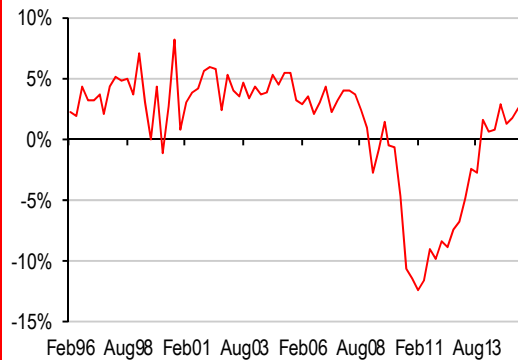
Source: Thomson Reuters Datastream, HSBC calculations

Real GDP (y/y, constant prices, SA)



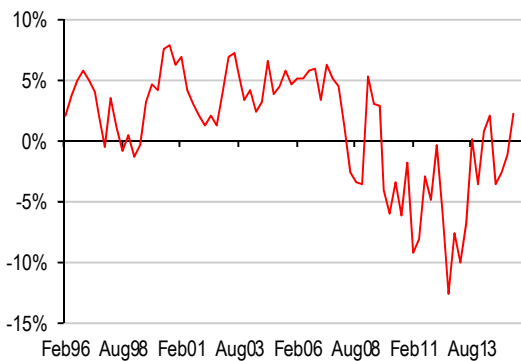
Source: Thomson Reuters Datastream, HSBC calculations

Consumer Spending (y/y, constant prices, SA)



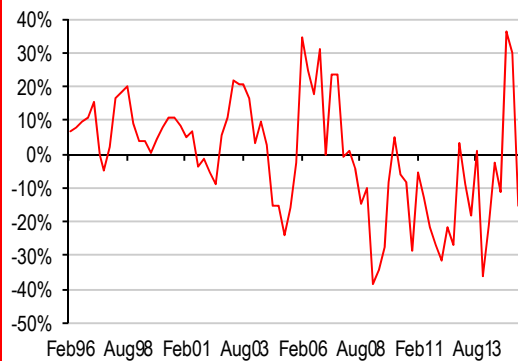
Source: Thomson Reuters Datastream, HSBC calculations

Government Consumption (y/y, constant prices, SA)



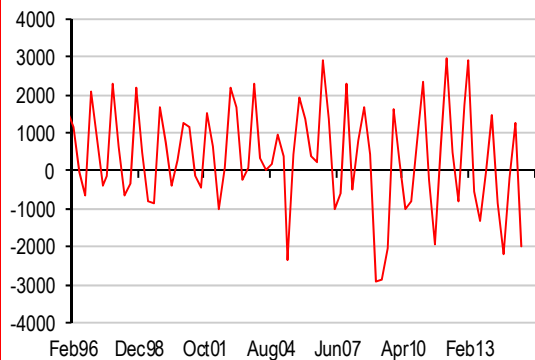
Source: Thomson Reuters Datastream, HSBC calculations

Capital Formation (y/y, constant prices, SA)



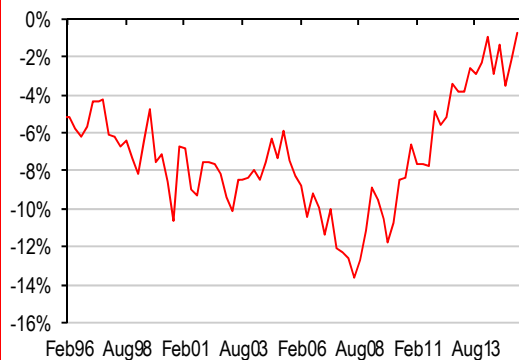
Source: Thomson Reuters Datastream, HSBC calculations

Changes in Inventories (current prices, NSA)



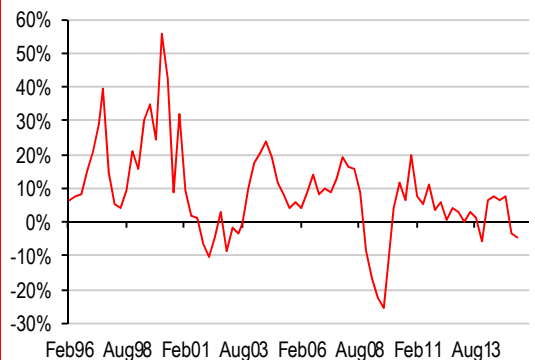
Source: Thomson Reuters Datastream, HSBC calculations

Net exports (% of GDP)



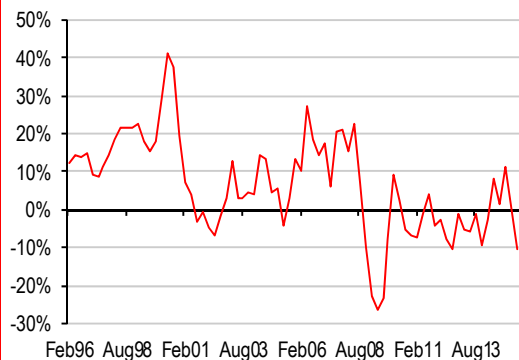
Source: Thomson Reuters Datastream, HSBC calculations

Exports (y/y, constant prices, SA)



Source: Thomson Reuters Datastream, HSBC calculations

Imports (y/y, constant prices, SA)



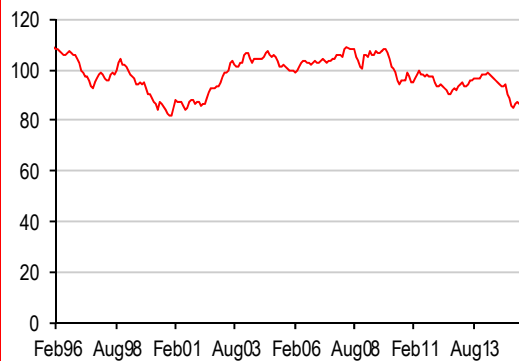
Source: Thomson Reuters Datastream, HSBC calculations

Trade Weighted Index



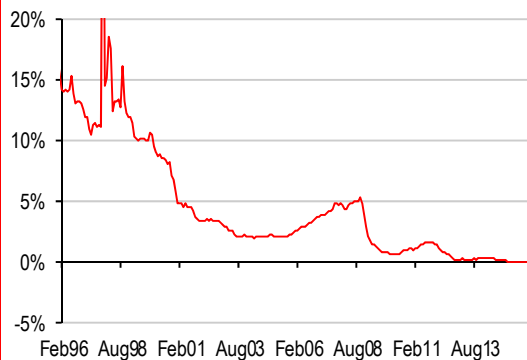
Source: Thomson Reuters Datastream, HSBC calculations

CPI Effective Exchange Rate Index



Source: Thomson Reuters Datastream, HSBC calculations

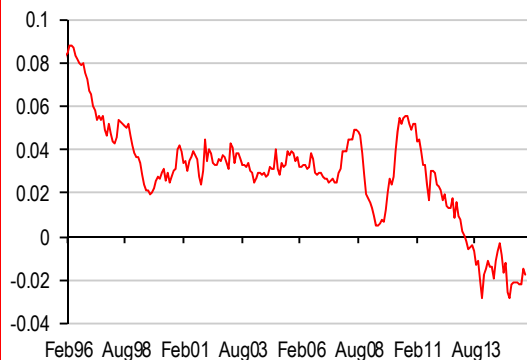
3M IBOR



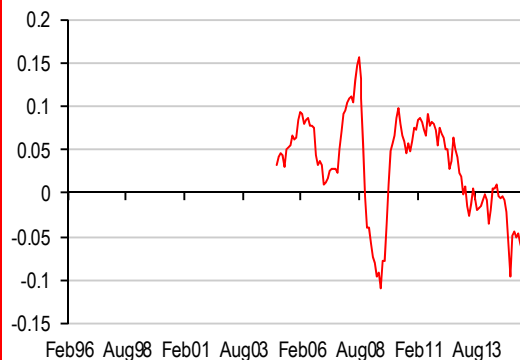
10Y GGB Yield



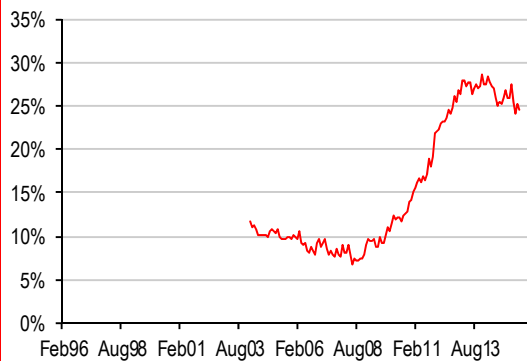
CPI



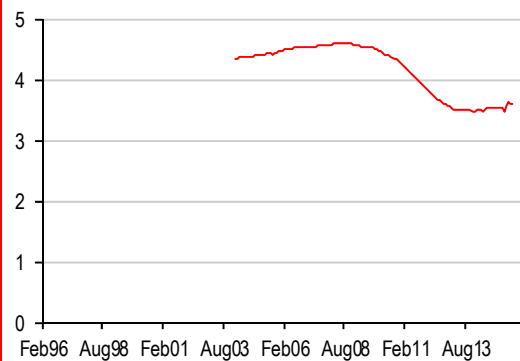
Producer Prices Index



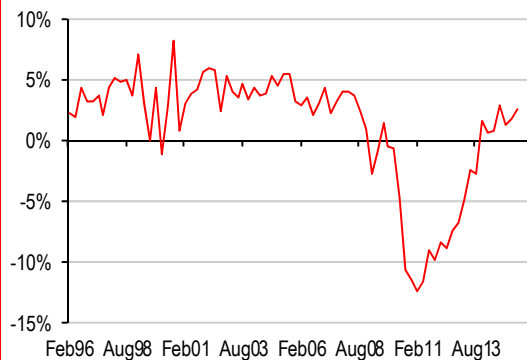
Unemployment Rate



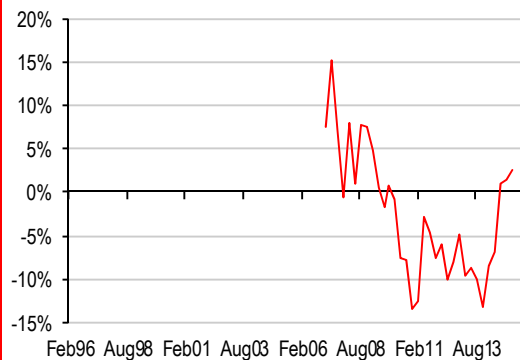
Employed (m)



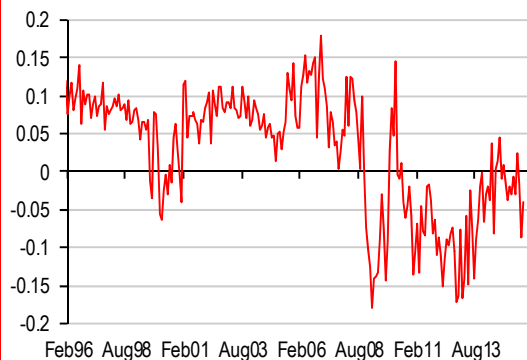
Consumer Spending (y/y, constant prices, SA)



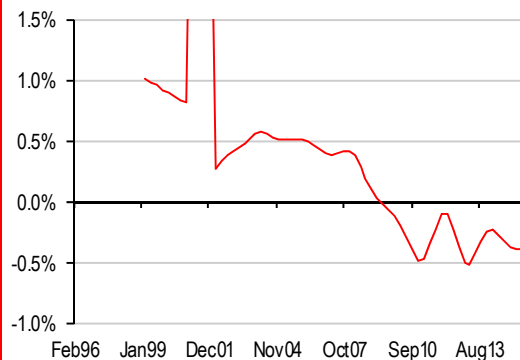
Gross Disposable Income (y/y)



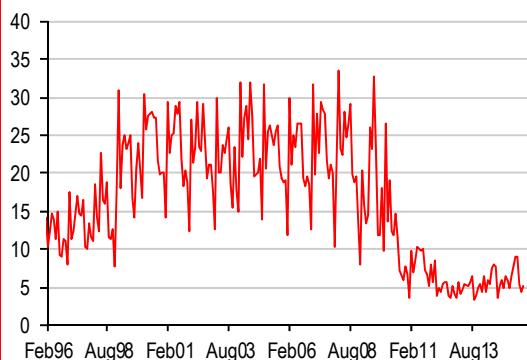
Retail Trade Turnover (y/y)



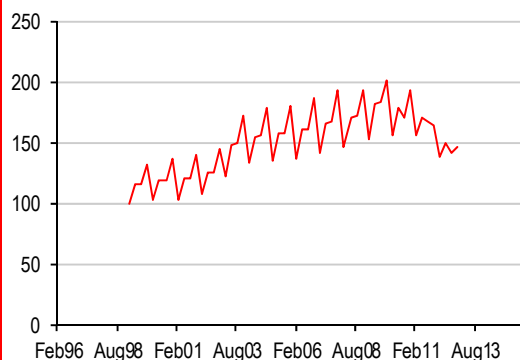
Population (y/y)



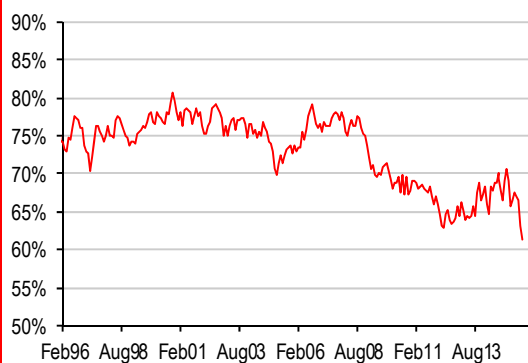
New Car Registrations ('000)



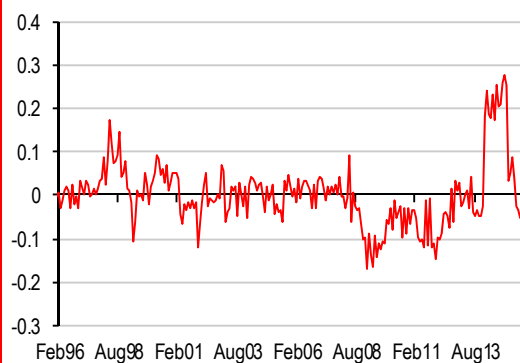
Unit Labour Costs Index (1999 = 100)



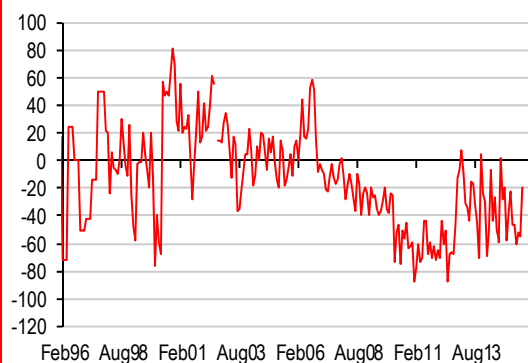
Production: Capacity Utilisation



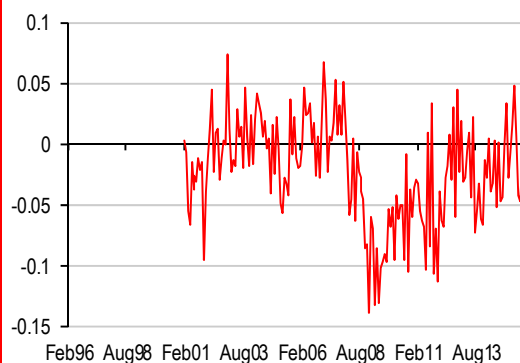
Industrial Production, Manufacturing Index (y/y)



Construction Survey: Building Activity, Housing

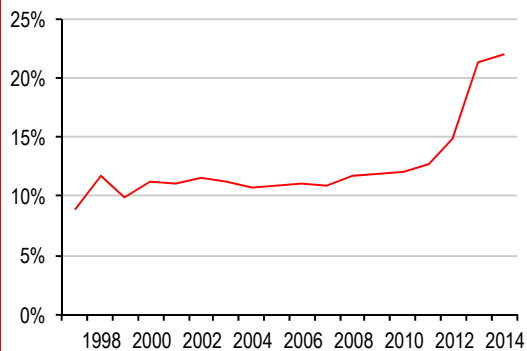


Industrial Production Index (y/y)



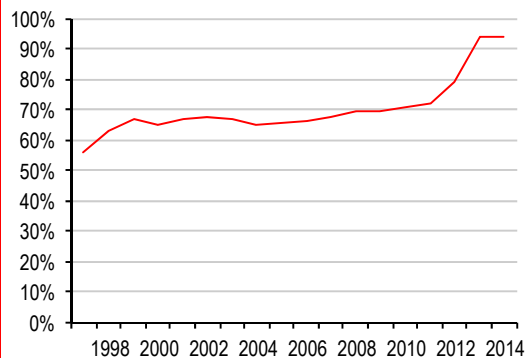
Banking structure

Herfindahl-Hirschman Index



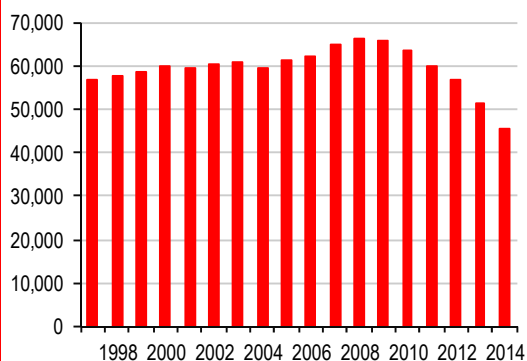
Source: Bank of Greece, HSBC calculations

Top 5 market share



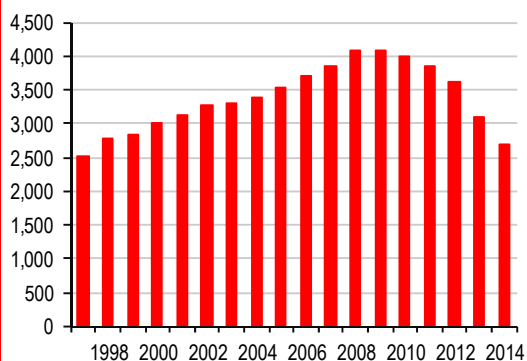
Source: Bank of Greece, HSBC calculations

Employees



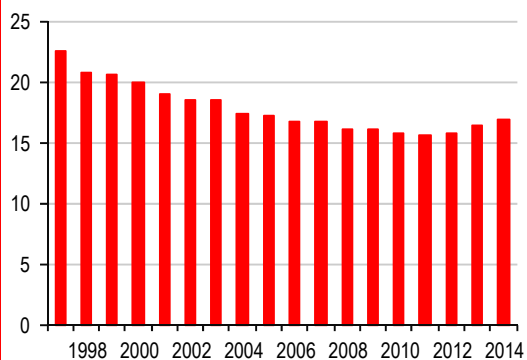
Source: Bank of Greece, HSBC calculations

Branches



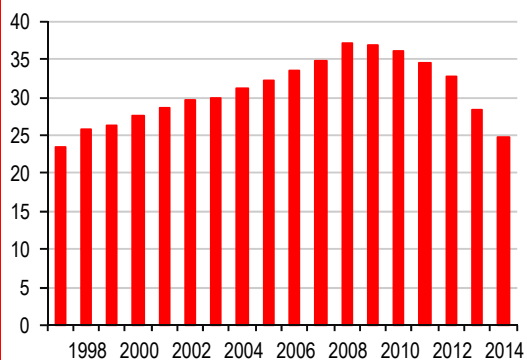
Source: Bank of Greece, HSBC calculations

Employees per branch



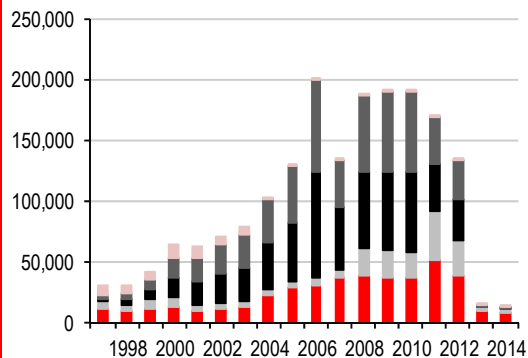
Source: Bank of Greece, HSBC calculations

Branches per 100,000 people



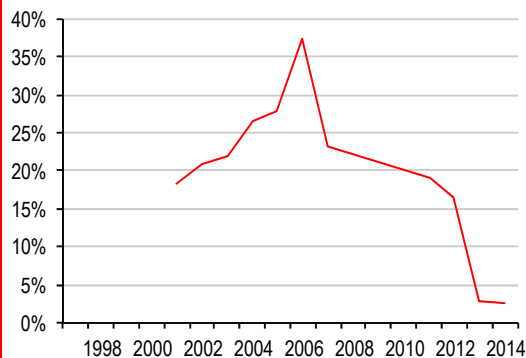
Source: Bank of Greece, HSBC calculations

Foreign-owned assets (EURbn)



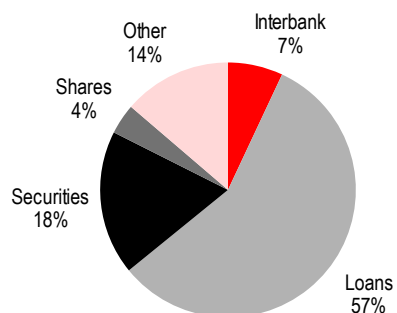
Source: Bank of Greece, HSBC calculations

Foreign-owned assets % of total



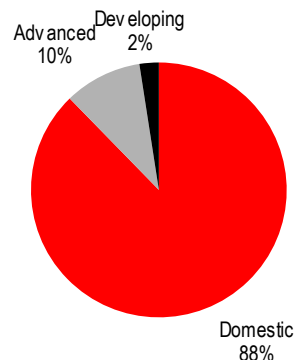
Source: Bank of Greece, HSBC calculations

Asset structure



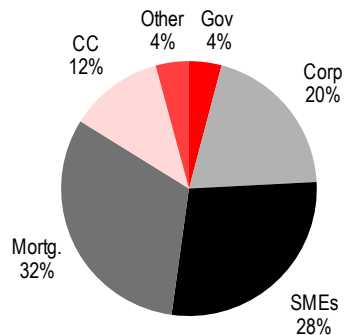
Source: Bank of Greece, HSBC calculations

Gross loans by geography



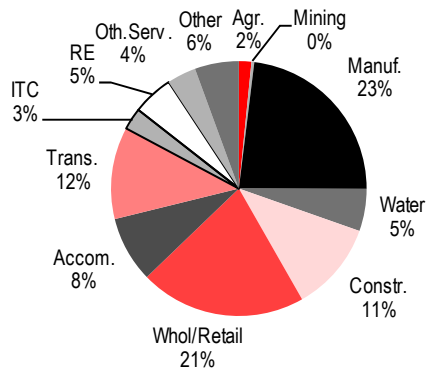
Source: Bank of Greece, HSBC calculations

Loan book breakdown



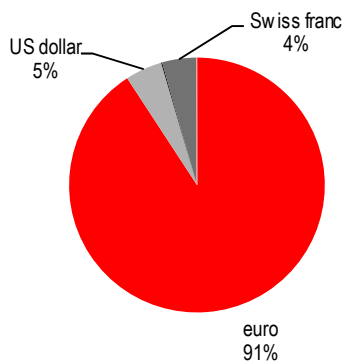
Source: Bank of Greece, HSBC calculations

NFC loans by activity



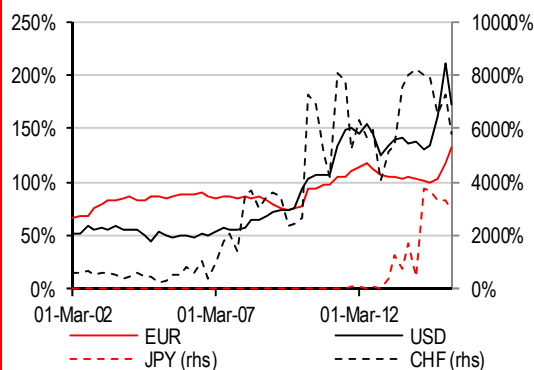
Source: Bank of Greece, HSBC calculations

Loans by currency



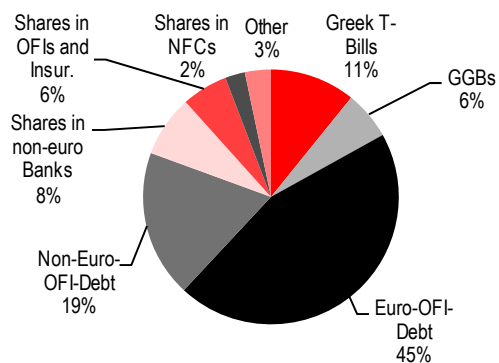
Source: Bank of Greece, HSBC calculations

Loans to deposits ratio by currency



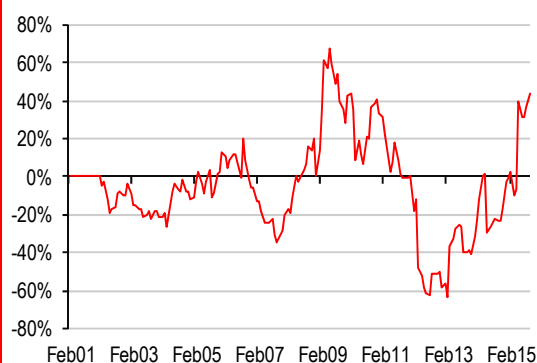
Source: Bank of Greece, HSBC calculations

Securities portfolio breakdown



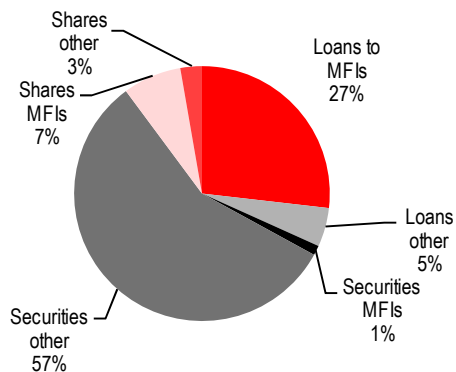
Source: Bank of Greece, HSBC calculations

Holdings of Greek government bonds and T-bills (y/y)



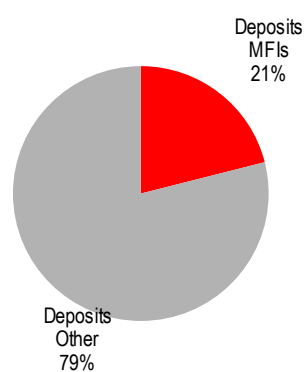
Source: Bank of Greece, HSBC calculations

Structure of foreign assets



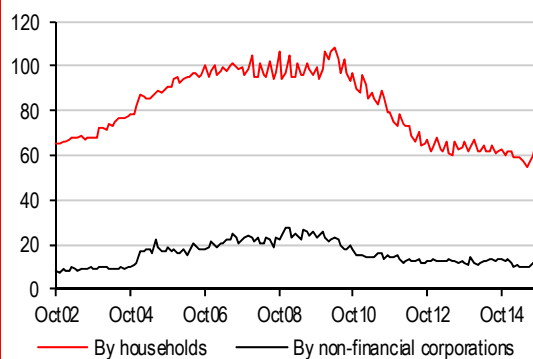
Source: Bank of Greece, HSBC calculations

Structure of foreign liabilities



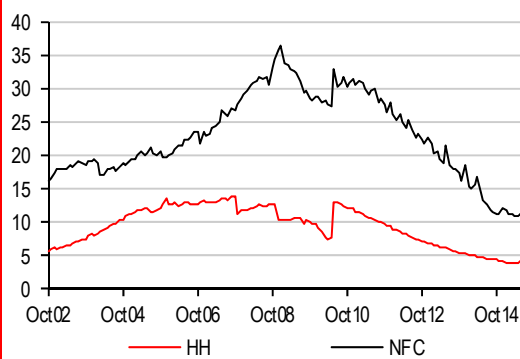
Source: Bank of Greece, HSBC calculations

Deposits: new production (EURbn)



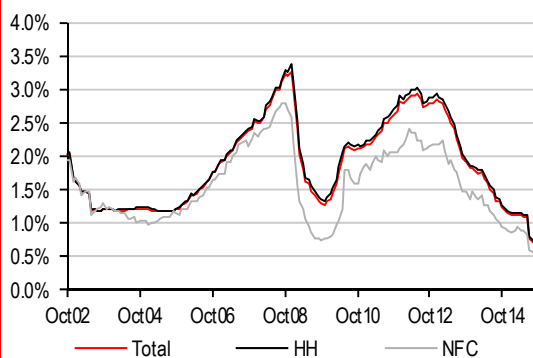
Source: Bank of Greece, HSBC calculations

Loans: new production (EURbn)



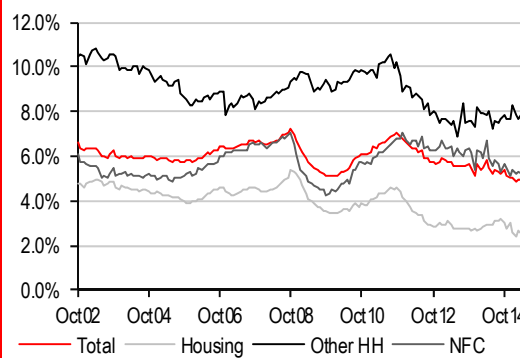
Source: Bank of Greece, HSBC calculations

New production rates on deposits



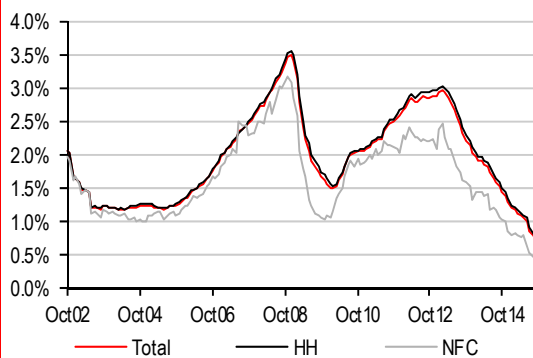
Source: Bank of Greece, HSBC calculations

New production rates on loans



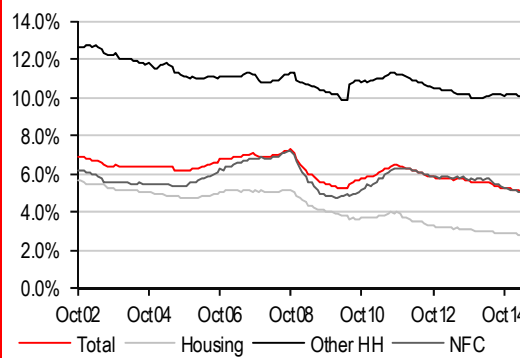
Source: Bank of Greece, HSBC calculations

Stock rates on deposits



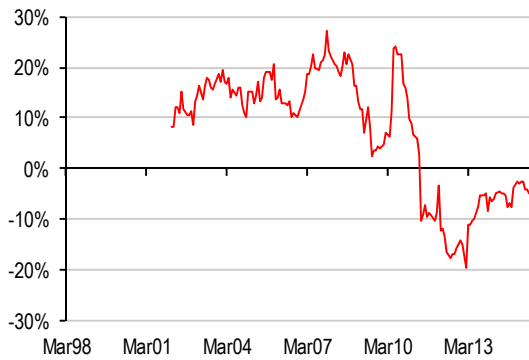
Source: Bank of Greece, HSBC calculations

Stock rates on loans

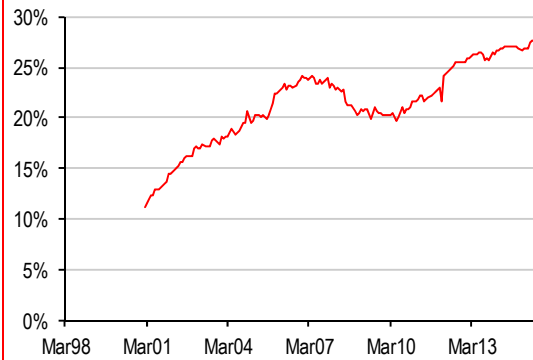


Source: Bank of Greece, HSBC calculations

Loan growth (gross, y/y)



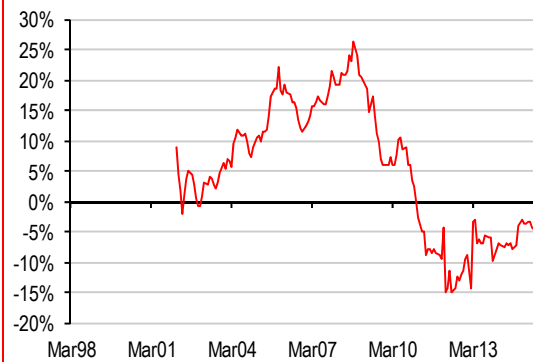
Housing loans as % of total loans



Customer deposits as % of loans



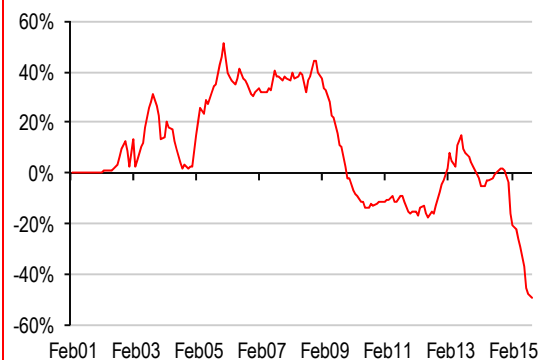
Growth in total assets (y/y)



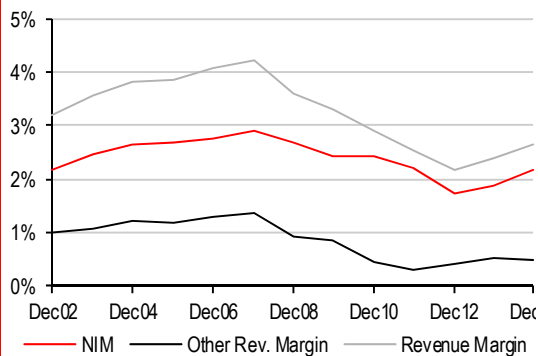
Liquid assets as % of total



Growth in domestic time deposits (y/y)

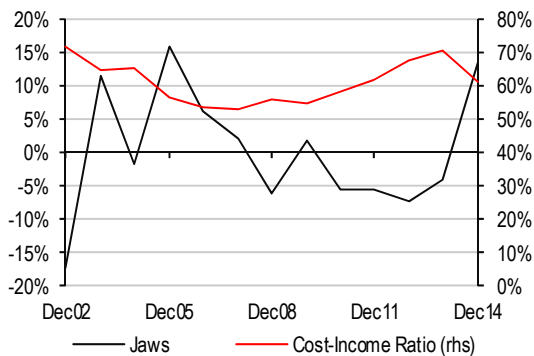


Revenue margins (% of ATA)



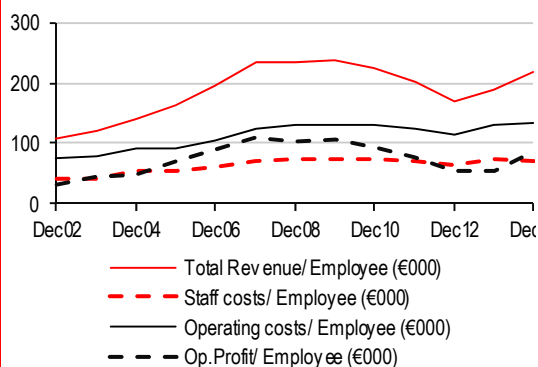
Source: Bank of Greece, HSBC calculations

Cost margins



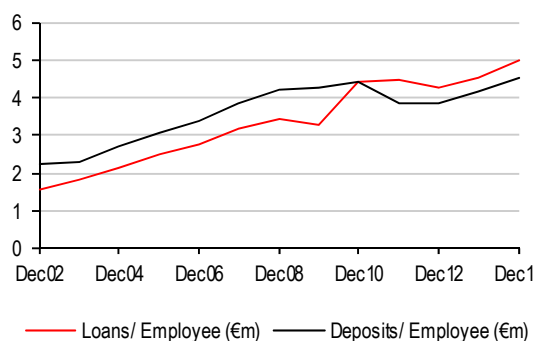
Source: Bank of Greece, HSBC calculations

Employee productivity



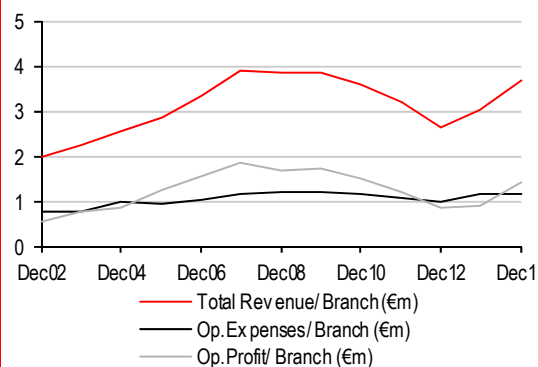
Source: Bank of Greece, HSBC calculations

Employee intensity



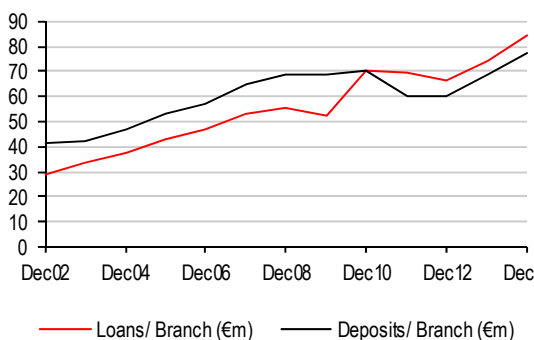
Source: Bank of Greece, HSBC calculations

Branch productivity



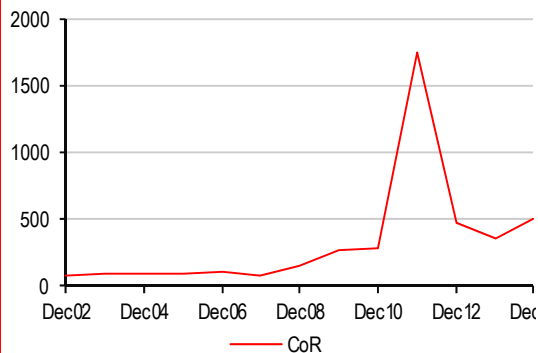
Source: Bank of Greece, HSBC calculations

Branch intensity



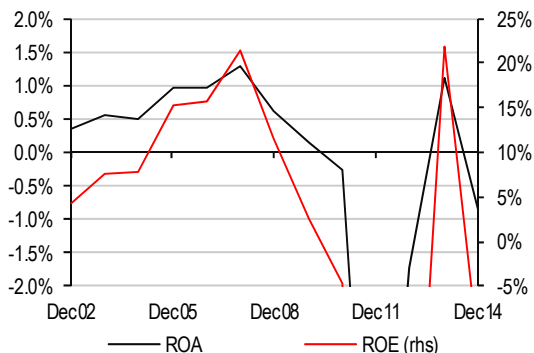
Source: Bank of Greece, HSBC calculations

Cost of risk (bp)



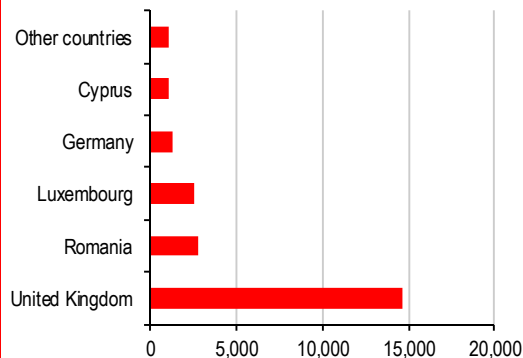
Source: Bank of Greece, HSBC calculations

Profitability



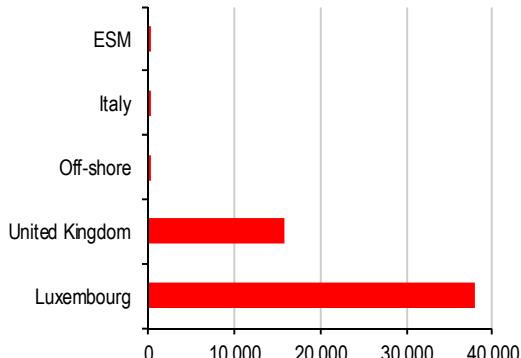
Source: Bank of Greece, HSBC calculations

Top 5 foreign exposures: loans to MFIs



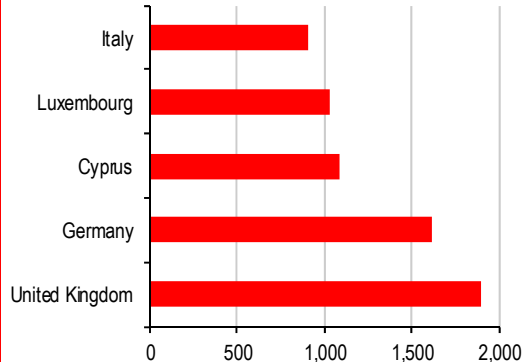
Source: Bank of Greece, HSBC calculations

Top 5 foreign exposures: Non-MFI securities



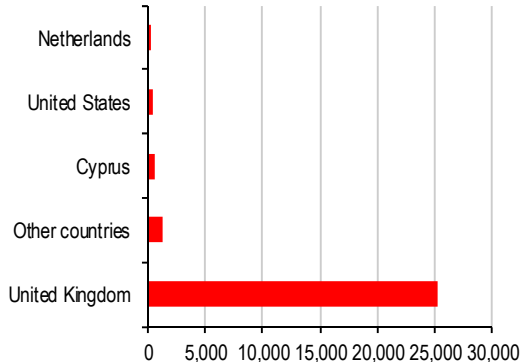
Source: Bank of Greece, HSBC calculations

Top 5 foreign exposures: MFI deposits % repo



Source: Bank of Greece, HSBC calculations

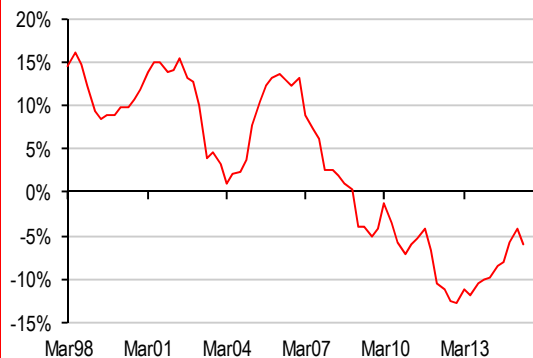
Top 5 foreign exposures: Non-MFI deposits & repo



Source: Bank of Greece, HSBC calculations

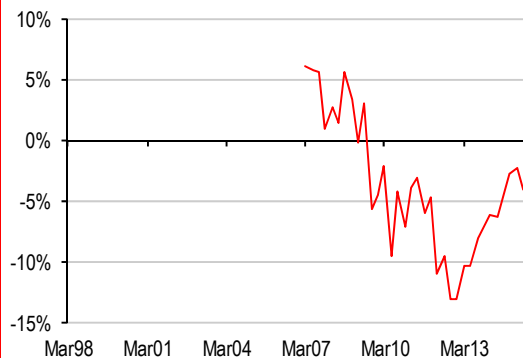
Real estate market

Apartment prices (y/y): urban areas



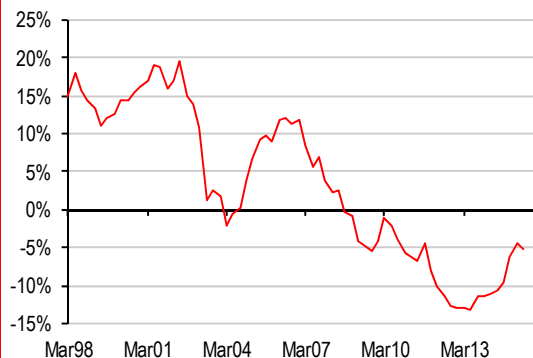
Source: Bank of Greece, HSBC calculations

Apartment prices (y/y): Other areas



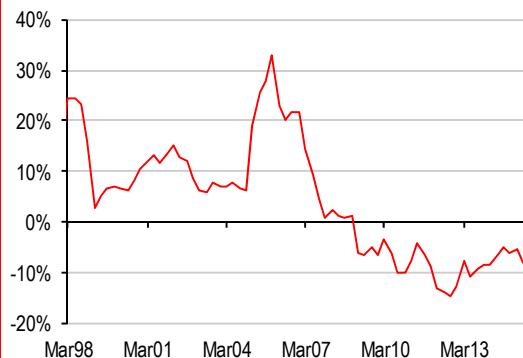
Source: Bank of Greece, HSBC calculations

Apartment prices (y/y): Athens



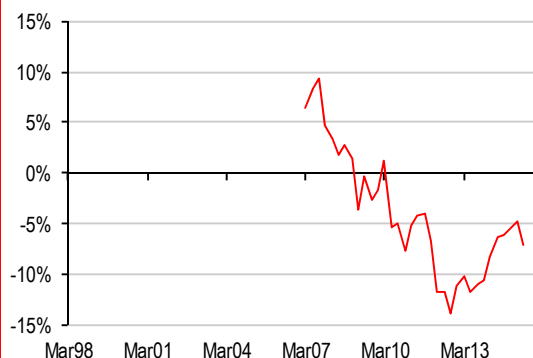
Source: Bank of Greece, HSBC calculations

Apartment prices (y/y): Thessaloniki



Source: Bank of Greece, HSBC calculations

Apartment prices (y/y): Up to 5 years old



Source: Bank of Greece, HSBC calculations

Apartment prices (y/y): over 5 years old



Source: Bank of Greece, HSBC calculations

Notes

Disclosure appendix

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Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation or resumption of coverage, change in target price or estimates).

Upside/Downside is the percentage difference between the target price and the share price.

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For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands were classified as Neutral.

*A stock was classified as volatile if its historical volatility had exceeded 40%, if the stock had been listed for less than 12 months (unless it was in an industry or sector where volatility is low) or if the analyst expected significant volatility. However, stocks which we did not consider volatile may in fact also have behaved in such a way. Historical volatility was defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility had to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Rating distribution for long-term investment opportunities

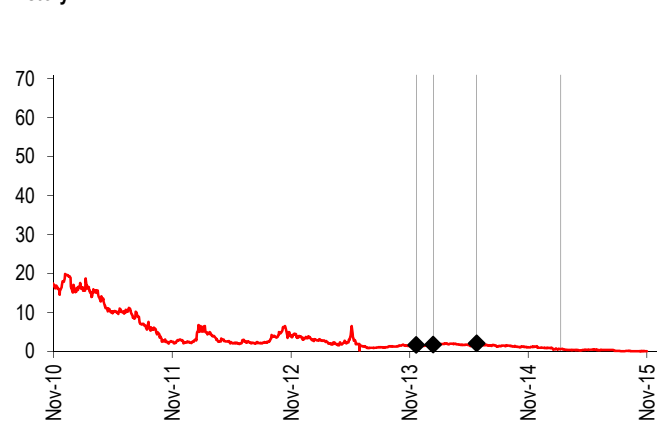
As of 12 November 2015, the distribution of all ratings published is as follows:

Buy	45%	(31% of these provided with Investment Banking Services)
Hold	41%	(29% of these provided with Investment Banking Services)
Sell	14%	(17% of these provided with Investment Banking Services)

For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see “Stock ratings and basis for financial analysis” above.

Share price and rating changes for long-term investment opportunities

Piraeus Bank SA (BOPr.AT) Share Price performance EUR Vs HSBC rating history



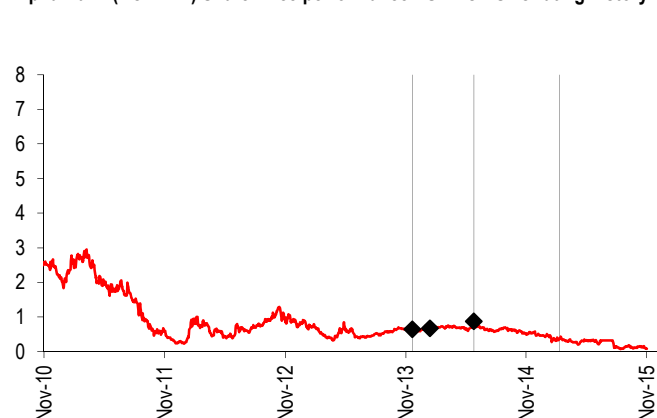
Source: HSBC

Recommendation & price target history

From	To	Date
N/A	Neutral (V)	02 December 2013
Neutral (V)	Underweight (V)	23 January 2014
Underweight (V)	Neutral (V)	06 June 2014
Neutral (V)	N/A	19 February 2015
Target Price	Value	Date
Price 1	1.63	02 December 2013
Price 2	1.69	23 January 2014
Price 3	2.08	06 June 2014
Price 4	N/A	19 February 2015

Source: HSBC

Alpha Bank (ACBr.AT) Share Price performance EUR Vs HSBC rating history



Source: HSBC

Recommendation & price target history

From	To	Date
N/A	Underweight (V)	02 December 2013
Underweight (V)	Overweight (V)	06 June 2014
Overweight (V)	N/A	19 February 2015
Target Price	Value	Date
Price 1	0.64	02 December 2013
Price 2	0.67	24 January 2014
Price 3	0.87	06 June 2014
Price 4	N/A	19 February 2015

Source: HSBC

HSBC & Analyst disclosures

Disclosure checklist

Company	Ticker	Recent price	Price Date	Disclosure
ALPHA BANK	ACBr.AT	0.08	12-Nov-2015	1, 6
PIRAEUS BANK SA	BOPr.AT	0.04	12-Nov-2015	6

Source: HSBC

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