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2nd UPDATE: Euro Stress Builds As PBOC Shows Greek Crisis Concerns

By Katie Martin

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LONDON (Dow Jones)--The People's Bank of China offered the first solid evidence that the Greek bailout fiasco is denting reserve managers' faith in the euro Thursday, as a top official expressed concern that the current rout reflects weak leadership and is just the "tip of the iceberg."

Speaking in Hong Kong, the PBOC's Vice Governor Zhu Min said he doubts that debt-ridden Greece will go bankrupt, but he added that "the main concern today is obviously Spain and Italy."

In a damning assessment of the way European Union leaders are addressing the issue, he also said that "we don't see decisive action that tells the market, 'We can solve it, we can close it.'"

The comments come just one day after Fitch Ratings downgraded Portugal, offering a fresh reminder that Greece is not the only euro member under pressure from excess spending. They also confirm concern in the market that debt strains in the currency bloc could sap some of the support that the euro has enjoyed as a key component of official reserves over the past 10 years.

"This is a good indication of how rapidly fundamental concerns are growing about the euro zone," said Simon Derrick, a senior currencies analyst at the Bank of New York Mellon in London.

"Indeed, this comment might well signal the point that we stop talking about a Greek debt crisis and start talking about a euro-zone structural crisis instead. It is hardly surprising that investors are in a major reassessment of one of the most favored major currencies of the past decade," he added.

A buildup of euro holdings by official reserve managers is widely seen as a key contributor to the currency's climb against the dollar since 2001, during which time it has swept up from below parity to a peak above \$1.60 in 2008.

China is the world's biggest single official reserve holder, with around \$2.4 trillion in assets--a huge share of the global total of around \$7.5 trillion.

Data from the International Monetary Fund show that emerging markets as a whole hold around one-third of their reserves in euros. China doesn't reveal its currency weightings, and its euro share may be smaller, but euros are still widely assumed to make up a significant part of the total.

Without its so-called reserve premium, most analysts agree that the euro would trade at around \$1.20 to \$1.25--way below current levels.

The Greek debt crisis itself is not new; investors have been questioning whether the euro member can repay its debts ever since it emerged that some of the country's key economic statistics were flawed back in December last year.

However, it is now becoming increasingly apparent that the euro zone and the European Union lack the political clout to deal with the problem efficiently.

The 16 euro-zone nations share a core monetary policy through the European Central Bank, but they have independent tax-and-spending powers and separate political leadership.

Over the past two weeks, the scale of disagreement between those different countries and within pan-regional bodies over whether and how to help Greece has grown, with contradictory potential plans emerging on a regular basis.

Meanwhile, the deadline for Greece to find a solution before it is forced to borrow funds from the open market at punitive rates from next month draws nearer.

European Union political leaders are holding a summit Thursday and Friday, but analysts expect to see little beyond a vague declaration of solidarity with Greece.

The International Monetary Fund--the world's lender of last resort--may emerge as a key part of any eventual rescue deal.

"This makes Europe look stupid. Leadership is completely absent," said Georges Ugeux, chairman of consultancy Galileo Global Advisors in New York earlier this week. "Going to the IMF would be disastrous for Europe. It would lose all credibility."

At 1115 GMT in London, the euro had recovered from declines earlier Thursday in Asia to trade at \$1.3366 against the dollar, as market participants awaited news from the European Union summit later in the day.

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