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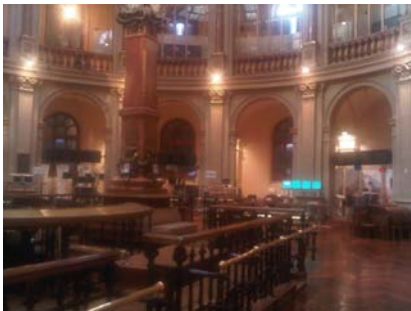
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Spain Is Not Close to Bankruptcy: Amalgamation Should Not Mean Contagion



The downgrading of Spain was done for strange reasons. Spain has a debt to GDP of 90% (against 144% of for Greece) and a budget deficit of 7% (against Greece's 14%). More importantly, the spread over German bunds is 250 bps against 700bps. With an AA rating (compared to Greece's BB), even after the recent downgrading from AAA, Spanish creditworthiness is strong.

We are living in a strange world where everything that is said can be published and then becomes a self-fulfilling prophecy. The role of the media is important, but also the way the authorities communicate is critical.

Jose Luis Rodriguez Zapatero and his Government need to stick to the facts rather than threatening the rating agencies or the markets. I happened to be in Madrid last week on the day Spain was downgraded. It was portrayed by as a catastrophic situation. Now is not the time for over dramatization and the endless shows of the European leaders giving more of an impression of confusion than leadership.

Whoever launched the rumor of a \$ 350 billion IMF financing for Spain that made the markets immediately tumble must be the same people who spread rumors to cover their short positions. Unfortunately short sales in fixed income are neither well regulated nor monitored. This was insane. But the fact that the market believed the rumor for a few hours is in itself a sign of its lack of knowledge.

The Spanish problem is totally different from that of Greece and these two should not be confused in the market. The Zapatero Government has been slow to act forcefully to the problems in the "cajas de ahorros." These savings banks are mostly providers of mortgages and many are close to collapse and will only survive through consolidation.

Local politics have delayed some of those transactions and the Spanish Government has not acted as decisively as it should have. Yet this is ultimately more of a private sector problem, since those cajas heavily borrowed abroad benefitting (until now) of the public sector 's AAA rating.

The largest Spanish banks, especially Bilbao Vizcaya and Santander had limited exposure to the subprime markets and are perfectly capable of weathering the storm of the real estate market collapse in Spain.

Contagion should only happen when there is an immediate connection between the issuers. While they share the commonality of the Euro, and therefore the slow growth in 2010, the decrease of the value of the European currency is also benefitting to them. Beyond that the situation of each individual country is specific and amalgamation makes no sense.

The amalgamation could provoke contagion, but it definitely does not need to be the case.