Irish Examiner

Spain, Italy and Portugal banks face €250bn losses

October 10, 2013

Banks in Spain, Italy and Portugal face about €250bn in potential losses on their business loans over the next two years, the International Monetary Fund (IMF) said.

By Sandrine Rastello
About one-fifth of combined corporate loans is at risk of default in the three economies, which are forecast to contract this year, according to the fund’s Global Financial Stability Report.

The Spanish banking system is the only one with enough reserves to cover the losses, it said.

The study is “an illustration of the potential magnitude of corporate risks for banking systems,” the fund said in the report. “Some banks in the stressed economies might need to further increase provisioning to address the potential deterioration of asset quality on their corporate loan books, which could absorb a large portion of future bank profits.”

The Washington-based IMF used the findings to urge the European Central Bank, which is preparing an asset-quality review of banks joining the euro-area supervision regime next year, to pay attention to corporate exposure.

While investors’ pressure on Europe has eased as policy makers took measures to strengthen the monetary union, the fund said it’s “vital” to clean banks’ balance sheets and end a cycle that has weak banks and businesses making each other worse off.

“The forthcoming bank balance-sheet assessment and stress tests provide a golden opportunity to carry out a comprehensive and transparent evaluation across euro-area banks that could help restore investor confidence in the quality of their balance sheets,” the IMF said.

The fund said its own exercise, which assumes that policy makers stall on their commitments, stops short of a stress test. Using data for about 2 million non-financial companies in the three Mediterranean countries, it estimated that Spanish banks face potential corporate-loan losses of €104bn, an amount that would be covered by existing provisions.

The estimate is €125bn for Italy, with €53bn exceeding provisions, and €20bn for Portugal, with €8bn that are not covered. Still, the financial system in those two countries would buffer the losses with operating profits, without having to use existing capital buffers, the fund estimated.

The ECB's stress test must be tough and deep, Jose Vinals, director of the International Monetary Fund's monetary and capital markets department, said during a press conference.

Once capital shortfalls are identified, the private sector should be the first line of defence, followed by national backstops or the European Stability Mechanism if needed, he said.

Vinals said the Bank of Italy is working on boosting provisions at Italian banks to address the potential corporate loan losses.

The IMF has just cut its global outlook for this year and next as capital outflows further weaken emerging markets and warned that a US government default could "seriously damage" the world economy.

Managing the exit of the US monetary stimulus may be challenging, with risks that long-term interest rates rise more sharply than currently anticipated, it said.

The effect would be magnified because many investors in recent years moved into fixed-income assets, with longer durations, the fund said.

Bond prices slumped internationally and emerging-market stocks plunged after May 22, when Federal Reserve chairman Ben Bernanke said for the first time the Fed may trim its asset purchase programme within the next few meetings.