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Europe's Debt Crisis, U.S. Banks' Exposure

American Banker | Wednesday, May 12, 2010

By [Paul Davis](#) and [Matt Monks](#)

The European debt crisis poses problems for American banks still recovering from the housing crisis, even though most of them have relatively little — if any — direct exposure to troubled economies like Greece, Portugal and Spain.

If Europe's plan to stem the crisis fails, big losses could result at global banks like [JPMorgan Chase & Co.](#) and [Bank of America Corp.](#) that actually do business overseas, while hurting regional banks with no direct foreign interests, market watchers say.

"Small banks are not going to have any direct exposure to Greece or other countries, so you might initially think they're insulated," said [Kevin Jacques](#), a former Treasury Department economist and now chairman of finance at [Baldwin-Wallace College](#) in Cleveland. "That is a faulty presumption."

Observers say Greece's problems — should they spread across the region — could hurt everything from real estate sales in Florida to corporate loan demand in Cleveland. Europe's debt issues probably wouldn't send the U.S. banking market into another meltdown, they say. But the problem may hinder U.S. banks' ability to recover from the credit crisis, and it underscores the problem of potential hazards there or in other regions.

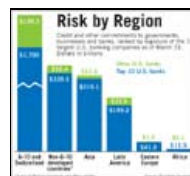
"There is so much interconnectivity in the global financial markets," said [Steven Sandler](#), chief executive of Crosswind Capital LLC, a distressed-real-estate investment firm. "What happens in one corner of the world can have serious impact elsewhere."

That sentiment was illustrated last week when shares of regional lenders with no overseas ties to speak of — think [Huntington Bancshares Inc.](#), [KeyCorp](#) and [Fifth Third Bancorp](#) — plunged as Europe's problems deepened.

[David Dietze](#), chief investment strategist of [Point View Financial Services Inc.](#), said regional lenders may not have direct ties overseas, but that does not mean their corporate clients don't, particularly in the technology sector. Also, European investors had been prowling the distressed U.S. real estate market before the crisis.

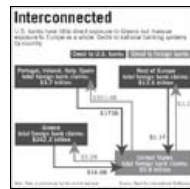
"There was a hope that some of the real estate woes being experienced by regional banks would be abated by the weakening U.S. dollar bringing in overseas investors," he said. "Now that their currencies are falling versus the dollar ... the Europeans aren't going to be buying Miami this spring."

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Large banks are more vulnerable to Europe's problems than regional players.

At March 31, [Bank of America](#) had \$1.3 billion of investments in Greece and \$731 million in Portugal. JPMorgan Chase, meanwhile, said its loss exposure in Greece and Portugal was under \$2.1 billion each.

Jes Staley, head of JPMorgan Chase's investment bank, described its exposure to Greece in a speech Tuesday as "de minimis, pretty much close to zero." He added that it is "comfortable" with its commitments in Italy and Spain.

But analysts said Europe's troubles cast a pall over large banks' promising first-quarter results even as big lenders play down their exposure there.

"Bank stocks plunged last week under the theory that banking companies will take large losses in Europe. The theory is correct. Banks will get hurt," [Richard Bove](#) of [Rochdale Securities LLC](#) wrote in a research note.

[Bove](#) wrote in a separate report last week that "big American banks have a bigger stake in this drama than thought." He estimates that JPMorgan Chase has \$1.4 trillion of exposure across all of Europe alone, while [Citigroup Inc.](#) has \$468.4 billion.

Analysts said large U.S. banks have opaque ties to the region through their overseas counterparts. U.S. money-center banks trade derivatives, orchestrate currency swaps and handle other transactions with large European banks. U.S. banks may not hold a lot of sovereign debt in Europe, but those European institutions do. If Greece defaults, that could create a crisis of confidence in the European banking market that would spread to large U.S. banks.

"Obviously, the European banks have exposure to Greece. The U.S. banks have loans out to those banks," said [Keith B. Davis](#), an analyst with Farr Miller & Washington. "There are a number of different ways they can have exposure — it's not hard to imagine how a wildfire can spread."

Though Europe presents complications for U.S. banks, analysts say it's unlikely it will develop into another full-blown crisis for them.

Large banks are much stronger than they were ahead of the housing collapse in 2008, as they have massive amounts of capital and liquidity.

Regulators also have more tools to stabilize the system than they did two years ago.

Still, U.S. regulators aren't taking any risks. [Federal Reserve](#) Chairman [Ben Bernanke](#) reportedly told lawmakers Tuesday that the central bank revived emergency swap lines with five foreign central banks over the weekend because if left unattended the European crisis could affect U.S. banks.

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