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The Pain in Spain Falls Mainly on the *Cajas*

Many nonprofit lenders face hard times even as the biggest commercial banks remain strong

By Mark Scott

As Spain's economy faltered over the past year, outsiders marveled at the strength of financial giants Banco Santander (STD) and BBVA (BBVA). How could the two largest banks have fared so well in such a troubled economy? The answer is that the pain has hit a separate category of bank: the *cajas*, nonprofit institutions that make roughly half of all loans in the country.

These banks—similar to savings and loan associations in the U.S.—eagerly served up credit as the housing bubble inflated over the past decade. Last September they had some $330 billion in loans to developers on their books, up from $50 billion in 2000, the central bank estimates. Today, nearly half of the *cajas*' $1.8 trillion in assets are mortgages or other real estate loans.

With home prices plunging, the 45 *cajas* are suffering. More than 7% of their loans could go bad this year, vs. 5.1% in 2009, according to the Spanish Confederation of Savings Banks, an industry group. Growing defaults "are a real concern," says Santiago Carbó, a finance professor at the University of Granada. Credit Suisse (CS) says the *cajas* might lose $3.4 billion this year.

The defaults could lead to a wave of foreclosures or writedowns that would further hobble Spain's anemic economy. Gross domestic product shrank 3.7% in 2009 and may contract an additional 0.8% this year, vs. a 2.2% expansion in the U.S., according to EU estimates. And there's little spare cash available for bailouts. The deficit is expected to hit 9.8% of GDP this year, and Madrid has announced $70 billion in budget cuts to bring the figure below 3% by 2013.

To raise cash, the *cajas* are scrambling to sell properties they have seized as collateral, which could further pummel housing prices. "Everyone is trying to offload assets," says Robert Tornabell, former dean of ESADE Business School in Barcelona. "It's a war out there."

Smaller *cajas* rarely publish financial reports, so it's hard to know exactly how they're faring. But Mauro Guillén, a professor at the University of Pennsylvania's Wharton School, says the biggest problems are in southern Spain, where billions were plowed into seaside resort hotels and condominiums. "Many got caught up in the real estate gold rush," Guillén says.

Cajas typically have close ties to provincial governments, so they often face pressure to back projects that may not be profitable. A prime example is Terra Mítica, a theme park in the southern resort town of Benidorm. Partially owned by Bancaja and Caja Granada, the park went bankrupt in 2004 and has struggled since reopening in 2006.

Second-tier commercial banks are also grappling with soured real estate loans, but the *cajas* have fewer options for solving their problems. As quasi-public institutions, they can't be purchased. So the most likely outcome for weaker players is a tie-up with a rival, and Madrid has offered $135 billion in long-term financing to *cajas* that merge. While many deals face opposition from provincial politicians, 24 *cajas*—with total assets of $470 billion—have indicated they plan to consolidate, according to ratings agency Moody's. "We are looking for partners to get stronger in Spain and [to expand] abroad," says Enrique Goñi, chief executive of Pamplona-based Caja Navarra, which is working on mergers with two smaller rivals.

The two biggest players, meanwhile, are sitting on the sidelines. Caja Madrid and Barcelona-based La Caixa both have a nationwide presence and are among Spain's top five financial houses. With billions of retail deposits to help them weather the downturn, they have little interest in taking over weaker rivals. Says John Raymond, senior analyst at research firm CreditSights: "They're big enough to ride out any problems."

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