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## WOULD A BIG BAD BANK BLOW THE REAL ESTATE PROBLEMS OF SPAIN DOWN?

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On November 20, 2011 Spain elected Mariano Rajoy, of the conservative People's Party, as prime minister.<sup>1</sup> During his campaign he claimed that "cleanup and restructuring" of the banking system in Spain was his primary concern.<sup>2</sup> Rajoy pledged to adopt a program to fund Spain's recovery by increasing the amount of available credit.<sup>3</sup> With the current financial troubles in the Eurozone, reviving Spain's banks could be a daunting task for the newly elected prime minister. The BBC reports that "Spain is[a] much more indebted or leveraged country than Italy" when aggregating all debts including government, corporate, financial, and institution debts.<sup>4</sup>

To fix the financial issues of Spain, Rajoy must conquer the seemingly insurmountable amount of troubled real estate loans held by the country's lenders.<sup>5</sup> The Bank of Spain stated that half of the €308 billion of real estate loans are classified as troubled.<sup>6</sup> These problems seem to stem from the decreasing values of Spanish homes, which have decreased by 28 percent on average since April 2007.<sup>7</sup> Pablo Cantos, a managing partner of MaC Group who advises Spanish banks on risk, claims that about €30 billion of real estate held by Spanish banks are "unsellable."<sup>8</sup> The future for Spanish real estate assets remains bleak as Taurus Iberica Asset Management--a Spanish mortgage servicer--reports that financial institutions have foreclosed on 200,000 homes and the foreclosures will rise to 600,000 homes due to

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<sup>1</sup> See Sharon Smyth, *The Real Threat Facing Spanish Lenders: Spain's Banks Hold Billions of Euros in Property That Will Be Tough to Sell*, BUSINESSWEEK.COM (Nov. 23, 2011, 5:00 PM EST), <http://www.businessweek.com/magazine/the-real-threat-facing-spanish-lenders-11232011.html>.

<sup>2</sup> *Id.*

<sup>3</sup> See Charles Penty & Emma Ross-Thomas, *Spain Set to Purge Banks of Property Hangover*, BLOOMBERG.COM (Nov. 16, 2011 4:51 AM EST), <http://www.bloomberg.com/news/2011-11-16/spain-set-to-purge-banks-of-real-estate-hangover-euro-credit.html>.

<sup>4</sup> See Mike "Mish" Shedlock, *Spanish Banks Are Stuck With 'Unsellable' Property And 50% Troubled Real Estate Loans*, BUSINESSINSIDER.COM (Nov. 19, 2011), [http://www.articles.businessinsider.com/2011-11-19/markets/30418837\\_1\\_real-estate-loans-medium-size-banks-madrid](http://www.articles.businessinsider.com/2011-11-19/markets/30418837_1_real-estate-loans-medium-size-banks-madrid).

<sup>5</sup> *Id.*

<sup>6</sup> *Id.*

<sup>7</sup> See Sharon Smyth, *Spanish Banks Have \$41 Billion of 'Unsellable' Real Estate*, BUSINESSWEEK.COM (Nov. 30, 2011, 6:47 AM EST), <http://www.businessweek.com/news/2011-11-30/spanish-banks-have-41-billion-of-unsellable-real-estate.html>.

<sup>8</sup> *Id.*

the increase in unemployment.<sup>9</sup> Fernando Acuan Ruiz, managing partner of Taurus Iberica, stated that Spain has 1 million new homes that will not be consumed until 2017.<sup>10</sup>

A solution to Spain's bank problems may lie in facilitating a "bad bank" according to some analysts.<sup>11</sup> Creating a "bad bank" would relieve banks of their toxic real estate assets and the bad bank would attempt to sell the assets as prices improve.<sup>12</sup> Fernando Fernandez, IE professor and former International Monetary Fund economist, believes that a bad bank is the only cure to clean up bank balance sheets and revive the flow of credit.<sup>13</sup> A bad bank worked well in Ireland because it restored confidence to investors.<sup>14</sup> However, creating a bad bank in Spain with the current financial troubles of the euro zone could be a disaster according to analysts.<sup>15</sup> One London-based analyst believes that the additional debt that will encumber Spain will be more than it can afford.<sup>16</sup> Prior to the election, Rajoy did not support a bad bank program, but sources have stated that Rajoy "has asked for at least two papers from academics on how to create" a bad bank.<sup>17</sup> While which solution Rajoy will ultimately employ to resolve the Spain's financial issues is uncertain, the current financial outlook remains very grim.

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<sup>9</sup> *Id.*

<sup>10</sup> *Id.*

<sup>11</sup> See source cited *supra* note 3.

<sup>12</sup> *Id.*

<sup>13</sup> *Id.*

<sup>14</sup> See Sonya Dowsett, *More Bank Bail-Outs Loom for New Spanish Government*, REUTERS.COM (Nov. 24, 2011, 7:50 AM EST), <http://www.reuters.com/article/2011/11/24/spain-banks-idUSL5E7MN1HQ20111124>.

<sup>15</sup> *Id.*

<sup>16</sup> *Id.*

<sup>17</sup> See Charles Penty, Emma Ross-Thomas, & Sharon Smyth, *Spain's Rajoy Said to Ask for Proposals on Creating Bad Bank*, BUSINESSWEEK.COM (Nov. 27, 2011, 7:37 AM EST), <http://www.businessweek.com/news/2011-11-27/spain-s-rajoy-said-to-ask-for-proposals-on-creating-bad-bank.html>.