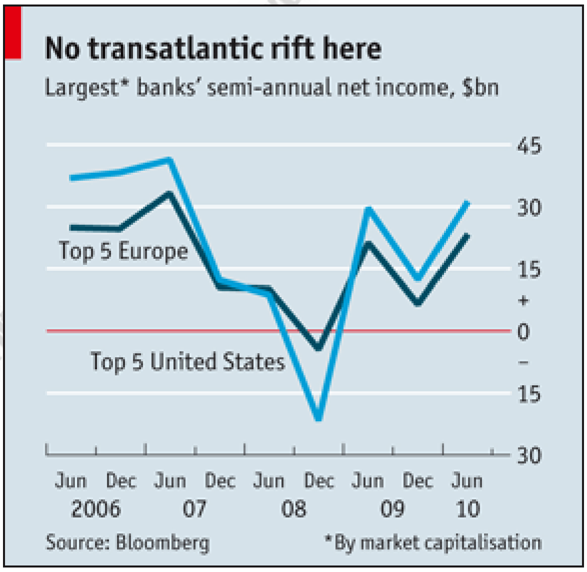
Letting the bottom line talk

Europe's banks are making money hand over fist. How odd.

A FEW weeks ago Europe's banks were in real trouble. Many struggled to borrow from their peers or from capital markets amid concern that bad debts could soar or that faltering government finances in Europe could start toppling them like dominoes. Now investment analysts are falling over one another to raise their profit forecasts and slap "buy" recommendations on the stocks.

That has less to do with the results of the relatively lenient "stress tests" the banks were subjected to in July, although they clearly played a part, than with the revelations that the first half of 2010 was highly profitable. Among the firms that comfortably beat analysts' forecasts were Deutsche Bank, UBS and BNP Paribas, the biggest banks in Germany, Switzerland and France respectively.

The main reason is that loan losses are falling quickly for most banks. At HSBC, a big British bank that burned its fingers playing with consumer finance in America, loan losses fell by 40% in the first half from the previous six months. At BNP they fell by 19% in the second quarter from the prior one. The trend is far from universal. UniCredit, Italy's biggest bank, posted a lower profit because of rising impairments on loans, many of which were in central and eastern Europe. Nor is it a uniquely European phenomenon. American banks benefited from a similar trend (see chart). But it is particularly pronounced at those firms that got into real trouble. Germany's Commerzbank said it expected to make a full-year profit. In Britain, Lloyds Group, which was bailed out too, returned to the black. The "bad bank" that was split off from Northern Rock (which was the first European bank to be nationalised in the financial crisis) also reported a first-half profit, although unfortunately its sister "good bank" didn't.



CEBR, an economics consultancy, was sufficiently impressed by the general turnaround to predict that the British government would make a profit of £19 billion ($29.7 billion) on banking bail-outs. Other countries hit hardest by the financial crisis also seem to have turned a corner. Analysts at Credit Suisse reckon that banks in Ireland may be especially profitable in coming years because competition has withered as a result of the crisis. The main remaining Irish lenders have a lock on as much as 60% of the market. British banks, which consolidated during the crisis, also face less competition.

European banks have benefited from relatively benign conditions not just in their home markets, but also abroad. Some of Europe's biggest banks such as HSBC, Santander of Spain and Britain's Standard Chartered have significant exposure to emerging markets, where growth prospects have remained strong. Although investment-banking revenues have declined everywhere compared with a year ago, the drops have been less sharp in Asia. Meanwhile commercial lending in Asia and Latin America has recovered smartly as businesses there have got their wind back.

The solid earnings reported by many European banks in the first half should ease jitters in credit markets about their solvency and underscore their ability to earn their way out of trouble—something the stress tests modelled, but in a way few investors found believable. Barclays, for instance, sailed through the examination, with regulators judging that it would have more capital in two years' time than now, because of strong underlying earnings. Its results on August 5th, which showed decent profits despite a slowdown at its investment bank, helped bolster this view.

Still, enthusiasm about the health of the region's banks should be tempered by the fact that many are still on government-backed life support and that the next few years are likely to be tough. Analysts at Moody's, a rating agency, fret that many more loans may go bad this year and next as unemployment weighs on countries such as Spain and that many banks will struggle to raise new finance as existing loans fall due. Europe's banks may have shown that they are more alive than dead, but their recovery is far from assured.

Fonte: The Economist, Aug. 5th 2010. Disponível em: <www.economsit.com>. Acesso em: 12 ago. 2010.