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# S.&P. Warns Bank Plan Would Cause Greek Default

By DAVID JOLLY

PARIS — Greece risks being judged in default on its debt obligations if banks are forced to bear part of the pain, Standard & Poor's said Monday, suggesting that current proposals for rescuing the euro zone's weakest member may have to be reconsidered.

In particular, a plan proposed by the French government and banks "could require private sector debt restructuring in a form that we would view as an effective default," S.&P. said in a statement.

The effects of a Greek default would be felt around the world. The country's debt of €330 billion might not be large enough in itself to set off a renewed financial crisis, but once the precedent of a euro-zone default had been set, investors would likely abandon the debts of other struggling members, including Portugal and Spain.

More worryingly, Western banks, including the giants of Wall Street, have built a tower of credit default swaps — essentially insurance — on the debts of those countries, and the cost of paying up in a default would be huge. While the French and German banks have the biggest direct exposure to Greek's debt, it is American banks and insurance companies that would [have the largest obligations](#) to cover payments to those holding the swaps.

A finding by the credit ratings agencies of default would also require the E.C.B. to impose discounts, known as haircuts, on the Greek debt it has accepted as collateral. That would inflict more financial pain on banks holding that debt.

Euro-zone finance ministers agreed over the weekend to provide Athens with financing of €8.7 billion, or \$12.6 billion, from the €110 billion bailout agreed to last year, to help the Greek government function through the summer. The new aid eliminates the prospect of a near-term default.

But the finance ministers put off the question of how to provide a second bailout, reportedly valued at up to €90 billion, to keep the country operating through 2014, when it is hoped that Greece will be able to return to the credit markets.

The thorny issue of how to share the pain with the private sector suggests that discussion of the second bailout could continue for months.

Nicolas Sarkozy, the French president, announced June 27 that French banks had agreed to a plan under which the banks would reinvest most of the proceeds of their holdings of Greek debt maturing between now and 2014 back into new long-term Greek securities.

“If it wasn’t voluntary,” Mr. Sarkozy said at the time, “it would be viewed as a default, with a huge risk of an amplification of the crisis.”

Germany’s biggest banks have also agreed to roll over some of their Greek debt holdings.

But Standard & Poor’s said Monday that it “views certain types of debt exchanges and similar restructurings as equivalent to a payment default”: when a transaction is seen as “distressed rather than purely opportunistic” and when it results “in investors receiving less value than the promise of the original securities.”

Both conditions would appear to be met by the French proposal, it said.

S.&P. has already cut Greece's long-term rating to CCC, deep in junk territory.

European officials are anxious to avoid setting off a default, Gilles Moëc, an economist at Deutsche Bank in London, said, because that could lead to a crisis in relations with the European Central Bank.

The E.C.B., which itself holds billions of euros worth of Greek debt, has said it could only accept the participation of bondholders in any restructuring if it were “entirely voluntary.”

The central bank — which has been helping Greece by buying its debt on the secondary market — “doesn’t want to jeopardize publicly its balance sheet anymore,” Mr. Moëc said. “It’s one thing to say they’ll accept Greek government bonds, it’s another thing to have something on their balance sheet that has ceased to pay, which is the definition of default.”

“It doesn’t mean the Greek securities are not going to be paid,” he said, adding: “The E.C.B. would be able to accept them if the final structure was relatively healthy. One thing the E.C.B. doesn’t want is any infringement of its right to decide on the collateral that it accepts.”

*This article has been revised to reflect the following correction:*

***Correction: July 4, 2011***

*An earlier version of this article misstated the timing of Standard & Poor's downgrading of Greek debt to CCC from B. It occurred on June 13, not Monday.*



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