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**Spanish Officials Hailed Banks as Crisis Built**

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As Spain edged closer to a real estate and banking crisis that led to its recent bank bailout, Spanish financial leaders in influential positions mostly played down concerns that something might go terribly wrong.

The optimism of Spanish central bankers who went on to top jobs at the [International Monetary Fund](http://topics.nytimes.com/top/reference/timestopics/organizations/i/international_monetary_fund/index.html?inline=nyt-org) echoes the attitudes of officials in the United States who misjudged the force of a housing collapse several years ago that crippled banks and the economy. And it underscores the complications that can arise when government officials take watchdog roles at international agencies that pass judgment on the policies they once directed.

Spain’s travails have now become central to the festering financial problems in Europe. The country’s biggest mortgage lender has failed, and European leaders are scrambling to prevent the Continent’s crisis from spreading further.

“The I.M.F. should be saying unpleasant things to countries to get them to reform,” said Jonathan Tepper of Variant Perception, a London-based research firm that in 2009 published [one of the first reports](http://blog.variantperception.com/wp-content/uploads/2012/01/VP-Spain-2009.pdf) to warn that Spanish banks were in serious trouble. “They have been quite late in Spain.”

From their lofty perches, first at Spain’s central bank and then as the I.M.F.’s top executives assessing global banking risk, José Viñals and Jaime Caruana were well positioned to sound alarms about the looming bank debacle.

But at a news conference in Washington in April 2010, when analysts were raising red flags about failing Spanish real estate loans, Mr. Viñals — who a year earlier had succeeded Mr. Caruana — offered assurances. The Spanish system was “fundamentally sound,” he said, and its needs for cash “very small.”

A year later, as the banking crisis showed little sign of improving, Mr. Viñals again called for calm, saying the market panic that had led to bailouts in Ireland and Portugal would not infect Spain.

Now that the recent failure of Bankia, the big mortgage lender, has prompted a 100 billion euro (about $125 billion) European rescue, it is clear that Mr. Viñals’s forecasts were too sanguine.

Mr. Caruana was no more prescient. Pressed at an I.M.F. news conference in July 2008 about falling house prices in Spain, he acknowledged there might be loan losses. But he said, “The financial system in Spain is able to cope with that and is properly capitalized.”

It is not that the I.M.F. was not paying attention. Under Mr. Caruana and then Mr. Viñals, the organization’s economists produced thousands of pages of analysis that, in real time, chronicled Spain’s unspooling bank crisis.

The I.M.F. says that it is not a regulator and that its economists and officials warned early and often on the need for Spain and Europe to address its banking problems.

In assessing financial risks worldwide, Mr. Viñals highlighted challenges faced by savings banks, or cajas, and he backed the efforts of his former colleagues at the Bank of Spain to bring order to the sector — such as the merger of seven cajas to form Bankia in 2010 — although he often urged them to move faster.

Certainly, Spanish officials were slow to acknowledge the depths of the problem.

In early May, Rodrigo Rato, then the executive chairman of Bankia, told journalists that the bank was in a situation of “great robustness, both in terms of solvency and liquidity.” Even after the bank’s bailout a few days later, Spain’s economy minister predicted that no more than 15 billion euros of public funds would be required to clean up the banks.

Mr. Caruana and Mr. Viñals, who declined to comment for this article, were not the only government officials to make the transition from Madrid to the I.M.F.’s headquarters in Washington.

Most prominent by far was Mr. Rato, now better known for his disastrous two-year run at the helm of Bankia. In 2004, he was picked to lead the I.M.F. after winning global recognition during an eight-year run supervising Spain’s growth burst as the country’s economy minister.

Until he left the fund three years later, Mr. Rato was better known for praising Spain’s economic miracle — one that relied largely on revenue driven by real estate to drive growth and balance budgets — than questioning its sustainability.

He considered himself the intellectual father of that miracle, as he made clear [in a 2004 speech](http://www.imf.org/external/np/speeches/2004/112504b.htm), citing his reforms as marking “a new era in economic policy” for Spain. Mr. Rato, too, declined to be interviewed for this article.

There were many others, of course, who did not foresee the Spanish banking blowup. Topping the list is Europe’s main bank overseer, the European Banking Authority.

In December 2011, the authority concluded that Spain’s two strongest institutions — Santander and BBVA — would need to raise more money than the 1.3 billion euros that was required of Bankia, which would need to be rescued just six months later.

And as the United States financial crisis made clear in 2008, it is no easy task to anticipate the point at which a decline in housing prices will ignite a financial collapse.

In Spain, the increase in house prices between 2000 and 2007 was particularly extreme — so much so that as early as 2006, a team of inspectors within the Bank of Spain sent a cautionary report to the government.

The study criticized the “passive attitude” of Mr. Caruana, who led the central bank from 2000 to 2006, and the extraordinary acceleration of loans to homebuyers and real estate developers.

The inspectors also warned of Spanish banks engaging in unusually heavy short-term borrowing at levels far beyond their deposits.

The 2006 report painted a much darker picture than Mr. Rato and the I.M.F. saw a short time later when the fund made its own assessment in 2007 of Spain’s economic and financial health — and the Bank of Spain’s ability to rein in excesses.

The analysis praised the “dynamism of Spain’s financial system,” and said that “its strong, prudential supervision and regulation remain a forte of the economy.”

Annual I.M.F. reviews conducted by the European department did become more critical, highlighting on numerous occasions Spain’s overreliance on real estate for its growth and warning frequently that the lax lending practices of the cajas needed to be revamped.

Although it was Mr. Viñals’s financial risk department that produced the most recent stress test on the banks, fund officials said that he recused himself from its preparation given his past ties to Spain’s central bank.

“The I.M.F. has consistently and clearly flagged the dangers that exist in Europe and the urgent need to recapitalize banks,” said William Murray, a spokesman for the I.M.F. “Anyone who claims the contrary is either misrepresenting the public record or just does not understand how the fund works.”

People who know Mr. Viñals, a Harvard-trained economist, describe him as smooth and politically skilled — his name emerged recently as a potential candidate to run Spain’s central bank — who during his stint as deputy governor at the Bank of Spain oversaw its international operations. .

A cautious technocrat by nature, Mr. Viñals and his colleagues are to some extent constrained in how much change they can demand from a government — especially in the sensitive area of bank supervision — before the country in question seeks a loan.

Analysts say that former Bank of Spain officials at the fund should have made more aggressive use of its bully pulpit in light of their broad familiarity with the Spanish banking system.

Bruegel, a Brussels-based research organization, recently conducted [an audit of the I.M.F.’s track record](http://www.bruegel.org/publications/publication-detail/publication/629-an-evaluation-of-imf-surveillance-of-the-euro-area/) in assessing euro area risks before and after the crisis.

Bruegel’s conclusion on Spain is that in the early going the fund was too slow to warn that tax revenue stemming from the real estate boom, and the budget surpluses they produced for Madrid, were illusory. Nor was it ever contemplated that one of Europe’s largest economies would experience a capital flight crisis similar to that in Mexico or Thailand.

“You did not see the sense of alarm,” said Jean Pisani-Ferry, the lead author of the report, which also said the I.M.F. oversight later improved significantly. “There was a sense that Europe was different.”

Experts say that Mr. Viñals and Mr. Caruana may not have warned earlier on Spain because of the trust they and others in the international financial community had in the Spanish central bank’s ability to restructure the cajas without having to resort to a bailout.

“It is fair to say that the I.M.F. may have thought that the Bank of Spain was going to take care of it,” said Luis Garicano, an economist at the London School of Economics.

In fact, up through the 2008 global financial crisis, Bank of Spain officials had become the toast of the international regulatory circuit for their innovations. Most notable of those was a so-called dynamic provisioning policy, a set of rules that forces banks to set aside extra cash during good economic times to protect against the inevitable rainy days.

For a time, Spanish financial institutions were hailed as paragons of responsible banking — having set aside over 110 billion euros in reserves.

But José Garcia Montalvo, a real estate specialist based in Barcelona, says that this figure could have been higher — and the banks better prepared for the housing collapse when it came.

The reserves proved insufficient, he said, because the Spanish central bank in 2004, led then by Mr. Caruana, succumbed to bank lobbying and pressure from Europe by halving the amount that banks had to set aside to 15 percent of overall loans, from 30 percent.

From that point, Spanish bank lending, already growing at 14 percent annually, went into overdrive — up 27 percent in 2005 and an additional 25 percent in 2006.

Mr. Caruana’s career has since thrived. After just three years at the I.M.F., he left in 2009 for one of the plum global finance jobs: chief executive of the Bank for International Settlements, the Basel-based regulatory body that serves as a forum for the world’s central banks.

Last weekend, [in a speech](http://www.bis.org/speeches/sp120624a.pdf) that explored the roots of the financial crisis, Mr. Caruana highlighted the economic distortions caused by frantic real estate lending, and he called for banks to be quicker to recognize losses and raise capital — although he did not mention Spain by name.

As for Mr. Rato, he left the fund abruptly in 2007, worked as a senior investment banker for Lazard in Spain and took charge of the entity that would become Bankia in 2010 — before being forced out last month.

Mr. Viñals continues to supervise global banking and financial risk at the I.M.F.

*Raphael Minder contributed reporting.*