IMF warns of further recession risks

September 23 2009

from FINANCIAL TIMES

Banks round the world have still to reveal about half of their likely losses resulting from the financial and economic crisis, the International Monetary Fund said on Wednesday, warning that there was still a "significant" risk of another downward lurch in the global recession.

The IMF described credit risks as remaining "elevated" even though financial conditions have improved significantly since spring.

It said these risks, alongside weakened banks, were likely to depress the availability of new credit and damp the global economic recovery unless significant additional capital was raised to improve the health and lending capability of banking systems.

In its twice-yearly Global Financial Stability Report, published on Wednesday in Istanbul, the IMF, estimated the ultimate losses in the financial system would total $3,400 billion between 2007 and 2010, an improvement from the $4,000 billion estimate it published in April.

The improvement in the prediction of likely losses reflects growing confidence in financial markets and higher assets prices, which have reduced mark-to-market losses on banks' books, and an improved economic outlook, with lowered estimates of credit losses.

Don't Miss

- G-20 leaders meet to bolster global economy

Even so, the IMF warned that much still needed to be done to secure a recovery and to ensure that renewed stresses in the financial system did not restart the vicious spiral of banking losses, rationed credit, deeper recession, increased defaults and further banking losses.

Within the banking systems, the IMF estimates that losses will total $2,800 billion alone and that banks have so far recognized only $1,300 billion of those losses. "U.S. domiciled banks have recognized about 60 percent of anticipated writedowns, while euro area and UK domiciled banks have recognized about 40 percent," the report said.

The largest proportionate losses in banks are in the U.S. and UK, where losses on residential loans and commercial property, the loans with the highest default rates, account for a greater proportion of banks' balance sheets.

Although banks have been profitable this year as their borrowing costs have fallen with exceptionally low interest rates and the rates charged on lending have remained higher, the IMF warned that this happy position for banks might not last. "In the medium term, banks are likely to suffer reduced margins from paying more for deposits and incur higher interest costs," it said, so greater capital-raising measures were still necessary.

But the capital-raising exercises by banks and recapitalisation by government already undertaken have made banks more resilient to the losses they are likely to incur, the IMF added. Capital will be drained by future losses, but the emergency measures implemented so far meant that "banks in all regions have achieved a degree of stability in their capital positions".

Massive public deficits also complicated the financial stability picture, the IMF warned. They implied that total borrowing needs in certain countries, particularly the U.S. and UK, will exacerbate the difficulties in raising finance for the private sector, and imply the need to raise finance from abroad, potentially undermining the dollar and sterling, or raising long-term market interest rates.

"In terms of regional vulnerability, the UK appears most susceptible to credit constraints ... given its significant reliance on the banking channel and the projected sharp decline in domestic bank balance sheets, as well as substantial public financing needs," said the IMF.

http://edition.cnn.com/2009/BUSINESS/09/30/imf.recession.warning.ft/index.html