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Europe Lending Woes Deepen

Two Banks Tap ECB for Dollars; Companies Look Beyond Euro Zone for Loans

By SARA SCHAEFER MUÑOZ, CARRICK MOLLENKAMP and BRIAN BLACKSTONE

Europe’s financial crisis intensified Wednesday as banks moved to obtain more dollars for loans to their U.S. customers, and some nervous corporate clients began looking to banks outside the euro zone for loans.

Tensions in the 17-nation euro zone are increasing despite attempts by central banks to pump badly needed dollars into the region, as U.S. sources have shrunk. On Wednesday, the European Central Bank said two banks had tapped it for $575 million, only the second time in six months the ECB had doled out dollar funding. The names of banks that tap the ECB are kept confidential.

European banks need the U.S. currency to fund loans they have extended to U.S. companies and consumers. European banks also need dollars to repay past borrowings they made in dollars, such as loans from U.S. money-market funds.

As expected, Moody’s Investors Service downgraded Société Générale’s long-term debt by one notch to Aa3—three notches below triple-A—with a negative outlook. It lowered Crédit Agricole’s rating to Aa2, one notch higher, and also kept it on review. Moody’s maintained BNP Paribas’s rating at Aa2 but kept it on review for a possible downgrade. Weaker credit ratings can mean it costs a company more to borrow.

The deepening problems illustrate how sovereign-debt concerns in Greece, Ireland and other places, which date to early last year, have spilled into the broader market. While problems haven’t reached 2008 levels, they have caused increasingly tough consequences for Europe’s banks.

Some French banks’ corporate clients, for example, have sought financing from banks outside Europe to lessen their reliance on French banks as a hedge in case lending dries up, according to people familiar with the situation.

The clients include energy and commodity providers, from oil giant BP PLC to midsize companies, which need liquidity for day-to-day operations, such as the transportation of oil and other commodities. Société Générale and BNP are among the key providers of this financing, which accounts for some 10% to 15% of their annual profits, according to analyst estimates.

Now, several major companies that have relied on them in the past are turning elsewhere. "If European markets close, they don’t want to have a funding gap. They want to be ready,” said a person involved in some of the talks.

U.S. banks, stuffed with deposits thanks to U.S. networks of branches and access to central bank money, have received requests from European companies seeking loans. One energy company is talking with Citigroup Inc. about obtaining a $1 billion credit line for its shipping operations amid fears that renewing credit with European lenders could prove too expensive, according to a person familiar with the matter.

It isn’t just natural-resources companies that have been tapping banks outside the euro zone. Some European banks have for the first time approached Japanese bank Nomura Holdings Inc. for ideas on how to access dollars from investors in Asia, according to a person familiar with the matter.

However, BNP Chief Executive Baudouin Prot said he isn’t seeing evidence of big European companies lining up alternative financing.

European banks have lost access to more than $700 billion in U.S.-dollar funding—short-term IOUs and interbank loans—over the past year from U.S. money-market funds and others worried about exposure to Greece and other troubled European economies, according to J.P. Morgan Chase & Co. and CreditSights research. That has forced the banks

to curtail dollar-denominated lending and find dollars far afield, such as in the Middle East. Banks need dollars to fund dollar-denominated loans and other obligations.

"Things are deteriorating," said Joseph Abate, a money-markets specialist at Barclays Capital in New York. "This week and certainly probably since August, it seems like their access to unsecured [funding] really has tightened up."

Jonathan Loynes, an economist at consultancy Capital Economics in London, says he fears the mix of fiscal belt-tightening, a loss of confidence among consumers and businesses and, now, the risk that financing costs may go higher in parts of Europe will lead to a 0.5% contraction in euro-zone output next year and a further 1% slide in 2013.

"There are growing concerns that we are going back into a credit crunch," he said.

That is partly because U.S. banks and stronger European banks aren't overly eager to fill the lending gap left by French and other banks. Nearly all lenders have seen their funding costs rise at least moderately in recent weeks, and are cautious about lending to companies in Europe's uncertain economic environment, said executives at major U.S. and U.K. banks.

Bank executives and traders said deep pools of liquidity remain. Foreign banks, for example, have parked $848.7 billion at the Federal Reserve.

Still, concerns are growing among U.S. regulators. In an interview with CNBC Wednesday, U.S. Treasury Secretary Timothy Geithner called problems in Europe "a dominant concern." He said the issue matters to the U.S. "because it adds to a caution around the world at a time when...we're still healing from the crisis."

In efforts in the past week to reassure investors and clients, chief executives at BNP Paribas and Société Générale said they are moving to reduce their need for dollars. In one sign, banks still have avenues to obtain dollars, a senior bank trader in London said that in the so-called repurchase market, where banks exchange collateral for dollars, European banks are still able to obtain loans.

Société Générale has said it is cutting back on certain lending, such as loans in the aircraft and shipping industries.

In trading on Wednesday, Société Générale shares fell 2.9%, or €0.515, to €17.385, while BNP Paribas declined 3.9%, or €1.10, to €26.90. Crédit Agricole added 1.2%, or €0.063, to €5.216.

A person familiar with Société Générale's corporate-funding business said that the bank is still providing money to key clients and that its long-term expertise in finance-advisory and related services will keep that part of its businesses strong.

Spanish banks sharply increased borrowing from the European Central Bank in August as a deepening sovereign-debt crisis cut off alternatives for banks in Southern Europe. According to data released by Spain's central bank on Wednesday, gross borrowing by Spanish banks from the ECB hit €81.22 billion in August, up 42% from €57.20 billion in July.

U.S. money-market funds continue to curtail lending to European banks. When the funds do extend IOUs, they are doing so for shorter terms in order to protect themselves, analysts said.

The market where banks provide loans to one another is under stress, according to CreditSights. Bank loans to other euro-zone banks had fallen by €600 billion during a one-year period through June.

A benchmark bank borrowing rate continued to increase. The three-month dollar London interbank rate edged up to 0.3491% on Wednesday, from 0.3471% on Tuesday. In June, the rate was around in 0.254%. Mr. Abate, the Barclays analyst, said earlier this week the rate could hit 0.50% by year end.

The move by Moody's in France wasn't as severe as some investors expected, with BNP Paribas dodging a downgrade and Société Générale avoiding a two-notch downgrade that Moody's warned of in June. Moody's ratings for Société Générale and Crédit Agricole remain above those of other ratings firms.

Moody's factored in potential losses of 60% on Greek sovereign debt for the French banks, much larger than the 21% write-downs they have taken already.

The French government is determined to monitor the banks' efforts to strengthen their equity capital and will guarantee the soundness of the country's financial system, spokeswoman Valerie Pecresse said after the weekly cabinet meeting. Bank of France governor Christian Noyer said any talk of the nationalization of French banks "makes no sense and is completely surreal."

—Guy Chazan and Inti Landauro contributed to this article.