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August 8: Credit Risk - The US Subprime Collapse Stretches into Germany

Location: **New York**

Author: **Lenny Broytman**

Date: **Wednesday, August 8, 2007**

The US subprime disaster has been reeking domestic havoc for close to a year now and according to published reports, the crisis has even begun to make its way across the Atlantic.

The New York Times reports that German lender IKB has fallen victim to the US housing crisis. IKB announced that their chief executive has stepped down and that their recent slump in earnings was a direct result of the subprime situation in the US. The announcements have sent the firm's stocks down more than 20 percent and prompted their biggest shareholder, the state bank KfW, to step in and offer a helping hand.

As is often the case, many are worried that news of IKB's recent woes has the potential to spark unwarranted fear within other German banks, thus needlessly creating similar situations across the board.

Shares of Deutsche Postbank for example, were down 1.2 percent at 55.06 euros by mid-afternoon two days ago and were even lower earlier that morning, clocking in at 52.60 euros. Another entity experiencing trouble in Germany was international property financier Hypo Real Estate, who dropped 3.5 percent to 44.71 euros. Commerzbank was down 2.7 percent with a price of 30.84 euros.

According to Simon Adamson, an analyst at the credit research firm CreditSights, a lot of these current issues have stemmed from the fact that banks sometimes fail to adequately explain their obligations which result from certain types of structured finance deals.

"This announcement from IKB will confirm the fears of a lot of investors that we don't really know what the scale of the problem is," he said. "If you look through banks' annual reports you will not find information to tell you what this potential liability is and that is one of the main reasons that the market has been so worried recently."

There are others of course, who consider IKB's recent financial blunder to have no immediate connection to the US subprime situation. "We don't see any significant impact on the big German banks directly from U.S. subprime mortgage problems," said Standard & Poor's analyst Stefan Best.

According to Thomas von Luepke, chief German banks analyst for Fitch Ratings, many of the German banks are fully ready to handle a possible short-term hit that may or may not come their way. BaFin, the German financial watchdog, chimed in by saying the IKB deal ensured that there would be absolutely no fallout for the country's banking system.

Whether the statements are genuine or are designed merely for damage control purposes in Germany remains to be seen.
