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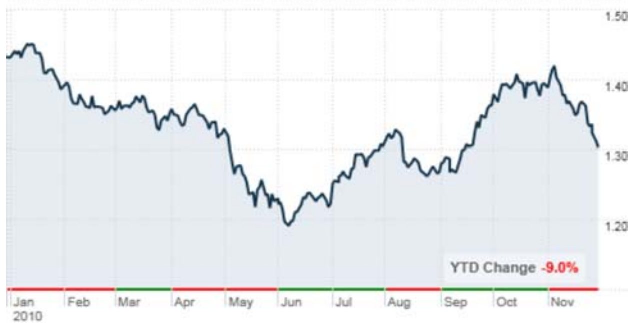
Only one of the PIIGS matters. S is for Spain.

So much for a weak dollar

The euro has fallen against the dollar again as sovereign debt fears for the PIIGS have returned.



By Paul R. La Monica, assistant managing editor

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NEW YORK (CNNMoney.com) -- The market has been referring to the problem nations in Europe all year as the PIIGS. But maybe it should be the piigS.

Excuse my brief lapse into a quasi-ee cummings style of writing. But there is a reason for it. While concerns about the five most troubled countries in Europe are valid, the country that really matters most is Spain.

Investors have been extremely nervous about the sovereign debt crisis in Europe. Three of the five PIIGS countries -- Portugal, Ireland and Greece -- have gotten the most attention. Italy is also a concern.

But some experts said that the market may be able to deal with more problems in any of those nations as long as they don't spread to Spain.

"The global economy likely can absorb defaults in Ireland and Greece. The global economy can probably deal with Portugal as well," said Dr. Robert Shapiro, chairman of Sonceon, an economic advisory firm in Washington. "But then you get to Spain. It's the ninth largest economy in the world."

Shapiro, who served as Under Secretary of Commerce for Economic Affairs in President Clinton's administration, said the big fear is that a default in Spain could significantly hurt German and French banks since they hold more than $600 billion in Spanish debt, a large chunk.

And that could create a scenario similar to the Wall Street meltdown of 2008.

"A default in Spain would endanger French and German banks and that would have serious consequences for U.S. financial institutions because they all have counterparty risk," Shapiro said. "Just as Lehman Brothers spread to Europe, a European banking crisis would spread to the

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United States."

If only success in the world of sports translated into economic might. With Rafael Nadal winning three of the four tennis Grand Slam tournaments and Spain's soccer squad claiming the World Cup, it would be unfortunate if 2010 also turned out to be the year that Spain doomed the global economy to another downturn.

Fortunately, Shapiro does not think that a Lehman or Bear Stearns-like collapse for Spain and European banks is that likely. But he doesn't think the threat of a meltdown should be dismissed either, pegging the odds of this worst-case scenario at about 15% to 20%.

He said investors should still be worried about the debt situation in Italy even though the market has not been overly concerned about problems there just yet.

Jeffrey Roach, chief economist and investment committee chair with Horizon Investments in Charlotte, N.C., also said that the problems in Spain bear watching.

He said investors should not be surprised that Portugal and Ireland could face problems with their debt loads. The worry though is that so much is still unknown about how deep Spain's problems are.

"The story has yet to be played out. The concern is the extent of the risks spread out in Spain," Roach said. "The markets may be surprised if the effects are much broader than what was experienced in the U.S. We all know that Spain, like the U.S., had an unusual housing bubble."

Roach added that Germany will play a key role in determining what happens to the rest of the continent.

"Germany is the only country with the strength to keep the eurozone together and the euro afloat," Roach said. "We need to see Germany remain committed to fiscal responsibility. Once Germany leads the way other nations will follow."

That sounds good on the surface. But there are fears about whether Germany actually has the wherewithal or desire to continue supporting its weaker brethren. There has been some chatter lately that Germany might want to consider leaving the euro behind and bringing back the mark.

One fund manager worries that could have a disastrous impact on the continent.

"The euro can survive but there needs to be a cohesive strategy. If Germany is talking about the euro as if it cannot be sustained, that's a worrisome risk," said Nainesh Shah, senior securities analyst with Roosevelt Investments in New York.

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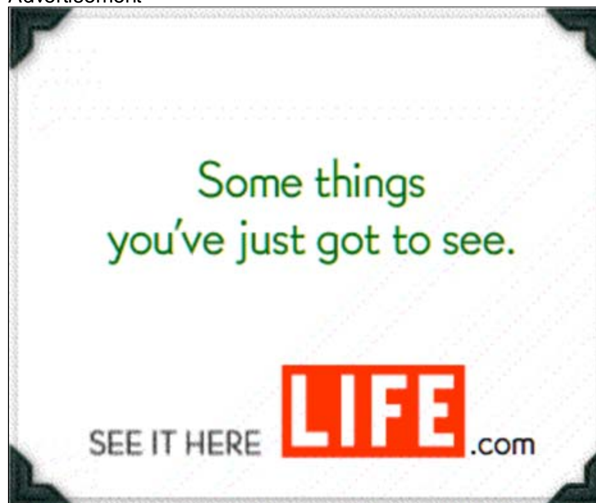

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Shah said that he's not overly concerned about Germany defecting from the eurozone. But he conceded that his firm's **Roosevelt Multi-Cap Fund**, which has the flexibility to invest in all markets around the world, has only two holdings based in Europe.

"We are not significantly worried. But are we uncomfortable with Europe? Yes," Shah said.

So for now, the euro continues to drop against the dollar, despite the Federal Reserve's best efforts to weaken the greenback with its **second round of quantitative easing**.

Shapiro said there is a chance for Europe to avoid creating another global credit nightmare. But it has to be nimble and more proactive.

"This could be a train wreck in slow motion," Shapiro said. "There is no quick solution here. What can the EU do? Our own government made enormous errors by ignoring worst-case scenarios. The EU needs to hold the line at Ireland and Portugal."

The problem is that investors don't seem to have faith that the EU can do that.

- The opinions expressed in this commentary are solely those of Paul R. La Monica. Other than Time Warner, the parent of CNNMoney.com, and Abbott Laboratories, La Monica does not own positions in any individual stocks.

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