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Greek, European woe could cause problems for US

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WASHINGTON —

Your 401(k) could sink again. A plummeting euro may make it harder for American companies to sell goods overseas. Credit could be tightened.

These are all potential complications of a European debt crisis that risks spiraling out of control. And in today's interconnected global economy, Greece's troubles could over time become a headache for all of Europe and by extension, the rest of the world.

That includes President Barack Obama as he faces an already difficult re-election bid, and voters as well, from machine tool makers in Michigan to chemical plant workers on the Gulf coast. Pensioners and home buyers also could be affected.

All this because Greece is at a crossroads, unable to form a government and decide whether it will continue on a path of harsh austerity measures or walk away from its debts and give up on the euro. That would leave many European countries holding their debts and shake the foundations of a currency used by 331 million people.

Here's what a Greek debt default and exit from the 17-nation eurozone might mean for people in the United States:

BANKS:

The short-term financial consequences of Greece defaulting may be limited across the Atlantic. American banks already have sharply reduced their exposure to Greece by more than 40 percent to $5.8 billion, according to the government. Cornell University economist Eswar Prasad said he foresees little immediate blowback for the U.S. financial sector.

But the concern is that market speculation would then fall on the far larger economies of Spain and Italy. Both are deep in the red and heavily dependent on credit markets to stay afloat. And their debts are held by Europe's big banks.

Economists call this threat contagion. Scared investors sell off their assets in Europe's most troubled economies and the governments struggle to access credit while falling into deeper recession. A crisis as bad as Greece's in a bigger nation would have severe global implications.

"Greece is peanuts as far as the United States is concerned," said Uri Dadush, former economic policy chief at the World Bank. "But if Greece leads to the contagion of Spain and Italy, the euro could implode. This is big business for the U.S. We're talking trillions of dollars in direct and indirect exposure to the European banking sector."

Economists cite the example of Lehman Brothers' collapse in 2008 and the financial turmoil that followed. A repeat scenario could see credit lines dry up as banks short of funds limit their risks, making it harder to secure loans for business expansion and home mortgages.

Lending and credit growth remain especially weak in Europe, where over $1 trillion in cheap, three-year loans to financial institutions by the European Central Bank helped stave off a complete credit cutoff. A massive bailout fund has been set aside in case Spain or Italy fails, too, but a default by either country could spell disaster for German, French and other heavily exposed banks. They, in turn, deal extensively with American banks.

"It's a question I don't want to find out the answer to, honestly," Dadush said. "There is a real danger of global depression."

MARKETS:

Many pension funds, insurance companies and other big investors have dumped or written off investments in Greece such as government bonds. But there's no telling how the markets will respond to a default.

For investors who have already faced a half-decade of turbulence, this weekend's failure in Greece to form a new government led Monday to steep market drops across Europe. Britain's FTSE slipped 2 percent, while Germany's DAX was off 1.9 percent and France's CAC 40 fell 2.3 percent. In the U.S., the Dow Jones industrial index was down 0.8 percent at 12,714.

Each round of bad news from Europe raises uncertainty. No one knows how a Greek exit from the euro would work and the financial swings have added to the stress on Europe's economy. And every time stocks plunge and the borrowing costs for troubled countries rise, businesses and consumers grow more cautious. This makes them more reluctant to expand companies or buy more property.

Europe's turmoil "does not bode well for the fledgling U.S. recovery," Prasad said. He predicted that uncertainty in Europe will rattle U.S. financial markets, as happened last year, shaking fragile consumer and business confidence.

Individual American investors should be concerned as well, even if most have little direct exposure to southern Europe. Market declines across Europe could drag down Asia and the United States, hitting portfolios and retirement funds. And when people feel poorer, economies shrink.

TRADE:

Exports have been a bright spot for the U.S. economy, and Europe has played a big role. More than half of U.S. foreign investment and a fifth of all American exports go to the European Union. A significant slowdown there could mean less revenue for U.S. companies, less expansion at home and lost jobs for American workers.

"Right now, the best case scenario in Europe is a recession," said Chad Moutray, economist at the Washington-based National Association of Manufacturers. "Any of the worst case scenarios threaten our growth strategy."

U.S. manufacturers have added 167,000 jobs over the last five months, but a European economic collapse would hamper growth in two ways. It would weaken Europe's general demand for goods. And if investors flee Europe for safer bets elsewhere, the value of the euro would sink and make American products more expensive.

Many major U.S. companies not only export but have large operations in Europe. General Motors and Ford both make cars there and have faced slack sales in a competitive market that offers manufacturers little pricing power.

Unemployment rates of over 50 percent for people under 25 in Spain and Greece have undermined the market for first-time car buyers in those countries. Unemployment across the eurozone is already at 10.9 percent, a record since the common currency was introduced in 1999. If that figure worsens still, it would further dampen American sales.

U.S. POLITICS:

Any new economic crisis presents a problem for Obama, even if Europe's problems are largely beyond his control.

Higher unemployment, a surge in gas prices or collapsing stock portfolios in the United States would undermine the president's argument that he has slowly but surely guided the U.S. out of its worst downturn since the Great Depression. His November showdown against Republican candidate Mitt Romney is still too close to call and will hinge on the economy.

"He's put us on a road to become more like Greece," Romney said last month, hammering away at a campaign message that has focused on debt, unemployment and the lackluster state of the American economy.

Even if a Greek default may also undermine the harsh austerity tactics championed by some Republicans, Obama would face a severe backlash if Europe's ills were to cause the U.S. to slip into a double-dip recession. That seems unlikely for now, but Obama is already challenged by unemployment hovering around 8 percent and an economy only expected to grow by about 2.5 percent this year, still slow for an economic recovery.

Yet Obama can do little about Europe's ills. His administration insists that Europeans should fix their own problems without U.S. assistance - a stance it must take because there is no appetite for U.S. taxpayers to help bail out Greeks or anyone else in Europe. Washington has pressed Europe to stimulate their economies more.

But Obama can't even control the U.S. economy, after pushing through a $787 billion stimulus package in 2009 that critics charged with not doing enough to create jobs and spur economic recovery.

"As has happened several times before, when our economy gets going, events elsewhere can intervene and throw a monkey wrench in the works," Obama senior campaign adviser David Axelrod recently said. "We're not hoisting a `Mission Accomplished' banner. We know there is a lot of work left to be done and the headwinds are part of that equation."

McHugh reported from Frankfurt, Germany. AP Economics Writer Paul Wiseman contributed to this report.