WRAPUP 1-Banks seen saving Spain property firms from falling

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LONDON, April 2 (Reuters) - Banks seeking to avoid multi-million euro defaults and to stem the tide of Spain's property meltdown are likely to rescue two of the country's biggest property companies from the risk of insolvency.

Spanish banks La Caixa and Banco Popular said on Wednesday they were considering a debt-for-equity swap that would leave them in control of Inmobiliaria Colonial.

Meanwhile, a 5 billion euro ($7.82 billion) debt restructuring for Martinsa Fadesa is in the works, sources familiar with the situation told Reuters.

"These talks would avoid the insolvencies, which would have very negative consequences for the economy and for the reputation of the companies," said **Carlos Gila**, managing partner at Gila & Co., a turnaround practice in Madrid.

Analysts said Spain's highly-fragmented property market was likely to see many more potential insolvencies in the coming months, particularly among smaller firms, whose failure would hurt banks less than if big fish like Colonial or Fadesa fell.

After a decade in which house prices have tripled, Spain's now weakening property sector has been savaged by the global credit crisis. Banks are turning off the credit tap to both buyers and developers, forcing an increasing number of property firms to file for creditor protection.

The crisis has worsened since the Socialists were re-elected in an election on March 9, prompting charges from the conservative opposition that the government hid the true scale of Spain's economic woes. The refinancing of a 1.6 billion euro debt owed by Barcelona-based Habitat was only achieved after the government leaned on banks to stop it going bankrupt just before the election, sources close to the situation said.

Firms such Cosmani have already filed for insolvency. Others, including Fbex, are desperately negotiating with creditors to avoid the courts.

Debt in Spanish real estate companies is being traded on London's distressed debt desks for as little as 50 pence in the pound, sources familiar with the situation have told Reuters, as lenders, once chasing hefty returns, rushed to exit.

Banks may favour a debt restructuring rather than insolvency as lenders need to make provisions of as much as a 100 percent of the value of the loan if a company files for insolvency.

Saving banks, controlled by Spain's regional governments, might be keener to see builders survive than fail because of the inevitable unemployment that brings.

However, the emergence of creditors like more hard-nosed hedge funds will make negotiations far harder, analysts said.

Spanish real estate companies borrowed heavily and expanded aggressively over the past few years on the basis that housing prices would continue their run after tripling in a decade.

Now interest rates are higher, financial costs are up and sales are falling -- down 27 percent year-on-year in January.

Lenders to Colonial's largest shareholders assumed share prices of more than three euros, but the stock is now worth less than one euro.

The construction sector has been the motor of Spain's economy for the past 10 years and accounts for almost 20 percent of GDP but the crisis on Tuesday forced the Bank of Spain to cut its 2008 growth forecast to 2.4 percent from 3.1 percent previously and to 2.1 percent in 2009. (Editing by Paul Bolding)