SHOULD GREECE STAY OR GO?

Jeremy Schwartz — Global Chief Investment Officer
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Professor Jeremy Siegel and I spoke with University of Texas professor James Galbraith on February 27. Professor Galbraith has an inside look on the ongoing Greek debt dynamics, as he became friendly with the current Greek finance minister Yanis Varoufakis as a colleague at the University of Texas. Our conversation touched on a number of key issues surrounding the eurozone conflict. ***We asked Galbraith what he learned from spending time with Varoufakis in Brussels and Athens during Greece's negotiations with the EU. He outlined the following:*** The agreement between the Greek government and its creditor partners allows for financial breathing room, with less anxiety over the Greek banking sector and its access to liquidity, and provides some space for negotiations over specific terms between Greece and its creditors. Galbraith highlighted three major points: 1. The Greek government went in determined to change the direction of its spending policies. Previous governments had taken orders from European institutions. The new government has had notable accomplishments thus far and has changed the mood for a couple of other European economies in similar situations. 2. This Greek government came to power under difficult circumstances and had to work with an unnecessarily accelerated time line. There was an artificial deadline of Feb 28 to reach a deal with Greece's creditors—as the previous government had turned down a six-month extension of a debt relief program, hoping to aggravate the circumstances for the current government in hopes they may fail. 3. Pending the outcome of further negotiations in July, the new government will have a four-year mandate to make the needed economic reforms. ***A number of people think the Greeks came away empty-handed from the most recent negotiations. Professor Siegel believes the Greeks gained something in the negotiations with the Europeans: they received flexibility. He also believes the Germans would never force Greece out of the eurozone—we asked for Galbraith's take:*** Galbraith concurs—the Greeks do not want to abandon the euro. There are important forces in Germany that would not mind if Greece left the eurozone (including German finance minister Wolfgang Schaeuble, who Galbraith believes would be happy to see them leave), but Galbraith does not think the German government wants to be saddled with the task of forcing the Greeks out, especially German chancellor Angela Merkel, the key figure. ***One of the key factors impacting Europe revolves around the politics in a number of elections this year. Galbraith noted:*** The governments of Spain, Portugal and Ireland were resistant to making any concessions to Greece due to elections they are facing in their own countries—and the growth of political parties that are rallying on the same type of anti-austerity platform that won the new Greek government the election. The Portuguese government feels especially threatened if Greece is able to bypass the strict austerity regime, as Portugal has enacted its own austerity measures. Galbraith emphasized the serious social implications of the Greek austerity: Greeks faced a 40% reduction in health expenditure; many Greeks were having trouble getting food, due to the many cuts; and some Greeks were being thrown out of their homes. But Galbraith believes we are seeing a big pickup in public mood with the new Greek government. Looking forward: Because the Greece economy has contracted 25%, Galbraith believes there's significant room for growth. **Summarizing the Greek Situation** Professor Siegel noted that the recent flare-up in Greek debt crisis did not spill over to the other peripheral European countries, as it had a few years earlier. When the Greek 10-year bond yields spiked above 11% at the end of January, it hardly caused a ripple in Spanish bond prices and yields, which is very different from the situation just a few years ago.[1] Professor Siegel's bottom line for investors as the European markets shrug off this Greek news to deliver strong returns for the start of 2015: investors are comfortable with the other peripheral European countries (such as Spain and Italy), and the Greek situation is not viewed as a systemic volcanic crisis by most investors. *Read the Conversations with Professor Siegel Series here.* [1]Source: Bloomberg.

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Eurozone (EZ) : Consists of the following 18 countries that have adopted the euro as their currency: Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Luxembourg, Malta, the Netherlands, Portugal, Slovakia, Slovenia and Spain (source: European Central Bank, 2014).

10-year government bond : a debt instrument backed by a government guarantee with an original maturity of 10 years.

Yield : The income return on an investment. Refers to the interest or dividends received from a security that is typically expressed annually as a percentage of the market or face value.

Peripheral European countries : Portugal, Ireland, Italy, Greece and Spain.