Country Report

Greece

March 14, 2011

# EU summit decisions: Greece in a Turning Point

- Eurozone leaders, unexpectedly, took significant decisions towards a 'comprehensive solution' to the region's debt crisis. According to their resolutions, among others, EU's financial stability mechanism will increase its capacity and its scope to buy sovereign debt from the primary market.

- Greece got an improvement of the terms of its EUR110bn loan in exchange for a strict, permanent, fiscal discipline as well as the implementation of a huge EUR50bn asset development / privatization program.

- The summit's decisions 1) alleviate default and sovereign debt 'haircut' concerns (at least for the immediate future), 2) reduce the financial burden on the country allowing the government to proceed to a more balanced economic strategy and 3) force Greece to make the necessary reforms in order to proceed to the pledged asset development / privatization program

- These developments should prompt the markets to take a fresh look at Greece. It is upon Greece now to take the necessary actions towards fiscal discipline and structural reforms and to persuade the markets that it is on a 'restructuring' course.

- The reaction of the equity market should be very positive. Our focus is on the banking sector (that holds Greek government bonds), the State-controlled companies (that are in a privatization course) and on companies that are listed in the Athens Stock Exchange but a substantial income stream of their income comes from abroad. These companies are punished because of the 'Greek risk.'

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# Towards Greece's Restructuring

Eurozone leaders during their informal meeting last Friday thrashed out a strategy on how to deal with the region's debt crisis.

In respect of Greece, they decided to:

- extend the repayment period for Greece's EUR110bn loan to 7.5 years rather than 3 years
- lower the interest rate on the EUR110bn loan to an average of 4.2% rather than 5.2%

In return, Greece committed to swiftly implement and conclude a EUR50bn asset development / privatization program and to introduce a strict fiscal framework supported by law.

Directly related to Greece is also the announcement that the EU's financial stability fund will be allowed to buy sovereign debt from the primary markets.

### The ramifications of the decisions for Greece

The implications of the decisions are very significant for the Eurozone and Greece in particular. After a long period of debating, EU leaders took steps towards a 'comprehensive solution' to Europe's debt crisis signaling to the markets that they will take the necessary actions to protect the region from the crisis. The indecisiveness of the EU leaders had led to speculation and increased pressure towards Europe's peripheral economies, including Greece.

Particularly for Greece, these EU decisions are 'game changing' as they 1) help alleviate default / sovereign debt 'haircut' concerns since they provide a safety net to the country in case Greece is not able to access the markets any time soon, 2) give the economy a breathing space, while 3) oblige the country for the introduction of an ambitious EUR50bn asset development / privatization program that will have ripple, positive, effects on the economy.

Specifically the resolutions:

- Quash any default and 'haircut' concerns, at least in the immediate future. The strengthening of the Eurozone's bailout mechanism (the mechanism's capacity increases while it will be allowed to buy debt from the primary markets) is increasing the government's flexibility beyond 2012, when Greece has to go back to the markets to refinance its debt. In an essence, the stability mechanism ensures that the EU will continue to support financially Greece, even if the country is not able to access the markets. Note that for 2011 the country's financial needs are covered by the EUR110bn bailout loan, while in 2012 Greece will need to raise EUR27bn from the markets. In addition, the mechanism will ensure a lower rate for the country when it seeks to reenter the markets. We also focus on the timing of the EU resolutions (before the regular EU summit on March 24-25) and the fact that Greece took almost all it was hoping to get from this EU summit, in our view, this also sends a strong message to the markets that Europe is determined to shield Greece from speculation and rumors as long as the government goes ahead with its program.

- Gives to Greece a breathing space for the implementation of its fiscal reforms and allow for debt sustainability. The extension of the repayment period and the lowering of the interest would give the government more leeway to its fiscal consolidation efforts and the ability to better balance its deficit reduction efforts with growth initiatives. According to the Ministry of Finance, Greece is estimated to benefit by these actions by cEUR6.0bn or c2.6% of GDP.

Greece will start repaying its EUR110bn loan in September of 2014 (instead of May 2013) until May of 2021 (instead May of 2015). All in all, refinancing needs of cEUR60bn are been pushed forward from 2013-16 to 2017-21. Just for 2014 Greece would had to refinance loans of EUR78bn but following the extension this number is reduced to EUR54bn.

- Forcing the government to plan and implement a very ambitious privatization / asset development program that worth EUR50bn. The implications of the implementation of this program for Greece are huge because of 1) the size of the reforms needed to create a framework that would induce investing 2) the economic growth push this program would entail and 3) the significant reduction of the country's debt obligations. We note that the intention of an up to EUR50bn asset development program had been announced by EU-IMF-ECB officials and the government last month but now Greece is committed to this number. Because the targeted amount is very big for the Greek economy and the time is limited, we would expect the government to proceed to quick and bold moves that portray its resolve and at the same time 'persuade' the market of its commitment to the goal.

All in all, the Greek government got almost all of what it wanted from the EU summit and this had not been discounted by the markets. Now has the ball to Greece's court to start taking actions.
The shock of the reforms and the asset development/privatizations program is expected to be very big for its highly protected and unproductive economy, while there are significant implementation risks.
On the other hand, there is no alternative for the country than to go ahead and implement its commitments and the EU is closely monitoring the country.
This could be the last and the biggest opportunity ever for the country to deal with its debt/deficit issues. It is possible that if Greece plays its cards correctly it could become a major 'restructuring' story for the years to come.

**The impact on the markets**

We would expect a rally on equities as the fear for a default or a 'haircut' on sovereign debt subsidies.

- Primarily the focus will be on the banking sector that holds substantial amounts of sovereign debt (especially the National bank of Greece that holds cEUR20bn in Greek government bonds but also EFG Eurobank, Alpha Bank and Piraeus Bank) and has suffered from increased speculation for a haircut.
- Attention on state control listed assets that Greece would have to eventually divest from in its drive to raise EUR50bn over the next few years. Government controlled listed assets include OTE, PPC, OPAP, Hellenic Postbank, ATEbank, Hellenic Petroleum, Piraeus Port Authority, Thessaloniki Port Authority, Athens Water Company and Thessalonica Water Company.
- Finally we would expect a positive reaction to the stock price of companies that are listed on the Athens Stock Exchange but substantial portion of their income stream (in some cases the majority) comes from abroad. Among the companies have been punished from the 'Greek risk' are Mytilineos, Metka, Folli Follie, Intralot, Frigoglass and Coca Cola Hellenic.

After the initial euphoria we believe that the markets will look for concrete signs that Greece is going ahead with its fiscal consolidation efforts and the implementation of the structural reforms. If Greece fails to show its determination then the market could react abruptly. On the other hand, if the government goes ahead with its commitments, the upside potential for Greek equities is substantial.

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