



Till Debt do us part...?

There are many thoughts that spring to mind when one thinks of Greece – Greek mythology, Olympics, the place where “Mamma Mia” was filmed – and now there’s an addition to that list, the Greek debt crisis. Greece is one of four European countries that are making headlines regarding large amounts of sovereign debt and are referred to in the bond market as PIGS – Portugal, Ireland, Greece and Spain. Last year, all of them broke the European Union’s budget rules that call for deficits not to exceed 3% of GDP. Portugal’s deficit equaled 9.3% of GDP, Ireland’s deficit was about 12%, Greece’s was just under 13%, and Spain’s deficit was 11.4% of its GDP in 2009.

They are not the only culprits however, as the aggregate budget deficit in the Eurozone is expected to climb to nearly 7% in 2010, from 2% in 2008. No country within the EU region is below the 3% limit. Greece is in a dire state and a default there could lead to a domino effect that could bring down other weak economies. Athens is under intense pressure by the European Union and financial markets to reduce its budget deficit by 4 percentage points to 8.7% of GDP this year. If the European Union forces these countries to slash their massive budget deficits, this will likely plunge their economies into deep recession. Years of government spending far exceeding tax revenues have driven the federal budget deficits in these countries. The European Commission highlighted in particular excessive employee compensation and capital spending as important factors behind Greece’s budgetary problems. To deal with the problem, Greece can either borrow money or reduce spending. The newly appointed (October 2009) Greek government has already unveiled an austerity program that involves a range of spending cuts and tax adjustments, including tax increases on fuel, tobacco and liquor, a freeze on public service salaries, and a 10% cut in salary allowances. These measures would also lead to a reduction in tax revenues as the economy shrinks, and this would further aggravate their financial situation.

The European Commission, which is the governing body of the European Union, is relatively powerless to help Greece. The EU treaty specifically prohibits providing a “bailout” to one of its members and the European Central Bank has no rescue power like the American central bank. Thus, such support must come from Greece’s fellow EU members. On February 11 2010, the leaders of the 27 EU member states promised to help Greece by taking “determined and co-ordinated action, if needed, to safeguard stability of the euro area as a whole.” Even though all 27 EU member states would be hurt by a Greek default, the 16 EU countries that have adopted the euro as their currency would be most affected. Among these, France and Germany have the most direct financial exposure to Greece. French banks hold almost US\$80 billion of Greek sovereign and financial institution debt and German banks hold about US\$43 billion of that debt.

Given the large amount of debt-crossover, it is unlikely that Greece will be allowed to default due to the financial ramifications for fellow EU states. Nevertheless, fears of default in the market tend to push up real interest rates, which, in turn, drag down economic growth. Sourcing finance for the PIGS is different when compared to the U.S. since adoption of the Euro currency excludes the option to devalue and print money. Monetary policy, and increasingly fiscal policy too, are dictated by Germany

and France, the core Euro nations. This leaves the bond market. Dealers have been selling off existing Greek bonds and pushing up the yields. The "spread" or difference, between Greek bond yields and bonds (German bonds) widened to nearly 400 basis points late January. When Greece recently made a new bond issue, it had to put a coupon rate above 6% as investors demand higher returns in exchange for the risk of default. Countries with large deficits that need to finance them by selling new bonds to financial markets may have to offer a higher coupon or interest rate to attract investors. This exacerbates the already large deficit by increasing debt levels. If recessionary pressures push the main Eurozone economies to reduce deficits, they could be at the mercy of rising taxes and spending cuts for years to come.

However, the problem is not just the current debt levels of these nations, because deficits in all the countries are rising as tax revenues are collapsing and governments' expenses are soaring. In the U.S, the federal deficit in 2009 was US\$1.5 trillion (10.7% of GDP) and it is forecast to stay around that level for many years. It took almost 200 years for U.S. Federal debt to reach US\$1 trillion in 1981. But in 2009, the debt increased by US\$1.9 trillion to US\$12.4 trillion.

As sovereign debt becomes less reliable and fears of default increases, the forex market may experience increased volatility. These include the dollar, euro, pound and yen. As a result gold could potentially continue to do what it has done for years and maintain its purchasing power and appreciate. Gold prices have been over US\$1,000 an ounce since October 2009 as there has been virtually no selling in the physical market. The IMF has said it would soon begin sales of 191.3 tonnes of gold to raise cash for lending programmes -- nearly four months after India purchased 200 tonnes of gold. The price of silver has also risen significantly over the past couple years and has proven to be another haven of value for investors. Gold increased 24% for the ninth year ending 2009 while silver futures were up 50%. Platinum prices have also been up as April futures are trading in the range of US\$1,504.00 - US\$1,531.80. At the moment, precious metals seem to be providing investors with the highest form of wealth protection. This begs the question, how 'superior' is sovereign debt?

Current Happenings in Local and International Markets:

- Canadian firm sells T&T gas asset
- UWI to begin Global competitiveness survey next month
- NEL outperforms JMMB, Sagicor
- Drop in first quarter profits for FirstCaribbean Group
- Government under fire over JDX effect on pension funds
- Scotiabank to focus on shareholder profit
- S&P moves Jamaica out of selective default
- Emerging Markets Lead stocks higher as Metals gain on expansion
- European Stocks climb as Mining shares, Saint-Gobain Advance

Table 1: Regional Market Performance (as at 25 February 2010)

Index	Closing Value	Weekly Change (%)	Monthly Change (%)	YTD Change (%)	1 Year Change (%)
TTSE Composite	801.42	1.01	4.76	4.46	-4.77
All Trinidad	1,172.49	1.46	5.54	6.28	1.85
JSE Index	79,141.59	-0.42	5.36	-5.00	-4.49
JSE Select	1,949.96	-0.16	14.31	2.74	-2.42
All Jamaica	71,296.05	0.12	11.22	0.47	5.32
BSE Composite	772.61	-0.79	-1.32	-1.74	-15.25

Table 2: International Market Performance (as at 25 February 2010)

Index	Closing Value	Weekly Change (%)	Monthly Change (%)	YTD Change (%)	1 Year Change (%)
S&P 500	1,102.94	-0.34	0.56	-2.65	44.19
Nasdaq Composite	2,234.22	-0.33	1.06	-3.21	56.74
Dow Jones Industrial	10,321.03	-0.69	1.22	-2.48	41.95
German Dax	5,532.33	-2.61	-1.76	-8.53	43.84
FTSE 100	5,278.22	-0.88	0.34	-4.04	37.13
Nikkei 225	10,101.96	-2.26	-3.91	-5.19	35.39
Hang Seng	20,399.57	-0.11	-0.97	-6.52	56.86
Eurostoxx	2,684.42	-3.38	-4.38	-11.05	36.59

DISCLAIMER

The information contained in this documentation is for your information only. All information contained in this documentation has been obtained from and is based on sources, including but not limited to, newspaper and magazine articles that CMMB believes to be accurate and reliable. However such information, facts, calculations, methodology, assumptions and estimates contained in this documentation have not been verified by us. All opinions and estimates constitute the Author's judgment as of the date of the documentation which are subject to change; however neither its accuracy and completeness nor the opinions based thereon are guaranteed. As such, no warranty, express or implied, as to the accuracy, timeliness or completeness of this documentation is given or made by CMMB in any form whatsoever. Consequently, CMMB assumes no liability for the accompanying information, which is being provided to you solely for general information.