Bankrate

‘Fiscal cliff’ vs. news on Greece

By Sheyna Steiner · Bankrate.com

Wednesday, November 28, 2012

On Tuesday, Greece finalized a deal with the International Monetary Fund and euro-area finance ministers that granted the next tranche of the Greek bailout loan and avoided the messy problem of another debt haircut, for now, pushing down the potential of a Greek exit from the eurozone.

"The bottom line with Greece is that this is an economy that remains very much in recession. By the end of the year, the Greek economy will have shrunk by 26 percent over the five years it has been in recession," says **Bernard Baumohl, chief global economist at the Economic Outlook Group.**

The indebted country got a pretty good deal in addition to the 43.7 billion euro loan installment. Most of the loan, 34.4 billion euros, will be paid in December. The remainder, 9.3 billion euros, will be disbursed through the first quarter of 2013.

One thing the deal did not include was debt forgiveness, which many experts believe may come in the future.

"There has been about 150 billion euros that have been actually lent out to Greece. While the European countries refuse to forgive any of that debt, the fact of the matter remains that I don't think that Greece will be able to pay back the 150 billion euro loans that have accumulated before the sun runs out of fuel. It's not going to happen. So Greece still has lots of trouble ahead. Europe will continue to lurch from crisis to crisis," **Baumohl** says.

But with the European Central Bank's recent plan to purchase sovereign bonds from countries that seek bailouts, known as the Securities Market Program, and the Greek deal that was reached this week, the worst seems to be past, at least for now.

"I don't think we will see any resolution for years. I see this as another temporary Band-Aid," says Scott Wren, senior equity strategist in Wells Fargo Advisors' Advisory Services Group.

But as far as the stock market goes, Band-Aids are an acceptable solution. "When you kick things down the road, the market gets back to the economy and earnings," Wren says.

According to the press release from the eurozone finance ministers, called the Eurogroup, in addition to the loan, the Greek deal also included:

- A lower interest rate on loans from the Greek loan facility.
- Lower fees on the European Financial Stability Facility, or EFSF, loans to Greece.
- EFSF loan maturities were extended by 15 years, and interest rate payments on EFSF loans were deferred by 10 years.
- The European Central Bank will give back to Greece any profits from the Securities Market Program, the ECB's bond-buying program aimed at lowering yields on Greek, and other floundering countries', debt.

All of that is conditional on Greece's implementation of budget plans that should reduce debt to 124 percent of gross domestic product by 2020 and lower than 110 percent by 2022.

Greece is also planning on buying back debt sometime soon. "The Eurogroup was informed that Greece is considering certain debt reduction measures in the near future, which may involve public debt tender purchases of the various categories of sovereign obligations," reported the Eurogroup press release on the meeting.

It's not all good news. Though the deal adds some clarity and stability to equity markets, according to John Stewart, managing director at Vantage Economics, it may be too complex to be sustainable.

"This would imply that further concessions will be needed down the road unless everyone is just kicking the can down that road and hoping that better economic growth will begin to ease the burden on its own a bit," he says.

'Fiscal cliff' hangs over Greek news

How does this news affect Americans? Though the news early Tuesday morning buoyed European stocks, The Wall Street Journal reported, American investors remained focused on the so-called fiscal cliff. Standard & Poor's 500 index fell 7.35 points, or 0.52 percent, the Dow Jones Industrial Average closed down 85.25 points, or 0.66 percent, and the Nasdaq fell 6.77 points, or 0.23 percent.

"Even though we have had interesting things go on in Greece recently, retail investors are thinking much more about the fiscal cliff," Wren says.

Baumohl agrees. "People are sort of holding back until they get some more clarity as to what will be the resolution to the fiscal cliff. I think that has been the biggest headwind facing the U.S. economy," he says.

If the country manages to skirt the budget and tax issues looming at the end of the year, **Baumohl** predicts that GDP could grow as fast as 3.5 percent in the coming year and knock the unemployment rate down significantly.

For his part, Wren believes the U.S. will avoid the tax and budget crisis. "I still think that the market is convinced that we are not going to roll over the fiscal cliff, but investors are certainly thinking about that now," he says.

Have you changed your investments as a result of the fiscal cliff? What do you think about Europe? ###