


## Greece: The new AIG?



The Greek crisis has sent global financial markets plunging for the past few weeks and sparked concerns of a wider sovereign debt slump. Greece's credit rating was cut last week to junk by S&P and Moody's Investors Service, which currently has an A3 rating on the country, said its decision will depend on the measures announced by the EU and the IMF. While signs of an accord ended between Greek officials and the EU/IMF, Moody's Investors Service warned that Greece could be vulnerable to a multi-notch downgrade if measures don't go far enough. Yields on Greek two-year bonds rose to the recent high of 26%, implying that Greece will probably default. At the same time, Greek 10-year bonds currently yield between 6.32% and 6.44%. Many investors wondered why these have any worth at all given the many alternatives offering a better return and greater liquidity. For example, AT&T, Inc. is currently paying

a 6.4% yield and Verizon Communications Inc. is offering 6.25% for the same horizon. These casts doubt that normal investors will buy Greek bonds and hold them for ten years. If interest rates rise in coming years, which is close to a certainty, then the value of Greek bond will diminish. According to European Union estimates, Greece's budget deficit may have exceeded 14% of GDP last year. Although Greek officials will reach an agreement with the EU and the IMF in coming days on budget cuts that may be worth 24 billion euros, Greece may still need a total 120 billion euros of support from the IMF and EU over three years should Greece try to close that gap. So, is there any panacea? Let us go through fact about a centuries-old rivalry, Turkey. In 2001, Turkey posted a budget deficit dwarfing Greece's 2009 record and failed to

collect enough taxes even to cover interest payments. Turkey's debt approached 80% of GDP in 2001. It stood at 46% last year, compared with 115% for Greece. In 2003, S&P's rated Greek debt 11 steps above Turkey; this week the gap shrank to one. Turkey's budget deficit measured by EU criteria was 24.5% in 2001. The government and IMF capped government salaries, raised taxes, curbed investment spending and sold assets. They cut the deficit to 0.6% by 2005 and posted a surplus of 1.2% in 2006 after selling about \$30 billion of state-owned companies. Turkey's economy has grown at an average pace of 4.4%. Turkey has a population of about 72 million and a \$660 billion economy, while for Greece the figures are 11 million and \$314 billion. As Turkey has made it, will Greece have the same story? 

## Microscope

Obviously, there are many obstacles for Greece to implement similar measures as those actions being taken by Turkey before. There were 65% of Greek voters polled by researcher Alco last week saying Prime Minister Papandreou must reject any measures that lead to more wage and pension cuts. Greece's membership of the euro deprives it of devaluing currency as adopted by Turkey in 2001, while the global economic weakness also makes it hard to match Turkey's rebound. Many also argue that IMF aid is sweetener toxic to Greece. In Hungary, the first EU member to turn to the IMF, its fiscal conditions attached to the \$27 billion loan exacerbated the country's recession as unemployment soared to a record. Turkey got about \$45 billion in IMF loans between 1999 and 2008. When Turkey sold euro-denominated bonds in 2003, they yielded almost 10%. Ten-year Turkish bonds in euros now yield 5.3%, compared with 9% for comparable Greek debt. Certainly, as Papandreou said last week, the country faced a new Odyssey. There is obviously no other choice out there. Right now, Germany pays 0.79% to borrow for two years, while Greece must pay over 12%. 

### MARKET BRIEFING

#### YTD % (local curr)


<b>US DJ</b>	11,008 (5.6%)
<b>Nasdaq</b>	2,461 (8.5%)
<b>Euro Stoxx 50</b>	2,816 (-5.0%)
<b>HSI</b>	21,108 (-3.5%)
<b>Japan NK225</b>	11,057 (4.8%)
<b>China Shanghai Composite</b>	2,870 (-12.4%)
<b>Singapore</b>	2,974 (2.7%)
<b>India BSE30</b>	17,558 (0.5%)
<b>Brazil BOVESPA</b>	67,529 (-1.5%)
<b>Aus All Ord</b>	4,833 (-1.0%)
<b>US-10yr Bond</b>	Yield 3.65%

As at 30/04/10

## Insight: "High Yield Bond"


High-yield bond, or junk bond, is a bond that is rated below investment grade at the time of purchase. These bonds have a higher risk of default or other adverse credit events, but typically pay higher yields than better quality bonds in order to make them attractive to investors. High-yield bonds can also be repackaged into collateralized debt obligations (CDO), thereby raising the credit rating of the senior tranches above the rating of the original debt. The senior tranches of high-yield CDOs can thus meet the minimum credit rating requirements of pension funds despite the original high-yield debt. As low

rates have fuelled investor appetites, even though fears over Greek bonds have disrupted debt markets, companies have sold risky debt in record volumes this year, totaling \$67.8bn at the end of

the Q1, an all-time high for the first three months of the year, according to Thomson Reuters. Junk bonds are trading within a half cent of face value for the first time since June 2007 in a sign that investors are convinced the economic recovery and profit growth will keep the neediest borrowers from defaulting. It is expected the transaction activity of high yield bond remains robust as many companies aim to pre-empt a so-called maturity cliff of largely leveraged buy-out related loans coming due from 2012 to 2014. Persistently low rates have driven yield hungry investors out of money market funds into high yield bonds. 

## Financial "In & Out"

**IN:** Gold price will break through recent trading range amid the concern over the money-printing activities are never ending due to the Greek debt crisis and a slow recovery in the US economy.

**OUT:** Euro may face long-term downward pressure with regard to aid package to PIIGS in coming years although there may be short-lived rebound. 



### IBC Group

Comprehensive Financial Planning  
Wealth Management Advisory  
International Business Advisory  
Call 2268 6308  
Email: insider@ibccapital.com

**Next Insight**  
"Commodity Price Analysis"