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Greece

WHAT'S NEXT AFTER ELECTION?

27 January 2015

MACRO | ECONOMY | Equity Market

Global Macro, Equities, Phillip Securities Research

OW = Overweight ; NW = Neutralweight ; UW = Underweight

Region	Country	Rating Present	Rating Prior	Unit Trust	ETF
G3	US	LT OW ST NW	LT OW ST NW	Fidelity - America Legg Mason - Clearbridge US Aggressive Growth Legg Mason - Royce US Small Cap Opportunity	SPDR S&P500 (SGX) - S27 Lyxor NASDAQ (SGX) - H1Q iShares Russell 2000 (NYSE Arca) - IWM
	Europe	NW	NW	Templeton - European Schroder - European Equity Alpha Schroder - ISF European Smaller Companies	DBX Tracker MSCI Europe - IH3 VGK Vanguard European Stock Index
	Japan	OW	OW	Aberdeen Japan Equity Fund Lion Global Japan Growth Fund Nikko AM Shenton Japan Fund	DB X-trackers MSCI Japan ETF – LF2 (SGX) iShares MSCI Japan – EWJ (NYSE/Amex) WisdomTree Japan Hedged Equity – DXJ
Asia ex-Japan	China/HK	OW	OW	Fidelity Greater China First State Regional China Schroder Greater China	db x-trackers MSCI China TRN Index 1C (LG9.SGX) db x-trackers CSI300 Index ETF 1D (KT4.SGX) ChinaAMC CSI 300 ETF (3188.HK/83188.HK) iShares FTSE A50 China (2823.HK) CSOP FTSE China A50 ETF (2822.HK/82822.HK)
	India	OW	OW	Aberdeen - India Opportunities SGD Fidelity - India Focus A SGD Lion Global - India Acc SGD	MSCI India (I98.SGX) DBX India (LG8.SGX)
	Indonesia	OW	OW	Aberdeen Indonesia Equity Fidelity Indonesia A USD	Lyxor Indonesia10US$x@ (P2Q.SGX) DBXT MSINDO 10US$x@ (KJ7.SGX) Ishares MSCI Indonesia ETF (EIDO.NYSEARCA) Market Vectors Indonesia Index ETF (IDX.NYSEARCA)
	Thailand	NW	NW	Fidelity Thailand Fund Aberdeen Thailand Equity Fund	Lyxor ThaiSET 10US$x@ (P2P.SGX) Ishares MSCI Thailand Capped ETF (THD.NYSEARCA) X DBMSCITHAI (3092.HK)
	Malaysia	NW	NW	Lion Global Malaysia Fund Aberdeen Malaysian Equity Fund	db x-trackers MSCI Malaysia TRN Index 1C (LG6.SGX) XIE Shares Malaysia (FTSE BM KLCI) ETF (3029.HK)
	Singapore	NW	NW	DWS Singapore Small/Mid Cap Fund Nikko AM Singapore Dividend Equity Amundi Singapore Dividend Growth Fund	SPDR STI ETF (ES3.SGX) Nikko AM STI ETF (G3B.SGX)

Source: PSR (as at 16 Dec 2014)

- On Sunday Jan. 25, the far-left, anti-austerity party Syriza won the Greek election, which was called after the country's parliament rejected Prime Minister Antonis Samaras's preferred presidential candidate in late December. The move came in after the country was given an additional two months to fulfill is bailout obligations by the European Central Bank (ECB).
- Alexis Tsipras, 40, Syriza's charismatic leader, sworn in as the country's youngest prime minister in 150 years.
- While Syriza's victory was more decisive than polls had predicted, the results of the vote left the party just short of a majority. Syriza took 36.3% of the vote with 149 seats in the 300-seat Parliament, compared with Samaras's New Democracy, which took 27.8% with 76 seats. The far-right Golden Dawn placed third with 6.3%, followed by To Potami with 6.1%.
- The radical leftist Syriza party formed a new coalition government on Monday with the right-wing fringe party, Independent Greeks, within hours of its election victory. The Independent Greeks party leader then expressed his support for Syriza in a vote of confidence in Parliament scheduled on Feb. 5. The alliance's anti-austerity policies threaten to derail Greece's bailout program or even offset the euro bloc's economy recovery stimulus.
- Nonetheless, Tsipras has recently softened his tone and has pledged to keep the nation within the single currency area as he negotiates a write-down of Greek debt and eases budget constraints that were imposed in return for aid after the country's economic collapse.

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MCI (P) 022/11/2014
Ref. No.: SG2015_0021

Greece Economy

- Greece has struggled under repeated rounds of austerity that have pushed unemployment up to 25% compared with the Eurozone average of 11.5%. The country has the highest unemployment rate in the Eurozone.
- Greek debt, at 175% of gross domestic product (GDP), remains at unsustainable levels.
- With unemployment painfully high and economic growth painfully low, calls for an end to austerity increased among the Greeks.

A game changing milestone

- Syriza's victory marks a turning point in the long euro zone crisis – a possible "Grexit", changing bailout rules and policies involving other Eurozone members, especially after last week's quantitative easing plan (QE) announcement by the ECB.
- Now, the new coalition government's mandate is to confront the European debt inspectors on the nation's austerity program imposed since May 2010.
- The coalition wants to renegotiate the terms of Greece's EUR 240bn bailout deal with the European Union (EU) and International Monetary Fund (IMF) five years ago to deliver its election pledges, which includes a writedown of Greek debt while persuading European creditors to keep aid flowing.
- The current round of funding expires on Feb. 28 and talks with the European Central Bank (ECB), IMF and European Commission, or collectively known as the "Troika", for its renewal have stalled since September amid demands for further belt tightening.

Two possible outcomes

(1) A continual standoff over debt restructuring until at least one of the parties make concessions for Greece to remain in the EU

- The Troika has made clear that, at least for now, they were unlikely to oblige to Tsipras on his demands, especially his pledge to seek a write-down of Greece's huge debt.
- However, Greece needs its next allocation of bailout money — a EUR 7bn payment — to keep the government running and pay off looming debts to avoid a potential default. And for Greece to be eligible to the additional lending, available in July, Greece would need to comply with the current austerity program.
- It has a choice between compromising with the Troika and a huge state bankruptcy that could lead Greece further into the abyss.
- As exiting the single currency bloc also has significant implications on the Eurozone *(please see Point 2 below)*, it has become a vehicle for Greece's political brinkmanship.
- Even if the European creditors are prepared to relax some of the terms of Greece's bailout, further debt relief was out of the question. Any debt relief will be met with fierce opposition from northern states, particularly Germany.
- As such, we do not expect any reduction of Greece's huge debt commitments, but we should be seeing the Troika working with Athens in the interest of all to enable further progress – helping Greece to have more growth, more jobs, and more investment. Therefore, the standoff may ultimately find both sides reaching a middle ground — one on which Greece could move toward an eventual economic and social recovery, with European officials partly relaxing their insistence on strict budgetary discipline.

(2) Greek exit from the euro, or "Grexit"

- Having said the above, even if the Troika made concessions, Greece could still opt to exit the euro.

Implication to the Greece economy:

- Greece would be pushed into a serious crisis — with money running out and neither the Troika nor the ECB in any position to help, and rapidly turn into a disastrous spiral that it defaults within the euro or even out of the euro.
- Defaulting on its sovereign debt could push up the cost of borrowing in its private sector and tipping its modest economic recovery into recession. This would further exacerbate the country's already troubling debt-to-GDP ratio, leading to a downgrade in its sovereign credit rating, and further slowing investment and the GDP.
- The new drachma would drop and the extent would depends on the considerable amount of debt that would have to be forgiven/restructured.
- A run on Greek banks as depositors would avert the risk of "haircut" by transferring euros in Greek banks to a more stable banks. The Greek central bank has already requested emergency liquidity assistance from the ECB in anticipation of the upcoming elections, however, provided some relief to the depositors.

Implication to the euro area:

- The ECB last week pledged to pump EUR 1.1trn into the region's economy to stave off deflation and ignite growth. With Syriza in the lead, the result will be important to determine whether Greece will be participating in the expanded asset purchase program.
- Nonetheless, with or without Greece, ECB's QE would remain as the dominating effect to the euro economy. Falling energy costs and anticipation of more European Central Bank stimulus helped lift optimism about an economic recovery.
- Should Greece default on their debt, the other euro members would have to face the aftermath – non-Greek taxpayers would be left to foot the bill. Eurozone governments are the biggest holders of Greek debt at the moment.
- But Greece is a small country and trouble there might be manageable. But it would send a wrong signal to the other countries to follow suit - euro economic recovery would stall, reforms and restructuring could never take their course, and affecting global economy.

Conclusion: Time to get insurance?

- It seems like we are set to have a very uncertain year ahead. Investors should take a step back to consider buying some insurance – whether in the form of options, futures or some other financial instrument – that is reasonably inexpensive to hedge these risks.
- Investors may also wish to consider gold, as the yellow metal should thrive on uncertainty in terms of a big rise in safe haven demand – as a reaction of the ECB money printing, Swiss peg exit and overall uncertainty. It is reasonable to expect that it might move tactically even higher in case of a Greek tragedy, but strategically it should be on its way to go back to fundamentals.
- Asia ex-Japan (AxJ) region should be rather insulated from the Greek contagion – relatively healthy local banking systems should provide a buffer as they did after the global financial crisis in 2007. However, the region (mostly are export-reliant economies) is still likely to be affected through trade linkages. As such, we maintain **OW on AxJ** as demand from US (stronger economy) would likely to pick up the slack from the eurozone somewhat. Breaking down, we **OW on China, India, Indonesia; NW on Malaysia, Thailand and Singapore**.

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