

Special Market Update: Weakness in Greece, Other European Countries Unlikely to Derail Global Recovery

- Global equity markets fell sharply this week, as concerns spread about Greece's fiscal struggles and the potential impact on other European economies.
 - AllianceBernstein owns no sovereign debt of Portugal, Ireland, Greece or Spain in any of our fixed income portfolios as of January 31, 2010
 - In our assessment, weakness in European countries won't derail the global economic recovery that's underway
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Fears of Greece's Fiscal Struggles Rattle Markets

Global equity markets tumbled this week, amid growing fears about the fiscal situation of Greece and potential contagion to other weaker European economies.

Yield spreads on government bonds in the peripheral euro countries (Portugal, Ireland, Greece and Spain) have risen sharply, but the widening of Greek spreads has been particularly pronounced, reflecting investors' concerns about the budget overshoot and the lack of a credible strategy to put public finances on a sustainable footing.

Markets have also been spooked by signs that the European Central Bank will soon start reducing the very generous amounts of liquidity that it has been providing to the euro area banking system.

No Exposure in Our Portfolios

We have steered clear of these countries' sovereign bonds for quite some time in favor of core countries (Germany, France, Belgium and the Netherlands), so widening spreads have been good for our relative performance.

We've been predicting a widening in spreads based on numerous fundamental factors. For example, Greece, Portugal, Spain and Ireland have the biggest current account deficits in the EU (11% of GDP in Greece's case) and Greece, Ireland and Spain have the biggest budget deficits. We think the spread widening trend may run further.

Our Assessment

- o We think valuations among the peripheral euro countries could continue to fall for some time, but at this point we don't believe this turbulence threatens to break up the euro area.
- o Even if things go wrong, we would expect other euro area countries to support Greece, emphasizing the overriding political dimension of the European project. That said, a bail-out and the resulting corrective action would likely involve a painful process.
- o It's worth remembering that most of the peripheral countries are pretty small in size. Greece accounted for 2.5% of total euro-area gross domestic product in 2008, with Portugal at 1.8% and Ireland at 2%. (France, Italy and Germany accounted for about 65% between them)
- o We believe the direct economic impact of weakness in European peripheral countries will be small, and should not derail the global economic recovery. Having said that, we believe heightened uncertainty will likely continue to weigh on market sentiment in the near term.

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