AQUILA

Flash

Only another bailout package can save Greece from a declaration of bankruptcy.

Greece has no money left and her borrowing requirement for this year is probably around 20bn euros. Given this context, handing over the remaining 7.2bn euros from Greece's second bailout package will not put off the day of reckoning. Only a third rescue package can save Greece from bankruptcy. In our opinion Brussels should not waste any more money on Greece and should cut the cords that bind that unhappy country to the Eurozone. Unfortunately, this is not the most likely course of events. More probable is some mixture of another aid program, a partial default by Greece on her liabilities and a move in the direction of Grexit. Far too much time has now been wasted for Greece's problems to be solved in an efficient and orderly manner. Market declines as a result of what happens to Greece should be viewed as a buying opportunity.

Greece's membership of the EU seems to have been cursed from the start.

The entry of Greece into the European Union has been problematic right from the start – when her acceptance as an EU member was a matter of dispute. Greece's admittance as a member of the Eurozone was only possible as a result of cosmetic financial transfers that made its government's balance sheet look better than it really was. The revelation of the true state of Greece's budgetary condition was enough to tip the Eurozone into its first big crisis in 2010. Greece also played a prominent role in the next two Eurozone crises, which occurred in 2011 and 2012. Since elections earlier this year, in which the leftist coalition Syriza emerged as the strongest party, Greece and the rest of the EU have been on a collision course.

Greece needs another 20bn euros this year to stay afloat.

Ostensibly the current fight is about the disbursement of the remaining 7.2bn. euros from Greece's second bailout package. So far this is being held back on account of the Greek government's refusal to implement reforms that were agreed as conditions for the package. It is impossible to see how and when Athens can meet her financial obligations. Scheduled interest and capital repayments to the IMF and to European institutions are set to total 12.9bn euros by the end of the year, with the lion's share falling in July and August. Barclays Capital estimates that Greece's requirement for external finance will amount to around 20bn euros. this year. Meanwhile, experts are unanimous that Athens' funds will be exhausted, if not by the end of April, then certainly by mid-May.

Only a third bailout package can save Athens from a declaration of bankruptcy.

It's therefore obvious that, even should Greece receive the entire financing involved in the second aid package, she would still need to borrow more. On our figures, and assuming the 7.2bn euros is handed over, an additional need for funding would kick in around July 20th. As Greece no longer has access to the international capital markets, only a third rescue program can save her from bankruptcy. Experts suggest such a package would need to be between 20 and 30 bn euros. But it is hard to see Brussels and Athens agreeing on the conditions for a fresh package when Greece is unable to comply with the terms of the current one.

If she were a commercial firm Greece would have been declared bankrupt long ago.

Even should Greece summon the will to accept the conditions of a fresh multilateral aid package, it's hard to view her as a suitable recipient of the funds involved. The second aid package was agreed under the assumption that Greece's public indebtedness as a percentage of her GDP would fall from 174% in 2013 to 120% by 2020. Nobody now views this projection as realistic. Even under the optimistic assumptions of continuous economic expansion and a primary budget surplus of 1.3% of GDP in each of the coming years, projections still show government indebtedness at 170% of GDP in 2020, although this ratio is forecast to fall thereafter - to 135% of GDP by the year 2030. Given the negative developments of recent quarters, Greece's current position is extremely precarious and the country looks set to be dependent on external transfers for decades to come. Credit default swap rates in the market indicate an 80% chance that Greece will default on her debts. Any commercial enterprise with such balance sheet trends would have been declared bankrupt long ago.

Brussels should cut itself loose from the EU's weakest member.

It is a mystery why a third aid package to Greece might be thought likely to have a positive effect after 240bn euros have already been wasted this way with the first two bailouts. We think that Brussels should avoid throwing good money after bad. It would be far better if Greece were recognized as the bankrupt that she is. Her financial position can only be improved materially if creditors are forced to take a massive haircut on their positions. Although this would not automatically mean the expulsion of Greece from the Eurozone and the EU, we think that Brussels should use the opportunity to cast Greece adrift.

But more likely is a mixture involving aspects of more aid, default and Grexit.

A clean break, however, seems improbable. For one thing, a bankruptcy declaration need not lead to Grexit. One could also imagine a scenario whereby Greece fulfils its international debt liabilities for a certain period but resorts to fresh debt instruments, involving some sort of parallel currency, in dealing with domestic financial obligations. Moreover, the Greek government could hold a referendum to obtain the people's backing in agreeing to the conditions that would be imposed for a third bailout package. But given that so much time has already been wasted, it is difficult to see the Greek situation being resolved in an efficient and orderly manner. Investors should not be surprised if markets are thrown into a fresh crisis.

Trouble in the markets on account of Greece should be viewed as a buying opportunity.

Greece is an economic bantamweight and her public debt instruments are only held to a small extent by the private sector. The danger that an EU or Eurozone exit by Greece would seriously disrupt the broader EU has now been substantially limited by the setting up of new institutions such as the European Stability Mechanism and the European Banking Union. Because of this we think any crisis in the markets stemming from Greek developments is likely to be short-lived. Market declines in this context should be viewed as buying opportunities.

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