



KayneCast

A Podcast Series by Kayne Anderson Rudnick



Episode 21

CIO Commentary on the Greek Debt Crisis

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Len: Welcome to KayneCast. My name's Len Hirsh, and I'm the Assistant Director of Marketing Communications for Kayne Anderson Rudnick. Today our guest is Doug Foreman, our Chief Investment Officer here at Kayne Anderson Rudnick. Doug is joining us to share his thoughts on the most recent developments related to the ongoing debt crisis in Greece. Hey Doug, thanks for joining us.

Doug: My pleasure, Len. Thanks for having me today.

Len: So, Doug, the worsening debt crisis in Greece has been pretty top-of-mind for many investors over the last several weeks, but I think most of us have expected all along that some sort of last-minute deal would be worked out. Can you explain first what happened to make things seemingly fall apart here in the final hour?

Doug: Sure, Len. There was a breakdown in negotiations over the weekend between the Greek government and its creditors. Greece decided to shut down its banking system down yesterday, Monday, June 29th, and the country's central bank quickly enacted measures to control large waves of money from leaving the country. It's become clear that Greece will fail to make its €1.50 billion debt repayment to the International Monetary Fund which is due today, Tuesday, and the country will be cut off from any further international rescue loans for the first time in over five years.

Len: Okay, and what about the referendum that's coming this Sunday?

Doug: It will be interesting to see, Len, and I think the decision to put this to a vote is what shocked people the most, including the creditors. Political maneuvering has now boxed the nation into a critical decision this weekend on whether to agree to creditors' terms or say no and risk getting tossed from the 19-nation Eurozone. In the meantime, Greece's request for a one-month extension on its bailout has been rejected. Today, there are rumors of a last ditch effort to come up with an agreement, but we'll see. It's a very fluid situation.

Len: Okay, so what are your thoughts on the market's reaction to these developments, at least yesterday and so far today?

Doug: Well, we saw stocks in Asia, Europe, and the U.S. decline significantly on Monday in response to this uncertainty. However, it's important to note that these market movements—although big on dollar amount like the Dow [being] down 350—are relatively modest in relation to the heavy selloffs that we saw back in the 2008 and 2009 period when there was a lot of systematic financial risk going on in the world.

Len: Is that just a product of a healthier global economy this time around, Doug?

Doug: I think that's a big part of it, but I think even more importantly, the ECB (European Central Bank) is in a much more proactive



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stance this time supporting the market than they were in 2011. And European banks are in a much better position because they have reduced a lot of Greek debt on their books. So the debt issue and the Europeans banks' exposure to debt—Greek debt in particular—is much lower than it used to be. And in 2011, policymakers, including the ECB, were very late in reacting to these systematic financial risks which were materializing in the Eurozone.

Len: So, do you think investors were simply trying to shield their year-to-date gains yesterday while protecting themselves on the off chance that this becomes a more dramatic sell-off?

Doug: That's possible, Len. Honestly I don't expect this to become a more dramatic sell-off at all, at least based on anything happening in Greece. Rather I think the turmoil will be limited to Greece, and Greece alone. Potential contagion outside of Greece for the global economy, or even the rest of Europe, is a minimal factor I believe at this point in time. In fact, if you look at even the price action yesterday, and you look at the sovereign credit yields for countries in the region aside from Greece—such as France, Germany, Denmark, Switzerland, Sweden, and others—you can see that sovereign bond yields actually fell yesterday, and the euro itself actually went up slightly yesterday which is very unusual. In 2011, if there was more systematic risk, what you saw was sovereign bonds yield went through the roof. They went up dramatically across the board in every country in Europe, and the euro actually went down a lot. And we're not seeing that yet at all. So the systematic risks seem to be somewhat contained to Greece.

Len: Okay, well that's reassuring. What do you think we can expect moving forward? It should be an interesting week.

Doug: Well, yea, this will be an interesting week, and I think it's going to continue to be a fluid situation with ebbs and flows. We're seeing some of that today with the rumors of this last minute deal. So I'm expecting a pretty volatile week all the way through the vote on Sunday. We'll see how the vote turns out, but whatever happens here we believe long term that these developments in Greece are not going to change the outlook for most U.S. companies. Most of our holdings have little to no exposure to Greece in any way, shape, or form. So we think that stocks are going to hold up much better than they did a few years ago when these debt problems in Greece morphed into worries about the financial stability of the euro itself and bigger economies such as Portugal, Spain, and Italy. So, remember if no contagion occurs anywhere outside of Greece, the worst case for investors is a meltdown in an economy the size of Missouri. So this is not that meaningful in terms of global GDP. Even if the worst case materializes here—they leave the Euro, the Drachma gets adopted, and Greece goes into a major depression—it's a tiny economy. Unless it spreads, it's really not an issue for investors over any reasonable time period.

Len: Alright, well, thank you for your insight and your time, Doug, and thanks again to everyone who listened in. We hope you are enjoying the series, and again, we always encourage you to get the most up-to-date episodes by either downloading a podcast app on your mobile device and subscribing to the KayneCast feed via iTunes, or just by listening to the KayneCast player on our website, which is at kayne.com.

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