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Greece's road seen as rocky no matter what

By Jeff Buckstein

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With Greece having already defaulted on a $1.7 billion U.S. payment on an International Monetary Fund (IMF) loan, representing the largest sovereign debt default in world economic history, the future of the eurozone stands at a potentially dangerous juncture. Greeks are poised to vote in a referendum Sunday about whether to accept new austerity measures in return for further financial assistance.

A bigger question is what might happen should Greece ultimately leave the eurozone it has been a part of since 2001, either of its own accord or as a result of having been expelled by the 18 other member countries.

There would be a significant political and psychological impact because this would be the first time that a country has exited the eurozone because of financial difficulties. But the financial impact has to be taken in context, said Vern Krishna, counsel with TaxChambers LLP in Toronto.

"There already is short-term disruption in the form of capital controls and banking controls and so on. But looking out a little further, this should not have a terrible impact on the rest of the eurozone," said Krishna.

"The fallout must be considered in light of the size of the economy. Greece has an economy that is about the size of British Columbia. So although there will be some adverse fallout, it's not going to be nearly as catastrophic as one might imagine — in the long run, anyway," he added.

John Curtis, a senior fellow at the International Centre for Trade and Sustainable Development in Geneva, and a former chief economist for the federal government's Department of Foreign Affairs and International Trade, said the underlying financial issues signal tough times ahead for Greece, no matter what.

"It's a lose-lose for Greeks whether or not they stay in the euro currency zone. Either the tough austerity measures by the European Union and the IMF are accepted in due course, or a rapid devaluation will take place fairly quickly which will lead to much reduced standards of living for most Greeks.

"One way or the other, Greeks will have to pay higher taxes, enjoy lower social standards, and have reduced pensions later than before," he added.

Receiving more monetary aid from sources such as the European Central Bank and the IMF would only represent a temporary measure for Greece. Any long-term solution will require fiscal discipline. Greece will need to bring its expenditures, which are financed by debt and not sustained by growth in the economy, under control, Krishna stressed.

"At the end of the day, a creditor is not going to simply keep throwing good money after bad to sustain a drowning debtor, which is what Greece is. Greece has been terribly irresponsible in the management of its financial affairs, inefficient in its financial and tax collections, and has simply given away much more than it can afford by way of social programs and pension benefits.

"It is a financial basket case," said Krishna.

Greece has long-term problems, agreed Torben Drewes, a professor of economics at Trent University in Peterborough, Ont.

"They really do have to restructure productivity. They have to get some of their young people employed — and not export that talent or leave it idle. So I don't see how Greece is going to manage through this, either way. To stay within the euro, they're going to have to accept the bailouts. And they're going to have to borrow money they'll never be able to repay," said Drewes.

"The best thing in the long run for them is to have some debt simply wiped off the books. Just forgive the loans. Not all of it. You can't create a situation of moral hazard. You can't let Greece do in the future what's been done in the past, which is to take advantage of cheap loans and cheap money. You have to suffer some consequences," he added.

The issue of contagion is also of major concern. If Greece were to leave the eurozone, what will be the potential impact on other eurozone countries with high debt-to-GDP ratios, most notably Italy, the third largest country in the union?

Italy has improved its financial position quite considerably in recent years, said Krishna, who also noted that there are other situations where euro countries managed to get through very difficult financial circumstances. For example, Ireland had severe difficulties in the aftermath of the 2008 financial crisis, and is now off the life support systems of the international agencies, with their economy picking up and moving in the right direction, he said.

Curtis predicted that Greece's financial crisis will have little impact on most banks and other financial institutions around the world. They have taken their assets out of Greece since the last crisis in 2012, and most international players have isolated themselves from potential collateral damage over the past two years, he noted.

"There will be some further uncertainties in global currencies, stocks, and bonds which will not last all that long. Trade finance will not be influenced negatively, as it was following the financial crisis of 2008-09. So there will be limited after-shocks with respect to international trade," Curtis added.

Whether or not there may be new investment opportunities should Greece get on the path to mending is a very difficult question to answer, said Krishna. These types of situations always present risks and opportunities. But this is best left to the professionals to assess; now is not a time for amateur or retail investors to be speculating in the market, he added.

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