Economic Analysis

Greek Uncertainty and Risks to the U.S.

Kim Chase / Boyd Nash-Stacey / Nathaniel Karp

- **Short-term financial volatility is expected but will fade as things shake out for Greece**
- **U.S. trade, investment, and banking exposure to Greece remains very low**
- **Fed unlikely to delay first rate hike over Greek concerns**

Tensions are rising in the Eurozone, with Greece on the verge of complete collapse and the rest of the world wondering how to pick up the pieces. The deadline has come and gone for the small Mediterranean nation to make its €1.6 billion debt payment to the IMF, and now it's time to sit and wait for the results of the referendum on July 5th. Prime Minister Alexis Tsipras called a referendum on whether or not to accept the conditions of the troika (ECB, EU & IMF) in exchange for additional bailout funds. The Greeks are in a conflicting position as they try to balance softening the costs associated to the austerity measures with the goal of remaining in the Eurozone.

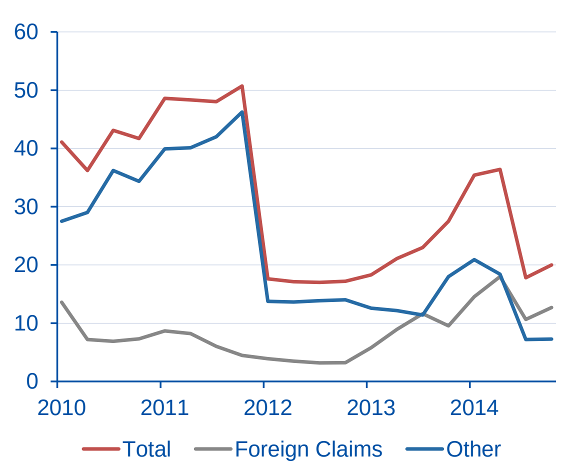
Meanwhile, Greek banks are closed until further notice, and ATM withdrawals have been limited to €60 per day per person. On June 29th, Tsipras urged his citizens to vote "no" on the referendum, stating that "we ask you to reject it with all the might of your soul, with the greatest margin possible. The greater the participation and the rejection of this deal, the greater the possibility will be to restart the negotiations to set a course of logic and sustainability." On July 1st, the Prime Minister announced that they would accept the creditor conditions (with some minor adjustments), but German Chancellor Angela Merkel has made it very clear that she is unwilling to negotiate further until after the referendum.

There are obviously some serious consequences for Greece and the rest of the Eurozone, but how does this impact the U.S.?

Chart 1
U.S. Direct Investment in Greece ($Mn)

Source: BEA & BBVA Research

Chart 2
Total Exposure of U.S. Banks to Greece ($Bn eop)



Source: BIS & BBVA Research

Potential impacts for the U.S. could stem from channels such as trade, direct investment, and banking exposure. Fortunately, the U.S. has taken significant steps over the past few years to decrease ties to the failing country. When it comes to trade, U.S. exports to Greece make up only 0.05% of total exports, and imports only 0.06% of total, so a failure in Greece shouldn't have much of an impact on the U.S. trade balance with the nation. U.S. direct investment in Greece peaked in 2007 (mostly in wholesale trade and manufacturing) and declined rapidly thereafter, never fully recovering after the global financial crisis. Before turning negative in 2013 and 2014, direct investment in Greece had dropped to a mere 0.04% of all direct investment in Europe (and only 0.02% of total in all countries). Other financial transactions with Greece are extremely low and will have little impact on the U.S. portfolio in the case of a Greek failure. Although the Greek banks are on holiday and in the midst of a collapse, U.S. banks have little to worry about. Total exposure of U.S. banks to Greece is very low, approximately $20B at the end of 2014 compared to a high of $50.7B in the fourth quarter of 2011. This accounted for only 0.4% of total U.S. banks' foreign exposure in 4Q14. Approximately $12.7B is tied up in foreign claims (mostly banks), with another $7.3B in other exposures (i.e. derivatives contracts, guarantees extended, credit commitments).

Regarding financial markets, we are sure to see some short-term volatility. This could intensify if the uncertainty regarding Greece spills over into other markets. However, this is unlikely to derail markets as participants have had time to prepare while the majority of Greek debt exposure is outside the private sector. Moreover, the economic conditions in the Eurozone have improved while local and central authorities have a better institutional framework to withstand financial instability; in particular, ECB's QE program.

Given the U.S.'s low exposure to Greece, we don't expect the economy to diverge from its current trend. This implies that we still expect GDP growth above 2% in 2015 and the Fed will start hiking rates in September. However, the FOMC could react by slowing the pace of tightening if conditions deteriorate significantly before the end of the year.