

Greece. Yes No. What Then? Tsipras and Merkel At Last Agree.

I was undecided before but the rhetoric from Berlin has now convinced me that for once, Merkel and Tsipras agree. They both want the Greek people to vote No in the July 5 referendum on creditors' terms.

Greece has been on explicit financial aid since the first bailout in 2010. In 2015, since Syriza won the general elections, all Greece has been trying to do is renegotiate the terms of its aid. It is not a bailout or a refinancing or debt reorganization, its aid. For the Eurozone, its members already struggling fiscally, with the exception of Germany, aid to an unproductive member was never sustainable. That the Greeks did not have a commercially acceptable business plan exacerbated the situation. Reprieve (for the EZ) came in the form of Syriza. Under ND, austerity had failed but its effects would only manifest will past the elections. Had Greece failed under a compliant New Democracy the effectiveness of the Eurozone's austerity programs would have come into question. Rather fortuitously, ND lost to a strident Syriza intent on tearing up the status quo became a convenient pawn in a gambit designed to see Greece out of the Euro, by its own hand, and facing painful consequences – as a warning to Portugal, Spain and Italy, that exit has a price too high.

Unfortunately, for the Eurozone and Syriza, the vote will likely be Yes. Quite what happens after such a vote is another matter but, polls notwithstanding, the human tendency is to go with the devil you know. A Yes is more probable because, Greeks do want to stay in the Euro, they receive aid from the Eurozone, their borrowing costs are or were held down by the Euro, but most of all, they cannot envisage life without the Euro, or life with a Drachma. More immediately, the banks are closed and

pension disbursements are drying up. Greece and her banks are short of cash. In the short term only Emergency Liquidity Assistance can restore the flow of cash and the ECB will certainly not raise the ceiling on ELA if there is a No vote. By imposing capital controls and a bank holiday, Tsipras may be encouraging his people to vote Yes just to free up the flow of money.

A Yes vote will mean a loss of mandate for Tsipras and his Syriza since he has recommended to his people to vote No. Tsipras may have to resign, triggering fresh elections. If so, a new government will need to be formed during which time it is not clear what the position of the Eurozone will be, they will have no one to negotiate with. The position of the ECB will be similarly unclear. Should they provide relief and lift the ceiling on the ELA? If they did, cash would start flowing again while Greek default risk would still be ring-fenced within the Greek financial system. So it is likely they would. Tsipras may not resign. A cynic might expect him to hold on to his position and resume negotiations with the creditors. He has already shown sufficient flexibility in between the time he called for the referendum and when the referendum would be held by attempting to negotiate terms with a softer stance. In any case, a Tsipras government or another government would have to respect the result of the referendum in negotiations with the creditors, basically accepting the terms of the initial creditor plan. The latitude for any government to be obstructive is significantly limited by a Yes vote. Very likely a deal will be struck and bailout disbursements would follow. Given the draconian terms of the creditor plan, Greece would limp along until the next crisis.

A No vote would keep Syriza in place but could well put Greece out of place. While it appears that anything is possible, if we are to believe the myriad official voices from Brussels to Berlin to Athens, Greece would probably be forced out of the Euro. Theoretically it could default and remain within the union, since membership does not explicitly preclude default, but the going concern status of Greece would be in question and there might be sanctions regarding Greece's access to the European TARGET2 payments system. Another possibility might be Greece

being removed from the currency union but not the European union in a similar way that the United Kingdom is part of the EU but has its own currency. In any case, Greece has for all intents and purposes already defaulted on the IMF loan due June 30. The IMF would simply formalize this by changing its status from being in arrears to being in default.

Under a No vote and default, could Greece remain in the Euro? Theoretically it could. Greek debt in Euro would default and face writedowns in the usual fashion that defaulted dollar debt faces writedowns. A plan of reorganization could still be formulated with Greece within the Euro that would restructure its debt. Creditors would still impose conditions, and Greece would negotiate for leniency, in fact the negotiations might look very much like what we have experienced in the past 5 months. The negotiations thus far have not only been ineffective, they have been irrelevant. Now it may be that the Eurozone then decides to remove Greece from the currency union. It may keep Greece in the broader union, or it may also eject it altogether. That is a separate analysis which would involve longer term strategic considerations as well as historical, cultural and emotional factors. The logistics of default are another matter. Upon default, Greece would have to be prevented from creating further liabilities, which it can do within TARGET2. Shutting Greece out of TARGET2 or limiting its access to it would be the equivalent of Europe unilaterally and exogenously imposing capital controls on Greece, which surely would encourage Greece to leave the Euro.

What other alternatives does Greece have? Tsipras has evidently approached Russia. Russia, however, is not entirely in shape for such extravagance. While the Russian economy has stabilized somewhat rates remain elevated and the currency may yet begin to weaken again and the budget has already begun to deteriorate again. Putin might be happy to spend some money on entertainment and Greece would be a source of worry in NATO's backyard but so far Tsipras' overtures don't seem to have borne fruit. Unless they are waiting for a more opportune time to come out.

The polls have been all over the place beginning with favor for a Yes, to

a more even balance to favoring a No. Polls tell you what people wish they could do, not what they will do. And even when the votes are counted, a new uncertainty will have begun.