Why the Greek Crisis Probably Won't Hurt the U.S.

Presented by Beata Dragovics

The Greek government's decision to pull out of debt-relief negotiations with the rest of Europe was a shock. Essentially, the Greek government has doubled down on confrontation with its creditors—and very possibly eliminated the possibility of any agreement at all.

Beyond the headlines, though, the reality is that the damage from this crisis is likely to be small. Remember:

- Greece makes up a very small part of the European economy and an even smaller part of the global economy.
- Everyone has seen this coming for a long time.
- Markets are reacting, to be sure, but in a measured way. No one is panicking.
- The fundamentals remain strong and are actually improving.

Greece is a problem, but it is primarily a problem for the Greeks and, to a smaller extent, for the Europeans. For the U.S., although we should pay attention, there is no reason for panic at this point. We've seen this movie before, in 2011. Everyone—Europe, the U.S., and their banking systems—is much stronger and better prepared this time. So, I think this too shall pass.

What are the ramifications for Greece's withdrawal from negotiations?

This crisis has resulted because Greece borrowed too much money. It simply can't pay back the funds and is now relying on external creditors to keep its financial system, including its banks, open. The Greek withdrawal from negotiations means that the existing financial support will expire shortly, and payments—which, again, the Greeks cannot make—will start coming due.

In the very short term (i.e., this week), the European Central Bank (ECB) has stopped providing additional support to the Greek banking system. This has forced the closure of that banking system and put a limit on the amount that can be taken from ATMs to prevent excessive withdrawals. The country's stock market has also shut down. This will hold until the referendum on Sunday, July 5, when the Greek people will be asked to decide whether to agree to continued cuts in spending in exchange for continued financial support.

If the people vote "no," then this week is the first stage of what could be a very nasty exit (or "Grexit") from the eurozone and the European Union (EU). No one knows exactly what will happen because it has never happened before. It was never supposed to happen. This uncertainty is fueling the fear that investors are feeling right now. Although a deal remains possible, it is increasingly unlikely, and governments and markets are preparing for a Greek default and exit.

Why there's little need to worry

What the markets are telling us, though, is that a Grexit may be much less damaging than expected. What is most surprising is how little reaction there has been so far. Yes, European markets are down—but not excessively so. You hear resignation and disbelief, rather than panic. There even seems to be a sense of relief that a resolution to this multiyear issue may finally be at hand.

This lack of reaction makes sense. Expected events may be tragic, but they aren't shocking. The Greek default has long been foreshadowed, and a great deal of work has been done to protect against just this event—much as we saw with Y2K more than a decade ago. Economies and financial systems around the world are much more solid than they were in the last crisis. Arguably, the eurozone and EU would even be better off, economically at least, without Greece. Eliminate the constant drama and uncertainty and countries could focus more on moving forward and less on resolving past problems.

The lack of reaction makes sense when you look at the fundamentals as well. Apart from Greece, European economic growth is accelerating, according to Bloomberg economics. The U.S. economy is also in the best condition it has been in since the financial crisis. With both the U.S. and Europe growing more quickly, the likelihood that a Greek default would rock the world is much less than it was five years ago.

The world financial system is also well prepared for a Grexit. Most Greek debt is now in public hands, not private, meaning a Lehman-like wave of contagion in the private sector is unlikely. The ECB has already started a quantitative easing program to support the European economy, and it could easily take additional steps to counter any problems stemming from a Greek default. Fundamentally, from both an economic and financial perspective, there is no obvious reason to panic.

Finally, as mentioned earlier, this all happened before back in 2011. Then, panic ensued because no one was prepared. Now, we are. Then, economies were still shrinking. Now, they are growing. Then, banking systems were weak and exposed. Now, they are much stronger and less exposed.

In short, any Greek default—which looks probable, although not certain—would cause damage, but that damage would most likely be limited and nothing to worry about, even in Europe itself. Here in the U.S., we are even more insulated and thus less vulnerable. Although risks remain, any damage here in the U.S. should be both limited and short lived.

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