# *Greece and China*

These two countries have been in the news frequently over the past three months. Their problems have caused significant short term declines in the global stock markets. Let's examine each a little more closely to see if the concerns will have a longer term impact.

**Greece and the euro**

The euro is the sole currency of 19 member countries. Each has its own duly elected government, system of taxation, and fiscal responsibility. Never before has a currency been shared by such a large number of countries that were governed independently. The current situation in Greece is the first crisis to truly test the experiment that is the euro.

Greece has been poorly run for years with some corruption as well as the country generally spending much more than it receives in tax revenues. The other stronger member states, primarily Germany and France, have loaned funds to Greece to keep the country solvent. The newly elected government of Greece has been concerned that the austerity measures required by the European powers to loan Greece additional funds are too severe. Greece has a mountain of debt and needs funds from the European Central Bank (ECB) in order to continue to service its debt.

The Greek people voted on July 5 to reject a recent ECB proposal. The negotiations have continued and they appear to have reached a final agreement. While Greece stays in for the short term, it may ultimately be asked to leave the ECB and the euro. That could precipitate a return to its original currency, the drachma.

Whether or not Greece stays in the eurozone has little impact on the world economy.

The gross domestic product (GDP) of Greece represents only 0.38% of the world economy. While this drama may cause short term blips in the stock markets, in the long term it is likely to have little effect. Greece is simply too small to rock the global economic boat.

## **China**

China is another matter. China's GDP represents 16.7% of the world economy and has been a primary growth engine for the past ten plus years. While the growth rate of the Chinese economy is slowing, it is still advancing at or around 7% per year, if we can believe the statistics recently released by the government.

Stock markets in mainland China have soared by over 150% in the 18 months through mid June. This rise was funded in part by individual investors, many of whom were borrowing money to buy on margin. The result was a median PE valuation of 85x earnings. Over the past month, the market began to plummet and was recently down 30% from its highs. The Chinese government, along with the top 21 brokerage firms, have raised funds to purchase securities in an attempt to prop up the stock market. We're afraid such an attempt will likely have little impact.

If economic growth slows significantly or China falls into a recession, that will have a significant impact on global growth and world markets.

## **Media Coverage**

While the news media is much more interested in the Greek crisis, the global economy will be far more influenced by the outcome of the economy in China. We'll be following China closely and suggest you keep an ear to the ground as well.