European Sovereign Crisis Postponed: Hurrah!

A financial crisis in the Eurozone has been postponed due to the efforts of a gaggle of politicians overcoming the urge to assault one another and instead come up with an incredible plan to stave of immediate default by Greece and potential default by peripheral Europe.

Unfortunately the plan misses the most important point. To understand this, we need to understand the Chapter 11 process in US bankruptcy. Basically, the basis of a debt restructuring in the case of an indebted and distressed enterprise is whether the business is viable in the first place. Only then is a new capital structure proposed. The analogous question therefore is, is Greece a viable economy in current form and if not, what needs to be done to make it a viable economy. We are not talking about Greek debt yet, only if it is a going concern. The answer to the question is, no, Greece is not a viable economy in current form and what needs to be done is to have a viable tax collection mechanism as well as structural reform in the form of a 30 – 40% deflation in Euro, or less painfully, a Drachma that can be immediately marked to achieve such a deflation. This is to make Greece competitive. Any debt restructuring without such 'structural reform' is merely refinancing a non-viable economy.

So it is a good thing that markets are rising once again. We need higher valuations to begin shorting. Again.

What should we be buying or selling? As markets rise, it makes sense to start shorting cyclicals again. The natural candidates will be expensive Emerging Market listings of businesses exposed to Europe and the US. The usual suspects are the exporters. The natural candidates to be buying remain in the resilient luxury sector as well as in the export sectors exposed to Emerging Market economies but listed in depressed developed markets such as Europe. Its an old story that will one day reverse but for now the game of chicken carries on.