Greek Week

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A banker friend vacationing in Greece this week reports asking a fifty-something customer in an Athens coffee shop what he did for a living. The man responds he's been unemployed for the last four years. "The Greeks invented everything," he said, "and now I'm taking a rest."

Certainly seems like *déjà EU* all over again: Greece on the precipice of default, on and off negotiations with the European Union, and both sides playing a governmental game of chicken. Meanwhile, global capital and currency markets seesaw in response, and the world waits to see where it all shakes out.

Even Puerto Rico's governor got into the act, jumping onto the bailout bandwagon and declaring Monday its $72 billion debt was "unpayable." Compared to Greece's $390 billion, the obligations of the 51st state seem a drop in the bucket. (The state and local debt of Massachusetts is $90 billion.) But the news added to general unease.

Back in the US, investors pondered whether these latest kerfuffles would derail the Fed's plan to raise interest rates later this year. Economists had predicted September as the most likely month for a hike, but some now say that may be pushed out.

A lot depends on what happens this week. If history is any indicator, we should expect the usual brinksmanship leading to can-kicking and half-measures from the EU. In the unlikely event of a "No" vote on the Greek referendum, things could get more interesting.

At the Buyouts conference in Chicago last week, much of the chatter (besides the usual complaints about high valuations) surrounding the deleterious effects of the zero-rate environment. The frantic search for yield creating too much cash chasing too few deals could only be stopped, many said, by a good old-fashioned correction.

How and when would that start? One long-time observer told us, "We're in the 7th inning of this recovery, so we're due for a correction. Any exogenous event could trigger one." Know of any?

Of course, the distressed crowd has been on the look-out for shoe-dropping since 2010. The prospect of market spreads blowing out warms the cockles of some managers' hearts, even if it takes a sovereign default to get us there.

A Grexit might create temporary dislocation, tampering down secondary loan prices in the broadly syndicated market. Some volatility would be welcomed by loan buyers. But the impact of past headline events has proven transitory on this seller's market. Not that we wish for a cataclysmic end to the current crisis. Just a *soupçon* of stress.

Meanwhile loan and bond investors are watching for signs of rising rates. As the Fed signaled a move, junk funds hemorrhaged $6.6 billion over the past three weeks. Loan buyers vote with their feet, depending on rate expectations (*Chart of the Week*), but market jitters and mixed monetary messages sent $800 million out the door in June.

The good news for middle market loan players is that smaller issues will be more insulated from market choppiness. And if large cap spreads widen, we expect midcaps to follow. Whether Greece stays or goes.