



The Greek Debt Crisis & Your Griffin Black Portfolio

The recent sell-off in worldwide equity markets occasioned by the Greek debt crisis has no doubt been of concern to many of you. Here are some things that you might want to know and consider.

First, the recent developments in Greece have had no immediate impact on Griffin Black's tactical portfolio allocations. The fact is that this sovereign debt crisis reflects many of the risks and uncertainties we have been discussing since the global financial crisis began to unfold in the second half of 2008. Our ongoing assessment of those risks caused us to adopt a relatively defensive (underweight) position in equities (and equity risk) in our balanced portfolios some time ago.

The Problem with Debt

The root of the systemic, global risk that has found a current flash point in Greece is an excessive build-up of debt (both by governments and households), compounded by unsustainable current and projected future levels of spending relative to revenues. We have written about the likely consequences of this situation in the US as (1)

sub-par economic recovery and earnings growth, (2) higher interest rates (bad for growth as well as for stock market P/E multiples), (3) the return of inflation down the road, and (4) a depreciating US dollar relative to emerging markets currencies, which are generally in much better fiscal shape than the US/Europe/UK/Japan. Greece's fiscal and economic situation is much worse than the US's, but without a credible plan for debt and deficit reduction in the US it might foreshadow what we can expect here as well.

Portfolio Specifics

Despite all the (currently) bad news, we do not (yet) think that the probabilities we assigned to the various economic scenarios used to guide our asset allocations have changed materially, and that is why our portfolio allocations have not changed. In fact, one could argue that what is going on in Greece is a good thing in that it may help encourage the US and other countries to act more aggressively to implement credible debt-reduction policies in order to avoid Greece's fate. So while the near-term



potential for a flight to quality or a spike in risk aversion remains high, we have not (yet) changed our longer-term (five-year) assessment of expected equity returns.

On the fixed income side, we do not have any direct tactical exposure to European sovereign debt. Both of our primary fixed income managers (PIMCO and Loomis Sayles) have said they are not/were not invested in any of the PIIGS' (Portugal, Ireland, Italy, Greece, and Spain) government debt. In terms of currencies, Chris Dialynas recently said that PIMCO is positioned for more euro weakness as a result of "the eurozone's fiscal risk premium" and Dan Fuss has minimal-to-zero euro exposure in his fund. If we do see a short-term flight-to-quality trade (i.e., money going into US Treasuries/the dollar from more volatile/riskier asset classes), our tactical position in emerging-markets local-currency bonds will almost surely take a short-term hit. Longer-term, however, the relatively strong economic fundamentals for emerging markets relative to developed economies continues to support the tactical thesis for owning emerging markets local debt.

From a contrarian perspective, extreme events and the fear generated by them can create great investment opportunities for fundamental investors with a longer time horizon willing to absorb shorter-term volatility and downside risk. Some of our fund managers, for example, tell us they are looking at potential stock-picking opportunities, particularly in Spain.

Finally, we continue to keep abreast of developments in Greece and the PIIGS, continue to read analyses and talk to fund managers to get their views and insights,

and continue to re-assess our risk exposures and portfolio positioning in the variety of scenarios that we think are likely to play out, as well as in lower-probability scenarios that would have very large negative outcomes. As always, we will apply our informed judgment in balancing the wide range of potential outcomes against each portfolio's shorter-term risk threshold and longer-term return objective.