

[Best Penny Stocks To Buy](#)

Up To 3000% Returns. Free Sign Up. Simply The Best Penny Stock Alerts.

www.OxOfWallstreet.com

[Debt Settlement](#)

Find Out In 60 Seconds If You Can Eliminate 70% Of Your Debt Legally

DebtHelp-USA.com

[3 Stocks Ready to Surge](#)

Get Stock Picks before they explode Picks that move 100%-300% in a day!

www.PennyInvest.com

Ads by Google



StreetTalk With Bob Lenzner

Smart Money Is Short Debt Of Greece, Spain, Portugal And Japan

Robert Lenzner, 04.30.10, 5:00 PM ET

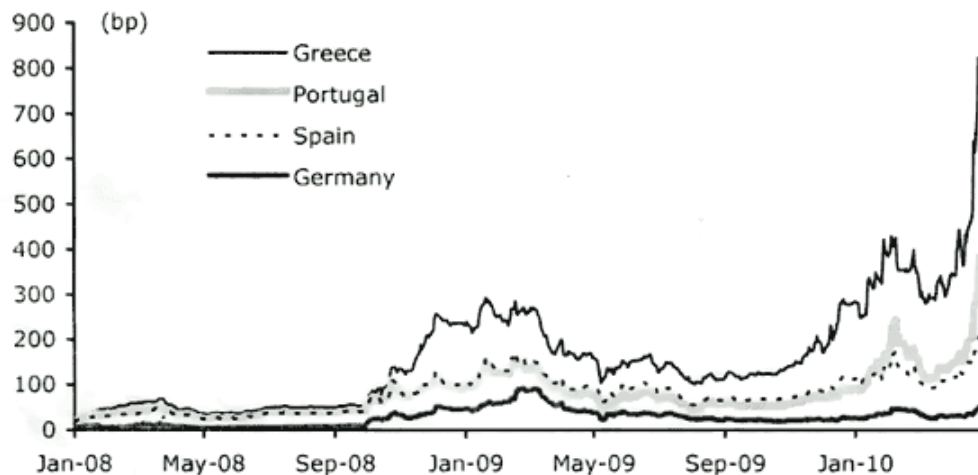
Smart money went short the bonds of Greece, Portugal, Spain and Ireland when the price of buying protection against default was cheap, some weeks ago. The price of buying insurance against default has spiked now that the crisis is full blown and a \$100 billion bailout of Greece is not a done deal.

The Smart Money, mostly hedge funds thinking ahead, were betting on the historic findings that over 800 years severe recessions are always followed by sovereign defaults. Smart Money had studied *This Time is Different*, a history of financial crises by Harvard professor Kenneth Rogoff and his co-author, Carmen Reinhart.

You want perspective on more than 2008-09, you have to read this book. One clear finding of Reinhart/ Rogoff is that sovereign debt default is in "a cyclical trough" based on a chart published by Hedgeye Risk Management this week. The percent of countries in default or restructuring is about the same as in 1930 as the depression took full force.

Figure 8

Greece, Portugal, Spain and Germany 5-year CDS spreads on government debt



Source: Datastream

Smart Money is worried. It has seen the need for bailouts segue from a few billion dollars for a single hedge fund, LongTerm Capital in 1998, to trillions on behalf of banks, insurance companies and quasi-public institutions like Fannie Mae to prevent an economic meltdown equal or worse than the 1930s. European Central Banks needed 27.5% of total European GDP to staunch the wounds, according to Jean-Claude Trichet, ECB chairman, at the Council on Foreign Relations this week. "The transmission of shocks were moving rapidly every half-day. There was no textbook to tell us what to do," he said.

Nor was he forthcoming about the odds of a deal for Greece. At stake in the first instance are European bank loans to Greece (\$190 billion), Portugal (\$240 billion) and Spain (\$840 billion). That's a nifty \$1.2 trillion exposure to the economically vulnerable European nations. Faced by French banks like Societe Generale, German banks and British banks as well. A big problem, but not of the proportion of the subprime crisis, which morphed into prime mortgages, LBO loans, credit card and automobile debt--making Citigroup, Bank of America, Fannie Mae, Freddie Mac, WAMU and others in effect insolvent. Still, a challenge to European bank balance sheets and further deterioration in European stock markets could be destabilizing.

[Double-Digit Dividend Yields! You can earn yields of 12% and higher on Canadian royalty trusts. Which ones are safe to buy and which will punish you? Click here for buys and sells from Richard Lehmann in Forbes/Lehmann Income Securities Investor.](#)

Bailout is necessary to avoid catastrophe. An effective response--expected by StreetTalk--can contain the contagion and the damage. But, bailing out Greece is roughly parallel to keeping Bear Stearns out of the bankruptcy courts to salvage counter party transaction. Too bad Germany can't just absorb Greece with aid from the ECB. If by some fool chance policy mistakes trigger an European Lehman disaster, then Smart Money could make a pile, John Paulson like. Both Martin Feldstein, Harvard economist, and Nouriel Roubini, NYU economist, believe Greece is going to default. Such turmoil would rile other nations, put further downward pressure on the euro. Smart Money will begin to look at Great Britain, maybe even Italy, as targets of the fallout in debt valuation.

Whatever transpires, there will be lower growth for Europe as Greece, Portugal, Spain and Ireland struggle to roll over their debts to prevent default. In the old days before the Euro, each nation would simply devalue its currency to pay off its debts like France did so many times decades ago. Should the euro continue to soften, European multinational companies like Nestle should be benefited, especially if revenues and profits are geared to emerging markets.

That's why Smart Money is looking at Japan as the next short because its debt is 100% of GDP, and it will be more difficult to refinance as the population gets older and may need to spend its savings, rather than buy more poorly yielding securities. The cost of shorting Japanese government debt is cheap as interest rates are so low. Expect to wait it out though, as crisis is not a short-term expectation. In the U.S. the crisis may take longer as rising debt levels eat into economic growth. Reinhart and Rogoff estimate that "debt in excess of 90% of GDP cuts growth by an average of 1.3% annually.

Smart Money hasn't quite made up its mind on how to cope with interest rates that are bound to rise as the deficit as a percent of the GDP also rises. Interest payments on U.S. debt are bound to be far higher than the CBO estimates, according to Leonard Burman, a Syracuse University professor of public affairs, writing in the *Milken Institute Review*.