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Are Geopolitics Enough to Avoid Grexit?

With less than ten days before a €303 million payment by the Greek government to the IMF comes due, there continues to be significant gaps between the position of Alexis Tsipras and Greece's creditors. Syriza continues to resist Eurogroup demands for pension cuts, delaying the implementation of minimum wage increases and proceeding with labor market reforms that would allow more flexibility for businesses to hire and fire. Still, we remain confident Greece will avoid a Grexit or sovereign default.

The important headlines out of Greece this morning are that the government and its creditors have begun to draft a 'staff level' accord for providing additional funding to the government. This is the necessary step before a final accord is reached and suggests a compromise is in the offing. Also, Germany's Foreign Minister Walter Steinmeier delivered a speech in Lisbon where he spoke more openly about the negative consequences of a Grexit, declaring there "wouldn't be any winner if Greece were to exit the euro." This suggests that the Foreign Ministry is now in league with Angela Merkel's talking points about the need to compromise to keep Greece in the euro for geopolitical reasons.

As client may recall on May 19, we [highlighted](#) our optimism on an eventual deal between Greece and its creditors, as we noted Chancellor Merkel had begun to suggest to party cohorts and hardliners that they may need to compromise and issue aid "even if Greece refuses to implement all changes demanded by creditors." Her trump card has been geopolitics. The braintrust around Merkel is united behind the thinking that a Grexit would mean the end of the euro, with a potential splintering of the EU, and potentially NATO itself. This is something neither Germany's hardliners nor its pan-Europeanists would like to see.

During the past twenty-four hours, we've seen additional evidence that Merkel is more aggressively lobbying for leniency from creditors on these grounds in order to keep Greece solvent and in the currency union. Yesterday, [Die Welt](#) noted how Germany's foreign policy office is now aligned with Merkel on the issue, and wishes to avoid a scenario of Greece "sinking it into turmoil and chaos, to perhaps even turn to the Russians, all because of a few billion euros." Another German media source, [Deutsche Wirtschafts Nachrichten](#), reports that Merkel has begun to discuss Greece's euro membership as part of its identity as a "NATO country" with the clear implication that her administration is willing to elevate "European security" as a legitimate justification for keeping Greece in the Eurozone. Accordingly, "The German taxpayer will get used to a third bailout – it will not be the last." Merkel's pragmatism on this issue will likely prevail.

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Of course, Finance Minister Wolfgang Schaeuble remains the hardliner on the issue and has been keeping the IMF engaged in negotiations so as to exert as much pressure as possible on Athens to make concessions. But with Athens remaining firm despite such pressure, it is not surprising that these geopolitical, European security arguments are being very publicly raised as the rationale for compromise. In our opinion, they reflect where the winds are blowing.

As for the timetable, Bloomberg suggests Greece has until late July before a Grexit and sovereign default scenario could occur. Technically, even if Greece fails to make its June 5th payment to the IMF, it does not necessarily spell default for Greece. There is at least a one-month grace period before the IMF would declare a default and that a late payment to the IMF would not necessarily force the ECB to shut off funds for the government. Crucially, on July 20, Greece will need to pay €3.5 billion due to the ECB. If it were to default on that debt, it could leave the ECB no other option but to shut off funds, which would set off the Grexit ball rolling.

Bottom line: Europe's hardliners are unlikely to counter the geopolitical argument from Merkel and others who are now arguing for leniency with Athens. In the face of this new rhetoric, continued resistance by Greece's creditors to compromise may wilt away rather quickly.

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