IF AT FIRST YOU DON'T SECEDE… GREXIT RISK AGAIN?

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I'm oen asked about unappreciated risks that can bite the stock market. Here's one: the threat of a Greek exit from the eurozone—Grexit—coming back.

Should this end up on the radar, the play is to underweight continental Europe in developed market equity allocations. At the end of this report, I will lay out some WisdomTree ETFs for this thesis.

Now, onto how things can fall apart for Greece.

Though the country faded from the front page in recent years, Greece's overwhelming debt load never actually went down; the burden just stayed on an even keel as the government—to its credit—abided by EU-mandated deep austerity packages. Many do not realize it, but Greece ran budget surpluses from 2016–2019.

COVID-19 lockdowns changed that.

Like most governments, Greece's national budget was blown out in 2020 as it marked a deficit equal to 10% of GDP. Deutsche Bank's economists see the country continuing to run a 7+% budget deficit this year and next. Another economics team at UBS is more optimistic, anticipating a deficit equal to 6% of GDP this year and 3% in 2022.

So much for a stabilized debt-to-GDP ratio. According to Eurostat, that figure jumped to 205.6% last year, a new high that looks to be heading higher. Toss in a recession somewhere along the line and this statistic will have a hard time falling.

Greece Government Debt-to-GDP Ratio (%)

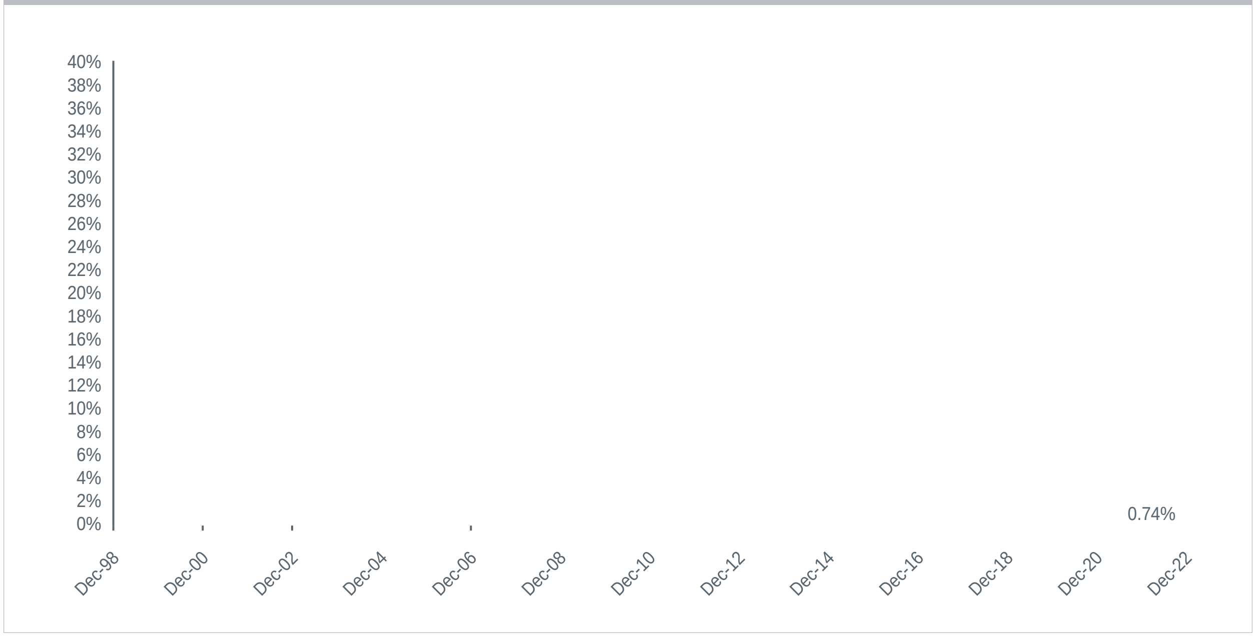
Source: Koyfin, 12/31/1980–12/31/2019, with data for 2020 from Eurostat and the European Commission.

The country also has one of the worst demographic profiles in Europe, which is saying something because low birth rates are ubiquitous, from the sunny climes of Italy to the frozen tundra of Scandinavia. With a birth rate of just 1.35 babies per woman—and with many of its young adults leaving for employment opportunities in more vibrant countries—I am not sure what could catalyze a reversal in Greece's population trend.

Population of Greece

Year	Population	

Greece 10-Year Bond Yield (%)



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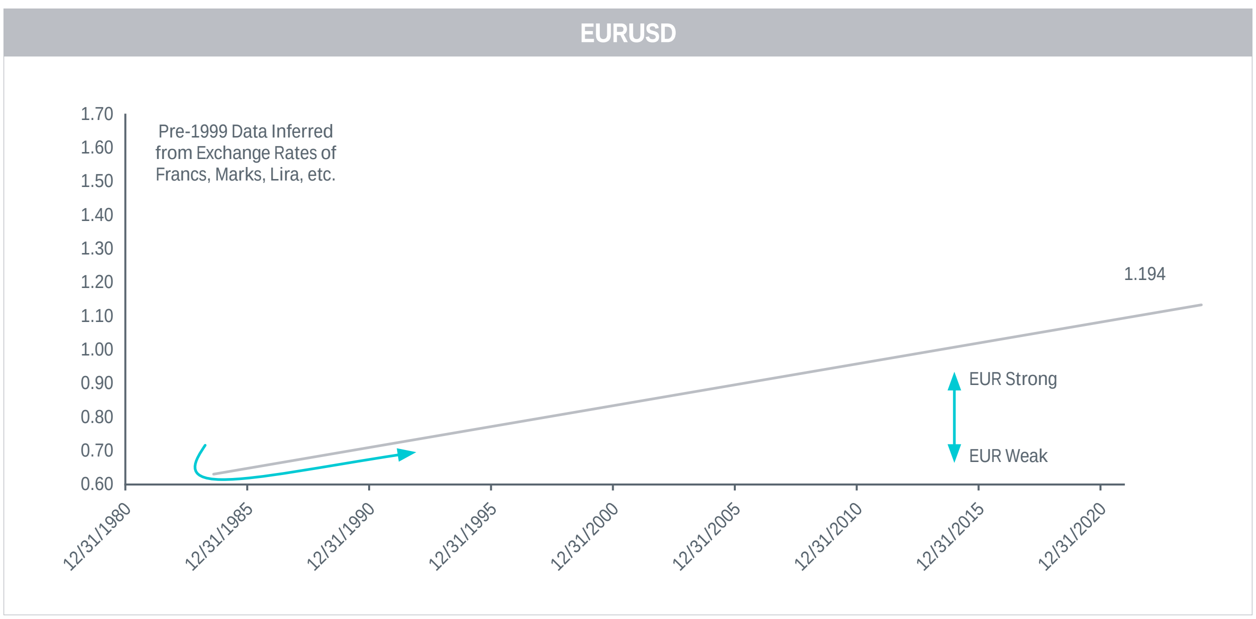
Start with the benchmark MSCI EAFE Index, which has 31% of its holdings in the eurozone.

Here are a few ideas, ordered by how much they tweak eurozone exposure relative to that Index.

First, owning the WisdomTree International SmallCap Dividend Fund (DLS) cuts the 31% down a little bit, to 24%. That may fit for someone who wants to underweight the eurozone without going too boldly away from EAFE. Our strategy may also prove more conservative than the MSCI EAFE Index, as 7% of DLS has companies with negative earnings, whereas 11% of the developed world's market capitalization is unprofitable. Additionally, the Fund screens higher on the quality factor, namely return on assets (ROA) and return on equity (ROE). That may help if bears arrive.

If you want to cut out the eurozone more than what you see in DLS, the WisdomTree International Quality Dividend Growth Fund (IQDG) holds 21% in the region. For avoiding the euro, IQDG has a sister fund, IHDG, the WisdomTree International Hedged Quality Dividend Growth Fund, that hedges away the currencies.

That may be helpful because the euro has been in a bull market since the global powers shook hands on the 1985 Plaza Accord, which sent the dollar into a bear spin.



Source: Koyfin, as of 6/17/21.

Finally, maybe you do not want 24% or 21% in Europe, instead preferring to shift capital to a country far, far away. For years, I have held that one of our more conservative mandates is the WisdomTree Japan SmallCap Dividend Fund (DFJ).

To me, its biggest appeal is its low volatility. The standard deviation since its 2006 launch is 13.9%, which is lower than the 17.4% for MSCI EAFE in that time. Critically, DFJ's risk is lower than the 15.2% standard deviation on the S&P 500. That presents an interesting situation where total portfolio risk may be reduced by adding foreign equities—Japanese ones—in the event of a Greek crisis.

Country Weights				
Currency	**Country**	**MSCI EAFE Index**	**WisdomTree International SmallCap Dividend Fund (DLS)**	**WisdomTree International Hedged Quality Dividend Growth Fund (IHDG)**
EUR	France	11.4%	3.5%	6.7%
EUR	Germany	9.4%	3.2%	6.0%
EUR	Netherlands	4.1%	1.0%	3.8%
EUR	Spain	2.6%	3.2%	0.5%
EUR	Italy	2.5%	3.3%	0.9%
EUR	Finland	1.0%	4.4%	2.6%
EUR	Belgium		2.2%	0.1%
EUR	Austria		1.5%	
EUR	Ireland		0.5%	
EUR	Portugal		1.6%	0.2%
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JPY	Japan	23.5%	23.7%	17.9%
GBP	United Kingdom			

Sources: WisdomTree, MSCI, as of 5/31/21. Subject to change. You cannot invest directly in an index.

There are risks associated with investing, including possible loss of principal. Foreign investing involves special risks, such as risk of loss from currency fluctuation or political or economic uncertainty. Funds focusing their investments on certain sectors and/or smaller companies increase their vulnerability to any single economic or regulatory development. This may result in greater share price volatility.

To the extent the Fund invests a significant portion of its assets in the securities of companies of a single country or region, it is likely to be impacted by the events or conditions affecting that country or region. Dividends are not guaranteed, and a company currently paying dividends may cease paying dividends at any time. Investments in currency involve additional special risks, such as credit risk and interest rate fluctuations. Derivative investments can be volatile, and these investments may be less liquid than other securities, and more sensitive to the effect of varied economic conditions. As this Fund can have a high concentration in some issuers, the Fund can be adversely impacted by changes affecting those issuers. The Fund invests in the securities included in, or representative of, its Index regardless of their investment merit, and the Fund does not attempt to outperform its Index or take defensive positions in declining markets. Due to the investment strategy of this Fund, it may make higher capital gain distributions than other ETFs. Please read the Fund's prospectus for specific details regarding the Fund's risk profile.