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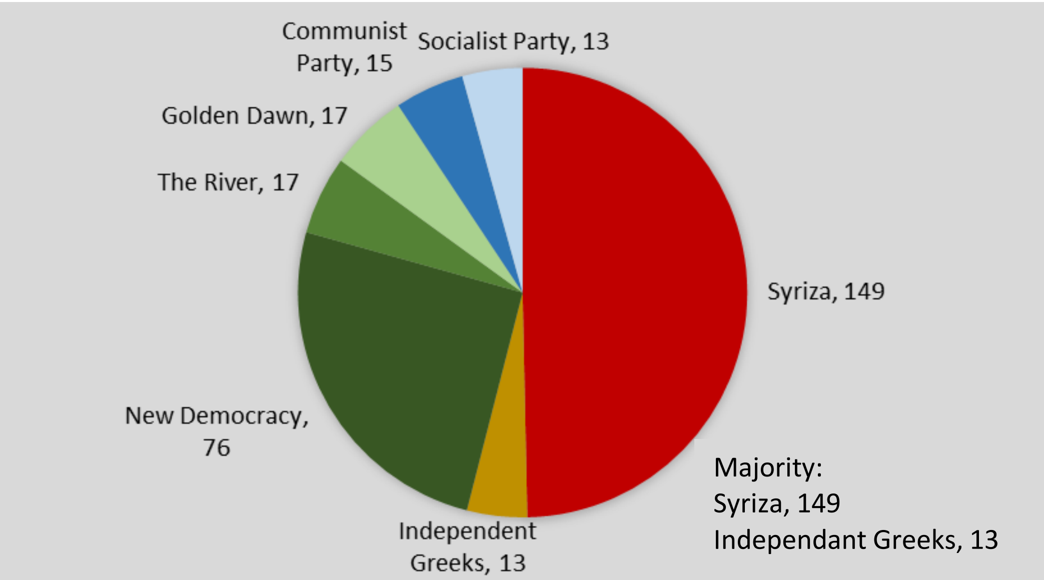
THE REAL REASON WHY YESTERDAY'S GREEK VOTE WAS IMPORTANT

- **The Greek parliament approved a package of reforms last night. The approval was a necessary step to move forward with a new bailout, to pave the way for a bridge loan, and to get the ECB to increase ELA access for Greek banks.**
- **The fact that 39 members of the current majority voted "no" means that the majority does not exist anymore. This is the real good news for investors – the radical Syriza component has effectively called itself out, and this should make any future government more stable and more pro-euro.**
- **The issue of how to get a bridge loan to Greece to cover debt payments until a bailout is agreed is politically very thorny. The use of an EU-wide mechanism (as opposed to EZ-wide) is quite possible. While it would be toxic for UK politicians, it might be the best solution for everyone else.**
- **Overall, we would look for risks associated with Greece to continue to diminish in coming days and weeks, even though the negotiations for the actual bailout won't likely be always smooth.**

COMPOSITION OF THE GREEK PARLIAMENT



Source: The Hellenic Republic.

The vote in parliament in favor of the austerity measures was 229-64, with 39 members of the governing coalition voting against it. This means that the current majority doesn't exist anymore.

Passage of most of the measures agreed upon with the creditors was never in doubt because most of the opposition parties pledged support. Still, the favorable vote removes whatever little uncertainty there was at this point that Greece is now committed to doing whatever it takes to stay in the euro. Investors probably shouldn't expect many negative surprises to come from their side.

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But the more important news from investors from last night was that the current majority didn't hold together. Of the 64 "no" votes, 39 belonged to the current majority. Since Syriza and the Independent Greeks add up to only 162 of the 300 seats, the 39 dissents mean that the current majority effectively does not exist anymore – at least not on crucial issues such as the future of Greece in the EZ.

It is still unclear at this stage how the political impasse will be resolved. There are three broad possibilities:

1. **The current government manages somehow to stay in power.** Tsipras might be able to substitute some ministers and continue to lead the current coalition, which would still support him on issues other than those related to the bailout. On bailout matters Tsipras could count on opposition votes. This probably wouldn't last long, but enough to see the remaining conditions for the bailout passed.

2. **A new "national unity" government is formed.** This would be the ideal solution because it would give the new government stability and it would ensure a duration longer than a few weeks. Tsipras would probably stay as prime minister, but that wouldn't be that important – a solid pro-euro majority would be what matters most for investors.

3. **New elections are called soon.** This would add uncertainty, obviously, but as a base case the most radical wing of Syriza would find itself isolated. The moderate wing would probably ally itself with The River or other more centrist parties, and a new, less-radical leftist government could be formed that way. A national unity government or an outright win by New Democracy are also possible outcomes.

For investors, the important thing is that all the scenarios above are more stable than, and therefore preferable to, what we have seen in the past seven months.

It would be hard to block financing under the EFSM. A qualified majority of 55% of member states and 65% based on population is sufficient for passage.

VOTING SHARES IN THE EFSM

Country	Population	Voting Share
Germany	80.8	15.9%
France	65.9	13.0%
United Kingdom	64.3	12.6%
Italy	60.8	12.0%
Spain	46.5	9.1%
Poland	38.5	7.6%
Romania	19.9	3.9%
Tne Netherlands	16.8	3.3%
Belgium	11.2	2.2%
19 Others	103.7	20.4%
Total	**508.4**	**100.0%**

Source: European Union.

From the point of view of the creditors, the urgent issue is how to make sure Greece will have the funds to pay the ECB on Monday and therefore allow the ECB to comfortably increase ELA access for Greek banks. At this point the most likely scenario seems a proposal put forth by the European Commission to provide Greece a bridge loan of €7 billion for the month of July via the EFSM.

The EFSM is an EU-wide vehicle, rather than a EZ vehicle, but it would allow for quick payment to Greece. The EFSM creates a headache for non-EZ governments, especially the UK one, which has to deal with anti-EU sentiment at home ahead of the EU-membership referendum. Under EU rules, the EFSM can be deployed with just a 65% percent voting share based on each country's population – the UK (and other reluctant smaller countries) wouldn't have veto power, as shown in the table above. In any case, steps are likely to be taken to guarantee non-EZ countries wouldn't lose money on the deal.

Looking ahead, our base case scenario is that the ECB will authorize an increase in ELA access to Greek banks, thus allowing the banks to reopen, albeit with capital controls still in place. That decision could come already at today's governing council meeting or after a bridge loan to Greece is approved. That – the approval of the bridge loan – should also come soon given Monday's scheduled maturity of Greek debt held by the ECB.

From a market perspective we would expect these favorable developments to continue to reduce investor risk aversion and thus to support risky assets. Equity prices in Europe have made up much of the ground they lost recently, and should continue to gain if the situation in Greece evolves according to plan. The same can be said for peripheral bond prices relative to German Bund prices. The euro should remain under some pressure, both because of a potential Fed rate hike in September and because of the possibility that the ECB will eventually have to do more QE due to the still substantial disinflationary risks.