

Cypriot banking crisis scr

[Finance](#), [Banking](#)



The current crisis of banking system in Cyprus had raised difficult moral dilemmas for Cypriot government, members of Euro Union and other affiliated governments.

Cypriot banks became unable to secure the deposits due to several reasons: the Greek crisis, crisis in real estate sector. It provided relatively high income on deposits, which is always associated with risky investments. The macroeconomic situation in the world only worsened the situation. To sum up, the some of the banks simply lost themoneyof the depositors. In this case, the problem of allocation of losses appeared. Who should bear the losses for the mistakes made by Cypriot banks, which were aggravated by the multiple unfavorable circumstances?

The depositors who brought their money to banks? All of them? Prosperous European countries? We should remember, that the ones who are in charge of this situation simply can't cover that costs (banks have no liquid assets cover the losses). In this paper we discuss the impacts of different possible solutions of this problem from the point of ethics theories. We start we describing the background of the problem including time-line of facts, the reasons for crisis of Banking System, than we move on to reviewing different options of how to save Cypriot economy using theories of ethics.

Time-line * 14-15 March – EU-summit as a result of which was reaching the deal between Cyprus Euro Zone and IMF (International Monetary Fund) for a 10 billion Euro bailout on condition that Cyprus imposes a one-off levy of 6, 75% to insured deposits (under 100 000 Euro) and 9, 9% to uninsured deposits (over 100 000 Euro). So that Cyprus will provide 5, 8 billion Euros to secure the 10-billion bailout. * March 16 – first day of Cyprus Bank closure

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after the government announced Bank holidays. The idea of imposing a tax on ordinary depositors resulted in mass protest-demonstration of Cypriots, citizens also protested against Germany dictating such harsh conditions. It had also caused anxiety in other countries – for setting such an extraordinary and threatening precedent. * March 19 – the Cyprus Parliament rejects a 10 billion Euro bailout package (lawmakers voted 36 against 19 abstaining) arguing that it is unacceptable to take money from regular account holders.

- The chairmen of the Cyprus Investor Association said Parliaments' rejection of the deal « will buy us some time to see if we can come up with a better agreement»
- The President of Cyprus Nicos Anastasiades proposed to make an exception for deposits with less than 20 000 Euros to calm the public, but that didn't work out either
- The failed vote intensified the relationship between Cypriot government and EU. Cypriots accused EU for pressing them to accept an unacceptable deal that heats ordinary savers and pensioners.

In return, German officials and IMF stated that they didn't force Cypriot government to impose the deposit on depositors but that one way or another the country must come up with the rest 5, 8 billion Euros to secure the bailout. The next step included testing to which extent Russia would be willing to assist Cyprus in this difficult situation. Investments of Russian depositors accounted for about 20 billion Euros in Cypriot banks, so Russia is for sure an affiliated party.

Russian officials reacted furiously to the proposed tax deposit bank

March 22 – Cyprus adopted legislation that allows the government to split the Cypriot lenders into good banks and bad banks and creates resolution framework to wind down banks. March 24 – a new bailout deal between Eurozone and Cyprus. Cyprus will get a 10 billion Euro bailout on condition that Laiki (Popular) Bank, the second largest bank in Cyprus will be wound down.

The deposits under 100 000 Euros will be fully compensated by the government, the depositors with more than 100 000 Euros on their accounts will face extremely huge losses. In this case Cyprus successfully avoided being excluded from EU, which occurred to be highly probable. What is more, this solution pensioners and clients with small deposits (which mean with low income level) won't be affected, so the anger of the public will be reduced. Finally, two biggest Banks will be restructured: Laiki Bank will be wind down, Bank of Cyprus will capitalize at the expense of it's clients; insured deposits of Laiki Bank will be transferred to Bank of Cyprus, owners of uninsured deposits of Laiki Bank will lose up to 80% of their deposits; 37, 5% of uninsured deposits of Bank of Cyprus are transferred into stocks of Bank of Cyprus which actually cost nothing, 22, 5% will be frozen so clients have no right to use that sums of money.

In this case the costs of bank mistakes lay down on clients with deposits over 100 000 Euros. By the way, most of such clients are Russian (Russian investments in Cypriot bank sector are estimated 26 bn Euro, they exceed Cypriot GDP which is around 18 bn Euro). Russians were happy to use Cyprus

as an offshore – due to double taxation agreement. This was a place where nobody asked where that money came from. At the same time EU and Cyprus were happy to transfer the costs to Russian depositors by expropriating their deposits.

The Greek financial crisis had put in danger the stability of all Eurozone. But the greatest impact was imposed on Cyprus due to their strong economic and financial bonds. Cyprus's banking sector was affected the most. It became quite clear that banking system of Cyprus is in danger a couple of years ago. Stavrakis -the Finance Minister of Cyprus said: « We are a small country and most importantly, we have a banking system which has invested heavily in Greek bonds». Nevertheless, the minister assured that Cypriot banking system was safe and sound, that it had a strong capital base and that there was a huge inflow of foreign deposits which helped to stabilize the situation. Anyway, the prime reason of crisis in Cypriot banking sector is cancellation of Greek bonds. It was not a secret that Cypriot banks invested heavily in long-term Greek bonds, so when a default in Greece was announced and it was stated that Greece is not going to fulfill its bonds obligations, and, as a result, the trust in Cypriot banks declined. As the trust in banks decline, depositors tend to take back their money.

But this is a trap: something happens in the banking industry, depositors leave, at the same time a lot of bank assets are frozen in long-term obligations. Theoretically, the bank has or practically has enough assets to return everything to clients, but these assets are not liquid, so at the moment when clients start to panic and claim for their money, the bank is under threat of running out of liquid assets to pay to clients. This can happen

to any bank, even the most reliable one. The moment panic begins - the bank is under great threat.

This is why laws that don't allow taking back deposits at any moment may be quite reasonable. Here is a brief summary of reasons of Cypriot banking sector crisis: Huge investments of Cypriot banking sector in Greek default economy =; sufficient losses and asset write-downs of Cypriot banks * A strong offshore orientation of Cypriot economy: total sum of deposits heavily exceed GDP

- As a result the government (does it have to?) is not able to compensate the losses of depositors
- Unfavorable macroeconomic situation in EU and world The fact that Cypriot banks haven't revalued their assets for a long time, so the assets were overestimated