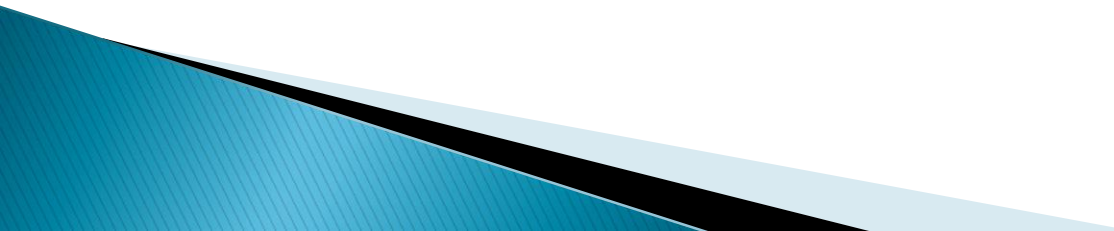


On Cyprus and its Aftermath

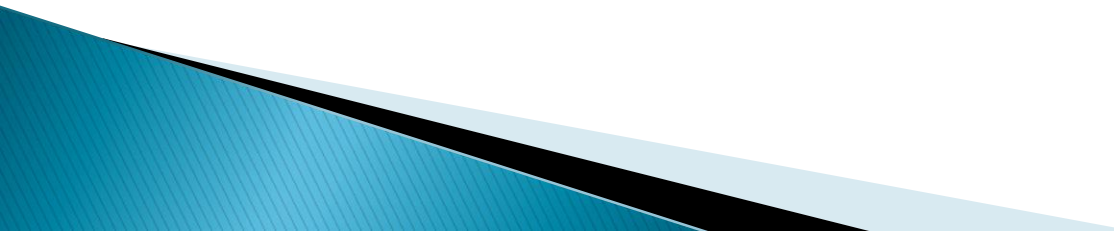
Presentation by William White

Euro50 Group Meeting
Rome, Italy
23–24 June, 2013

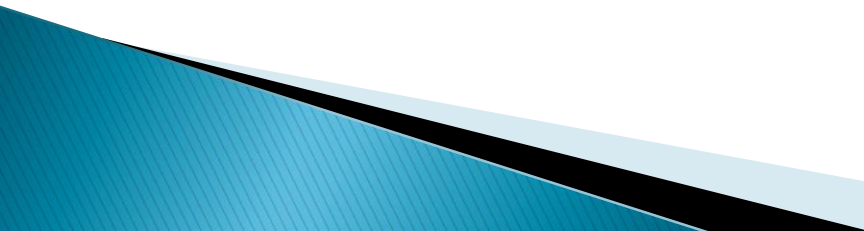
Problems in the world, the Eurozone and Cyprus

- ▶ The financial and economic crisis is global
 - ▶ Its roots lie in excessive credit creation and exchange rate arrangements
 - ▶ Leaving both borrowers and lenders dangerously exposed
 - ▶ Eurozone is a microcosm of global problems
 - ▶ And Cyprus is a microcosm of Eurozone problems
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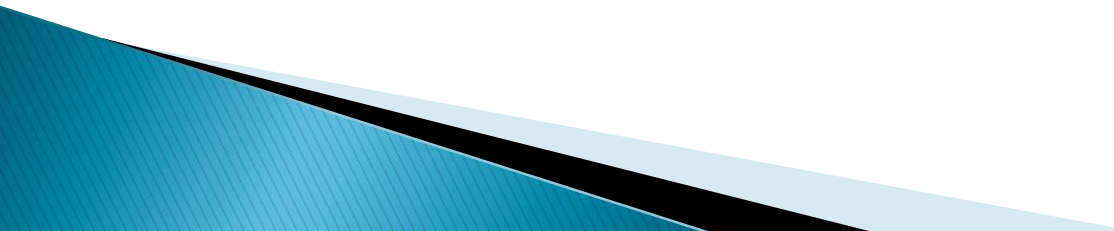
The Eurozone crisis to date

- ▶ Interest rates in core and peripheral countries converged starting in 1997
 - ▶ Easy borrowing conditions in peripheral countries led to a variety of excesses
 - ▶ Banking crisis erupted in 2008 and then spread to sovereigns
 - ▶ Today, both banks (core and peripheral) and peripheral sovereigns have serious funding problems
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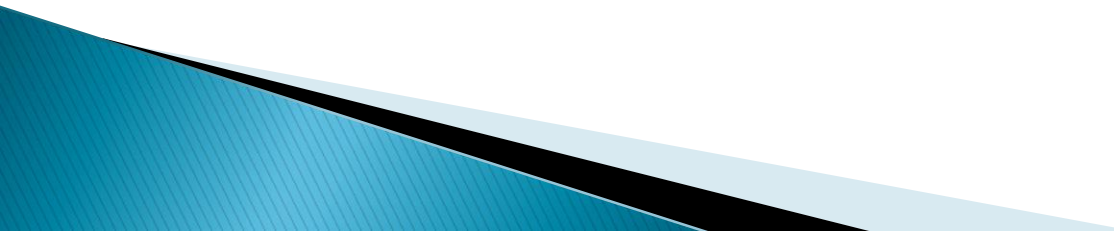
Crisis has not led to the right policy responses

- ▶ Wrong to tighten fiscal policies everywhere
 - ▶ Wrong to treat funding difficulties as problems of liquidity rather than solvency
 - ▶ Wrong to suggest that Greece could/should leave the Eurozone
 - ▶ And policy “timidity” has raised fundamental concerns about the capacity of policymakers to keep the Eurozone intact
- 

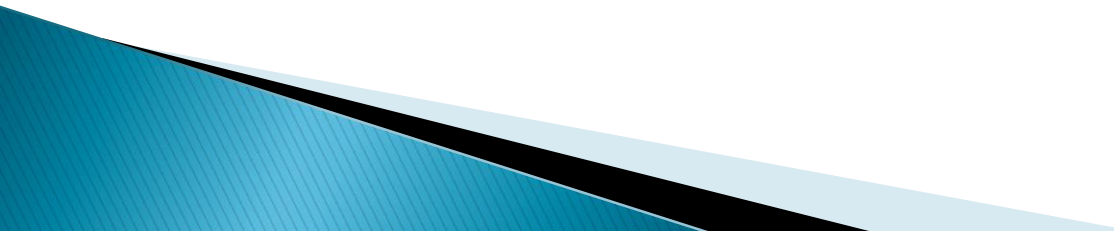
Finding solutions: should, could and would

- ▶ Should: strongly held beliefs and different visions of Europe
 - ▶ Could: no effective mechanism for dispute resolution, exit, bailout or restructuring
 - ▶ Would: a democratic deficit that promotes division
 - ▶ Leaving policy “behind the curve”
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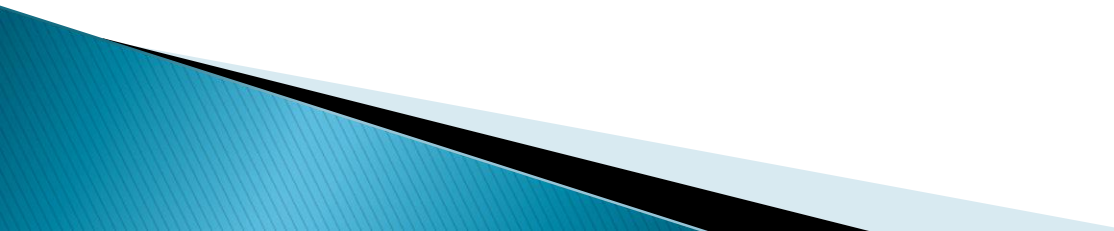
Policy Challenges prior to Cyprus

- ▶ Short term liquidity problem: restoring confidence in peripheral sovereigns and banking systems
 - ▶ Short term solvency problem: restoring bank lending in both the periphery and core
 - ▶ Long term problems: fiscal and financial oversight must move to the centre
 - ▶ Long term problems: structural reforms to raise growth and competitiveness
- 

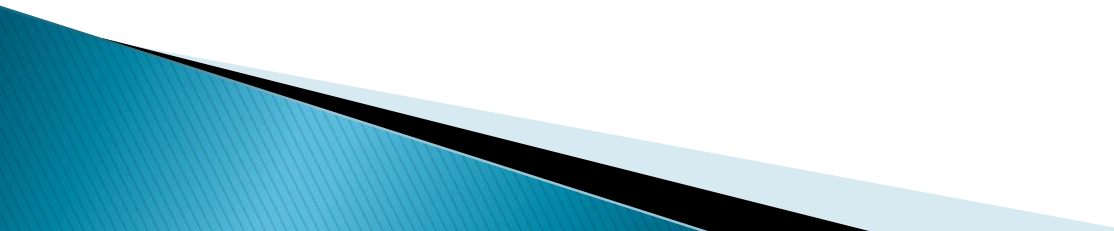
Responses to date

- ▶ Short term liquidity: money still leaving periphery. Regulators and the ECB
 - ▶ Short term solvency: the Japanese solution
 - ▶ Long term challenges: need for various “unions” recognized BUT
 - ▶ Long term challenges: progress BUT
- 

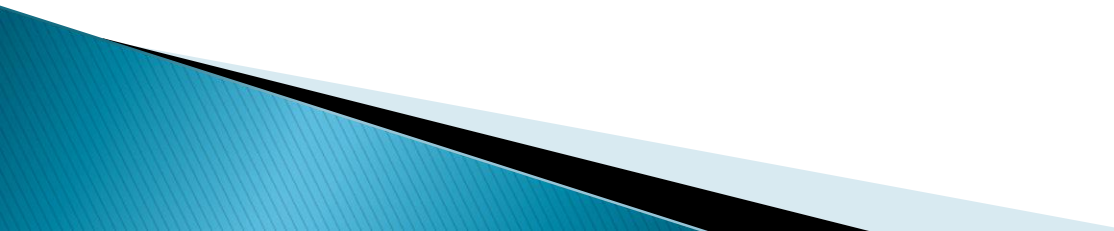
The treatment of Cyprus: still more of the same?

- ▶ Just enough liquidity
 - ▶ Banking system left unhealthy
 - ▶ No real Eurozone burden sharing
 - ▶ Locals bear the burden with predictable results
- 

The treatment of Cyprus: new elements and implications?

- ▶ Bailing in the creditors
 - ▶ Capital controls
 - ▶ Dictating the “business model”
 - ▶ Forced gold sales
 - ▶ Adjustment programs and structural reforms
- 

The treatment of Cyprus; broader implications

- ▶ For the vulnerability of the Eurozone
 - ▶ For banking union
 - ▶ For the European Central Bank
 - ▶ For the International Monetary Fund
 - ▶ And for the global economy?
- 

Pre Cyprus scenarios revisited

- ▶ An orderly outcome: market optimism continues
 - ▶ A disorderly outcome : markets deteriorate but further policy measures calm them
 - Measures provide hope for peripherals
 - Measures fail to provide hope for peripherals
 - ▶ A very disorderly outcome: markets panic and countries choose to leave the Eurozone
 - Debtor countries leave
 - Creditor countries leave
- 