

## Comment/European Law Report

# Malta is different to Cyprus



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**I**t should be shouted out loud: Malta is not Cyprus. Other than both being islands and members of the European Union and the eurozone, there is no similarity between the two countries. What has been happening in Cyprus has no bearing in Malta and there is no room for the jitters some people are experiencing.

This needs to be said in view of the backcloth of the Cyprus crisis. That came about for two reasons. The first is the island's close association with Greece. Long years of political clamour for union with Greece failed. Cyprus enjoys statutory independence. But its ties with Greece are vast.

When Greece began to experience its multiple crises, the tremors were bound to be felt in Cyprus. They were felt most strongly because of the second main difference to Malta.

The two islands have been promoting themselves as financial centres. Yet the models used

could not be more different. Malta enacted legislation, with bi-partisan backing, intended to ensure that Malta was not viewed as some brass plate tax haven. Its structured statutory provisions rest on very strict regulation by the Malta Financial Services Authority.

With accession to EU membership, Malta has been attracting a stream of investment proposals, diversified among banking, insurance and more lately hedge funds. Gaming companies, covered under separate legislation, are a linked sector.

Malta is not dependent on any one country. It does have a large banking centre, now boasting 27 units with the latest addition Agri Bank. But domestically it is dominated by two relatively large banks, Bank of Valletta and HSBC Bank Malta.

Both have a very extensive deposit and asset base. On the asset side, the banks' lending is to a huge extent to domestic borrowers, which are monitored closely by the banks' credit managers. A low element of non-performing loans is fully provided for under specific provisions.

General provisions are also in place to cover contingencies. Provisions are reviewed regularly and highlighted in the annual returns of the two institutions. While each of them has substantial exposure to construction and building industries, they have passed through the large decline in the market value of property successfully.

Investment assets suffered to the extent they were invested abroad, but have recovered to a considerable extent. A good proportion of investments is held in government stock, which is massively lent to domestic investors, and as such not subject to panic or strategic dumping.

The two banks' overall conservative philosophy, much

encouraged by the regulator, has paid dividends in terms of the calm and serenity of the institutions. Admittedly, there are other banks operating domestically some of whom might seem too aggressive in their bid for deposits. But they are comparatively minor, and under close watch by the regulator.

The Cyprus financial sector model is completely different. It is dangerously concentrated on Russian investors. To the extent that their deposits are made of clean money, the concentration was still excessive, and thereby very sensitive. There is also the suspicion that part of the Russian money in the Cypriot banks represents money-laundering flows.

The two factors, whereby their deposits made up some eight times the Cypriot GDP, were dangerous in the best of circumstances. They provided the leading Cypriot banks with more liquidity than could be absorbed through lending to the domestic economy. The banks therefore lent extensively to commercial interests in Greece and also invested heavily in Greek sovereign bonds.

As Greece passed through its debilitating troubles, which weakened the commercial sector and also forced the monetary authorities to impose 'haircuts' on bond holders, the Cypriot banks suffered huge losses. When the European Commission, ECB and IMF troika began to consider Cyprus's requests they were influenced by two

main factors. One, that the Cypriot model was no longer valid, if it ever had been that. The other that the troika, especially under German influence, was not minded to save the Russian investors who had flooded the island with their honest or ill-gotten gains.

To gain the bail-out Cyprus had to effect a bail-in, including slicing off deposits over €100,000, which might save the banking system but will have a further negative effect on the island's GDP for several years, especially if the island's newly identified gas fields have not been properly exploited, which might take years to accomplish.

The two vastly different structures should calm jitters in Malta, even though Cyprus has shown no one is too small to fail. The trouble is that the comparative line of reasoning used here is, to a considerable extent, unintelligible to most of the Maltese population. It is important that the message is spread in a sustained manner. By the Government and opposition speakers. By the media. By commentators. By anyone whose voice carries.

It would be ironic if a problem develops out of any incorrect reading of the situation.

That said, I have no doubt that the Malta Financial Services Authority will be following developments with an eagle eye and will take whatever further steps are required. Such as to shoo away Russian money seeking alternative deployment.

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