



Aftermath of the Elections: What Lies Ahead?

At last, after a prolonged campaign period, elections are over and the new Cypriot government has taken over from March 1. Expectations are high, and there seems to be a revived optimism that a new government, with fresh and innovative ideas, will help us resolve (sooner than later), the numerous problems that our country is facing. Psychology plays a big role in shaping the future, and the first signs are that this has improved, both within the country but also the way that foreign officials and investors are viewing Cyprus.

However, the massive problems are still there and the new government has a very difficult task to accomplish. First, there has to be a final agreement and signing of the memorandum, by the end of March, the latest. The reason is that it would take some time for the funds from the Troika to arrive, and we all know that on June 3 we have EUR 1.4 bln government bonds expiring that we need to repay. Thus, June 3 can be considered our "fiscal cliff" and we need to make sure that by then we have the funds available to honour our obligations, otherwise that would imply default with all of its negative consequences. Before arriving, though, to the final agreement, a lot of work still needs to be done. First, we might need to secure a short-term "bridging" loan, either from the Europeans or a third party, to have enough funds for our immediate needs before receiving the money from the Troika. The new government also needs to prove to the other EU members that we mean business by signing the memorandum as well as taking all the necessary steps to accomplish the reforms and fiscal/banking adjustments under the agreement. We also need to convince them that they wrongly and unfairly accuse us of being a "tax haven" or money-laundering location. Unfortunately, the prolonged delay in agreeing with the Troika led us to get caught in the middle of an election campaign in Germany. The outcome is that the German government and politicians are extremely harsh on us in an effort to prove to their own taxpayers that they are not using their money for bailouts of "corrupted" countries.

Furthermore, we need to take measures that will make our debt sustainable, so that we stop this damaging discussion about haircuts either on government debt holders, or on uninsured depositors in our banking system. First, a meaningful haircut on government debt holders (that

would substantially lower our debt level) is extremely difficult to achieve given the fact that only a small portion of our government debt is owned by foreign private investors (less than 21% of GDP). Given the fact that our debt in the near future could reach levels above 140% of GDP, such a haircut would not make a huge difference. Second, a haircut on uninsured depositors (i.e. deposits of more than 100,000 euros that are guaranteed by our Central Bank) can easily cause a bank run and a complete destruction of our financial and banking sector. Being a financial and service centre (almost 50% of our GDP comes from this sector) one can understand the outcome for the entire economy. Thus, the new government needs to find alternative ways to make the public debt sustainable, so as to avoid privatisations of profitable state-owned enterprises that are strongly imposed on us by the Troika. Over and above the much anticipated recapitalisation of our local banks, the government needs to include anti-austerity measures that will promote growth and help solve what seems to be our biggest problem – unemployment – by creating new jobs. These measures could be incentives for swift recovery of the crucial construction/ land-development sector, the utilisation of government land, the development of technological parks, the creation of casinos, and the drastic reduction of bureaucracy in the civil service, among others. Obviously, the prospects that lie ahead from the recent findings of natural gas in our Exclusive Economic Zone is a reason to be optimistic about the future, but it will take time to start benefiting and earning revenues that would substantially lower our public debt level.

Overall, although many obstacles lie ahead, I am optimistic that with the right and carefully-thought moves we can actually get the economy back on track. I would even say that in the medium to long-run these changes that are being brought upon us by the Troika and the memorandum will make our economy more resilient. By implementing the provisions of the memorandum we can emerge from the crisis as a much more solid and structured economy, with more fiscal discipline, and a healthier banking sector.

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