EU deal emerging to shut Cyprus bank, inflict losses

By Annika Breidthardt and Jan Strupczewski

BRUSSELS | Sun Mar 24, 2013 9:14pm EDT

(Reuters) - Cyprus reached an outline deal with international lenders for a 10 billion euro ($13 billion) bailout that would shut down its second largest bank and inflict heavy losses on uninsured depositors, an EU spokesman said early on Monday.

The tentative deal emerged after fraught negotiations between President Nicos Anastasiades and heads of the European Union, the European Central Bank and the International Monetary Fund - hours before a deadline to avert a collapse of the banking system.

The draft proposal, which still has to be approved by euro zone finance ministers, would save the Mediterranean island from financial meltdown by winding down Popular Bank of Cyprus, also known as Laiki, and shifting deposits below 100,000 euros to the Bank of Cyprus to create a "good bank".

Deposits above 100,000 euros, which under EU law are not guaranteed, would be frozen and used to resolve debts, and Laiki would effectively be shuttered. The EU spokesman said no levy would be imposed on any deposits in Cypriot banks.

A senior source involved in the talks said Anastasiades had threatened to resign at one stage if he was pushed too far. A first attempt at a deal collapsed last week when the Cypriot parliament rejected a proposed levy on all deposits.

EU diplomats said the president, flown to Brussels in a private jet chartered by the European

Commission, had fought to preserve the country's business model as an offshore financial center drawing huge sums from wealthy Russians and Britons.

The key issues in dispute were how Cyprus would raise 5.8 billion euros from its banking sector towards its own financial rescue, and how to restructure the outsized banks.

The speaker of the Cypriot parliament, Yiannakis Omirou, told reporters in Nicosia a bailout deal was "taking shape".

The EU's economic affairs chief Olli Rehn said earlier there were no good options but "only hard choices left" for the latest casualty of the euro zone crisis.

With banks closed for the last week, the Central Bank of Cyprus imposed a 100-euros per day limit on withdrawals from cash machines at the two biggest banks to avert a run.

French Finance Minister Pierre Moscovici rejected charges that the EU had brought Cypriots to their knees, saying it was the island's offshore business model that had failed.

"To all those who say that we are strangling an entire people ... Cyprus is a casino economy that was on the brink of bankruptcy," he told Canal Plus television.

The euro gained against the dollar in early Asian trading. Analysts had said failure to clinch a deal could cause a financial market selloff, but some said the island's small size - it accounts for just 0.2 percent of the euro zone's economic output - meant contagion would be limited.

The abandoned levy on bank deposits had unsettled investors since it represented an unprecedented step in Europe's handling of a debt crisis that has spread from Greece, to Ireland, Portugal, Spain and Italy.

ANXIOUS MOOD

In the Cypriot capital, Nicosia, the mood was anxious.

"I haven't felt so uncertain about the future since I was 13 and Cyprus was invaded," said Dora Giorgali, 53, a nursery teacher who lost her job two years ago when the school she worked at closed down.

"I have two children studying abroad and I tell them not to return to Cyprus. Imagine a mother saying that," she said in a central Nicosia square. "I think a solution will be found tonight but it won't be in the best interests of our country."

Cyprus's banking sector, with assets eight times the size of its economy, has been crippled by exposure to crisis-hit Greece.

Without a deal by the end of Monday, the ECB said it would cut off emergency funds to the banks, spelling certain collapse and potentially pushing the country out of the euro.

Conservative leader Anastasiades, barely a month in office and wrestling with Cyprus' worst crisis since a 1974 invasion by Turkish forces split the island in two, was forced to back down on his efforts to shield big account holders.

Anticipating a run when banks reopen on Tuesday, parliament has given the government powers to impose capital controls.

PARLIAMENT

About 200 Cypriot bank employees protested outside the presidential palace on Sunday chanting "troika out of Cyprus" and "Cyprus will not become a protectorate".

In a stunning vote on Tuesday, the 56-seat parliament rejected a levy on depositors, big and small. Finance Minister Michael Sarris then spent three fruitless days in Moscow trying to win help from Russia, whose citizens and companies have billions of euros at stake in Cypriot banks.

On Friday, lawmakers voted to nationalize pension funds and split failing lenders into good and bad banks - the measure likely to be applied to Laiki. The plan to tap pension funds was shelved due to German opposition, a senior Cypriot official told Reuters.

It was not immediately clear whether the revised bailout plan would require parliamentary approval or whether the government could try to bypass the assembly.

The tottering banks hold 68 billion euros in deposits, including 38 billion in accounts of more than 100,000 euros - enormous sums for an island of 1.1 million people which could never sustain such a big financial system on its own.

(Additional reporting by Luke Baker, John O'Donnell, Phil Blenkinsop and Robin Emmott in Brussels, Michele Kambas, Costas Pitas, Laura Noonan, Karolina Tagaris, Yannis Behrakis and Yorgos Karahalis in Nicosia.; Writing by Giles Elgood and Paul Taylor; Editing by Mike Peacock)

Comments (3)

Harry079 wrote:

"Deposits above 100,000 euros, which under EU law are not guaranteed, would be frozen and used to resolve debts, and Laiki would effectively be shuttered."

Then they should do the same to the deposits of ALL EURO Nations since under EU law they are not guaranteed and just get it over with.

Mar 24, 2013 9:05pm EDT -- Report as abuse

Greenspan2 wrote:

This was done in the US at the height of the financial crisis to the surprise of many depositors at US banks that folded or were reorganized. It is more evidence that the banking industry world wide needs more regulation and should return to its original charter of being a public utility to provide loans for community and business development.

Mar 24, 2013 9:14pm EDT -- Report as abuse

Greenspan2 wrote:

This was done in the US at the height of the financial crisis to the surprise of many depositors at US banks that folded or were reorganized. It is more evidence that the banking industry world wide needs more regulation and should return to its original charter of being a public utility to provide loans for community and business development.

Mar 24, 2013 9:14pm EDT -- Report as abuse

See All Comments » Add Your Comment