



Il-Fehma tal-Gvernatur #4: Never a dull moment

The banking turmoil in the United States and Switzerland is discussed in this Vlog. The financial stability in the Eurosystem, including Malta, is compared, and contrasted to the countries affected.

Translation of Governor's Vlog in English

In finance, as the British saying goes, there is never a dull moment.

In Maltese we say, something always seems to crop up. Not only have we gone through one major crises after another, but stability is not easy to achieve and sustain. There are always certain incidents that take place and that can have repercussions. Let me be clear, I am here talking about banking stability, and I am not talking about Malta. On the contrary, I want to put people's mind at rest and reassure everyone, and I say this with authority from the Central Bank, that Maltese banks are strongly liquid, enjoy a thus strong cash flow and make profits which is indeed an important factor.

Maltese banks also have a strong capital base. The financial stability report shows that our banks are in a good, healthy state. Healthy here, means robust.

In fact, in this regard, we meet monthly for what is called the Joint Financial Stability Board and we meet with MFSA together with the Ministry or the Minister for Finance and Employment to give an account of the financial stability in the country and the banking stability in particular.

From my end, we cannot ignore incidents that happen abroad. On the 10th of March, as you probably all heard an American Bank – not the largest bank, actually the sixteenth US largest bank - that has one hundred and seventy-three billion US dollar deposits, I think it is gigantic when compared with any bank in our country. Unfortunately, it had a run, this means people panicked and started withdrawing deposits and then the bank had to close down and then it was taken over by the American regulator, the FDIC and declared the bank as insolvent.

The reason was that the bank's assets fell when interest rates went up and assets lost value. When the depositors went to withdraw their money, the Bank did not have enough money so when the bank went to sell its assets, it made big losses.

When interest rates go up the price of the bonds the bank had – which actually were Government bonds - fell. For those, like the Maltese who buy bonds throughout the bond's lifetime (up to maturity), there are no problems however for those who need to exchange the bonds in an emergency such as what happened with this American bank one finds that due to the increase in interest rates, the old bonds with a lower interest rate will not be exchanged at par and one gets less.

For whatever reasons, the Bank failed and created instability not only for the American banks but also gradually affected the Europeans.

What happens is that the weakest of banks are hit most. This incident did not take place in the Eurosystem, meaning in the euro zone, but took place in Switzerland, a huge global bank, Credit Suisse Bank. Which is so big that it has fifty thousand employees around the world and operates in fifty countries.

What we call a global systemic bank. If we were to look at Maltese Banks such as the big banks BOV and HSBC, their roots both in terms of deposits, but even where they invest are spread across the economy in Malta, then nationally they are considered systemic.

This is a globally systemic bank meaning there are many banks around the world that deal with it.

So, if it collapses, it will affect all banks around the globe. Fortunately, regulators both in Switzerland and in America were quick to guarantee the deposits and not only up to one hundred thousand and in the case of America the first two hundred and fifty thousand of the deposits, but guaranteed all the deposits to put people's mind at rest. One need not rush to the Bank to pull out one's money as the American Government in that sense and the Swiss Government in the case of Switzerland guaranteed all deposits. That was important for us in the European Union and in the euro zone, in the Eurosystem, that this action was taken.

However, when it comes to the solutions, these banks will have to be sold. In the case of the Silicon Valley Bank (SVB), which used to lend and invest in technology and inventions which we enjoy using, was bought by First Citizen Bank and in the case of Credit Suisse, it was sold to UBS.

UBS in another big Swiss Bank.

What matters to us though is that the Swiss solution was not an ideal one. The rules in the Eurozone, in the ECB Eurosystem, when there is a bank that collapses as happened in Cyprus for example, what happens is what we call a bail in. In past years, in the case of bank failure the Government stepped in to try and save the bank with taxpayer's money. This no longer took place and we resorted to a new system called bail in.

In this case it is the shareholders that suffer as it is the shareholders that take the risk. The Bank fails, and the shareholder loses the money. The Banks would have been requested, all banks around the world are requested to have what are called 'buffers'; a strong capital base that acts as a cushion. This includes what are known as Tier 1 Bonds which are risky. Tier 1 Bonds come directly after the shareholders. This arrangement we have in the euro zone, in the European Union.

If this situation occurs, the shareholders will be hit first then it is the bond holders which come next to suffer the bank's failure. The latter might not necessarily lose all, but it may be the case that their capital is transformed into shares. The money will not be able to be as liquid as if it were a bond when it comes to be sold. The Swiss unfortunately changed this system. The bond holders lost everything, but shareholders did not lose all the money. This created uncertainty and from our end at the ECB and our President Christine Lagarde strongly emphasised that this situation did not affect us and our regulations we have created and intend to maintain. I would like to say that this instability was not created by a bank in the euro zone, that is to say, that while we do not enjoy witnessing such events, our own system was strengthened after the financial crisis. Malta is part of the Eurosystem family, and its banks are strong and liquid.

Not just having a strong capital base but there have been regulations upon regulations to strengthen this bank which let us put our mind at ease that, not only in our country but also in the system.

But we cannot say that speculation will not continue.

There are many short-term investors who make money from instability, they buy and sell and make profits in millions. In this regard, I can say that such investors enjoy this instability because this is literally their daily bread, making money based on speculation. Unfortunately, the media continues to amplify any incident and then all computers start automatically withdrawing money from the banks.

In the case of SVB, fifty billion US dollars were withdrawn in four hours. In past years, you would have to stand in line to get your money, today the computer will withdraw it by itself and then it will be done faster.

Although the system is not perfect, however the way the Swiss dealt with it does not affect us as we are part of the Eurosystem. In conclusion, I must say that from tomorrow after this programme appears, you will surely read in the papers that instability will not die so soon. Once there are doubts created with regards to specific banks and their possible lack of robustness, and I am here speaking in global terms, on instability.

Even the IMF Managing Director Kristalina Georgieva has just spoken and said that unfortunately instability has been created in the financial world and this does not do good for anyone. What one goes on to conclude from this is that the rules that the central banks make are for the need of stability and this is why sometimes banks complain about the many regulations upon regulations but yes, there is the need for this because we want to safeguard the workers' savings, families' savings and everyone including institutions and they in turn want to reassure themselves that the money they put in banks will be safe.

I'll stop here for today and look forward to the next programme.

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