



**Gikas Hardouvelis**

Professor of Finance &  
Economics  
University of Piraeus  
+30 210 4142323  
ghardouv@unipi.gr

**Ioannis Gkionis**

Senior Economist  
Eurobank Ergasias  
+30 210 3337305  
igkionis@eurobank.gr

**2015: Out of the woods**

**2016: Growth acceleration begins**

**2017: Surpassing the most optimistic forecasts**

**2018: Have we reached the cyclical peak?**

## **Key points**

- **The re-election of President Anastasiades ensures policy continuity for the next five years, yet new challenges appear driven by rising public expectations**
- **In Q4-2017 the economy expanded by 3.9% on an annual basis, bringing the full year performance to 3.9% - the highest during the post-Lehman decade - up from 3.4% in 2016 and 2% in 2015**
- **Most forecasters believe the Cypriot economy is at its cyclical peak to be followed by a slightly lower GDP growth in 2018, yet we think risks to the upside are also present thanks to an investment boom**
- **Rating agencies began a new round of sovereign reviews: S&P maintained unchanged its long-term sovereign rating of BB+ with a positive outlook**
- **Sustainable medium-term growth requires tackling head on the legacy issues of the previous crisis:**
  - **Stabilize the cooperative banks and speed up the reduction of non-performing loans**
  - **Generate political consensus in order to implement the remaining structural reforms in the MoU**
  - **Maintain solid fiscal performance also with an eye to further bring down public debt**

## 1. A review of 2017

The past year was not just a good year for Cyprus. It was a year that progress in most areas was well above expectations. Despite the election year, the country demonstrated serious commitment to fiscal prudence; it continued having uninterrupted access to international markets and at affordable rates, and all this progress was acknowledged by the rating agencies. Economic indicators confirmed the economy embarked on a fast growth recovery track. There was visible improvement in sentiment and in labor market conditions. Even sectors like construction and the real estate showed improvement, thus indicating the recovery is broad-based and affects most of the population. At the same time, there was an intense effort to address the legacies of the banking crisis and the high NPL ratios, with banking sector conditions stabilizing further.

More specifically,

- i. **Output growth reached a new post-Lehman high in 2017.** Real GDP growth expanded by 3.9% YoY in 2017 up from 3.4% YoY 2016, compared to 2.0% YoY in 2015, and after three years of recession and a cumulative drop of 10.1% over 2012-2014. This is among the highest growth rates between Euro Area members (behind Ireland, Malta, Slovenia, Estonia and Latvia) and 1.7 times the average 2017 growth rate in the Euro Area.
- ii. **Investments driven growth:** From a demand point of view, growth was driven primarily by the ongoing rebound in investments for a second consecutive year in a row. Private consumption also had a key contribution itself, being driven by improvement in Economic Sentiment. Net exports had a negative contribution to growth reflecting the double digit rise in imports.
- iii. **Economic activity is highly correlated with sentiment,** which is on an improving trend over the past three years. The Economic Sentiment Index (ESI) improved to 115.7 in December 2017, up from 113.3 in December 2016 and up from 106.7 in December 2015. It has now reached levels very close to those prior to the Lehman Brothers international crisis, in August 2008 (116.1). The ESI readings of the first two months in 2018 stand above that previous record level.
- iv. **The end of deflation:** In 2017 prices entered positive territory on an annual basis for the first time since 2013. The annual average HICP stood at 0.7% YoY in 2017, up from -1.2% YoY in 2016, compared to -1.5% YoY in 2015. The rebound was driven by higher world energy prices on an annual basis and domestic catering and hotel services for most of the outgoing year. Cyprus registered the second lowest inflation in EU-28 ahead of Ireland.

- v. **Labor market conditions improved further in 2017.** The unemployment rate declined for a third consecutive year in a row from 15.0% in 2015 to 13.3% in 2016 and further to 11.1% in 2017. Yet, this level remains the third highest in EU-28 behind Greece and Spain, at par with Croatia. Unemployment was on a steep declining trend in the first three quarters of 2017 but remained virtually unchanged in the last quarter of the year.
- vi. **Fiscal discipline and prudence was maintained in 2017, an election year.** The general government budget on a cash basis ended in a surplus of €361mn or 1.9% of GDP compared to €9.1mn or 0.1% of projected GDP in 2016, up from a balanced position in 2015,<sup>1</sup> -0.2% of GDP in 2014 and -4.9% of GDP in 2013. The public debt declined below the 100% threshold for the first time since 2012, ending at 97.4% of GDP in 2017.
- vii. **Uninterrupted access to the international markets:** Cyprus tapped international markets for a second time after exiting from the Economic Adjustment Programme in March 2016, with a new 7Y-Eurobond, issued at the lowest cost ever achieved in a benchmark bond issuance.
- viii. **Rating agencies acknowledge the improvement of macroeconomic fundamentals:** During the past year, all major rating agencies upgraded the sovereign rating of Cyprus by at least one notch. More importantly, they have all assigned a positive outlook implying a high probability of further upgrades in the near future.
- ix. **Banking sector conditions normalize further**
  - a. Deposits continue to expand for a second consecutive year in 2017
  - b. Yet NPEs remain the elephant in the room despite banks' intense effort to reduce them, and ...
  - c. Cooperative banks show signs of weakness
- x. **Tourism:** the industry registered another year of records in arrivals in 2017 contributing to the GDP growth rebound of the Cypriot economy
- xi. **The property market is showing visible signs of revival**
  - a. Property prices are on the rise, entering positive territory on an annual basis for the first time since 2009
  - b. Construction output rebounds strongly expanding in double digit territory

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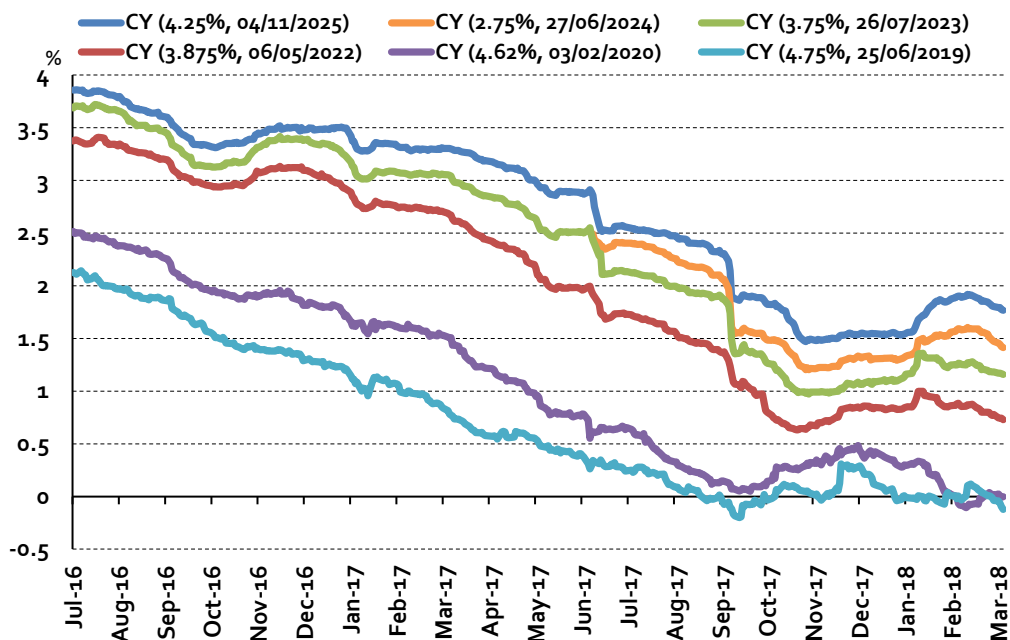
<sup>1</sup> The 2015 deficit excludes the recapitalization costs of the co-operative banks, which would otherwise bring the 2015 deficit to -1.1% of GDP.

## 1.1 Cyprus enjoys uninterrupted access to international markets

On June 21, 2017 Cyprus tapped international markets with a new 7Y-Eurobond for the second time after exiting from the Economic Adjustment Programme in March 2016. In the latest tender, the Public Debt Management Office (PDMO) sold an offered amount of €850mn of 7-year government bonds as part of its €9bn Euro Medium Term Note (EMTN) programme. Citigroup, Goldman Sachs and HSBC were appointed by the Cypriot government as the lead managers. The issue was more than four times over-subscribed with total bids amounting to €3.7bn. The average accepted price was at 99.686 and the corresponding yield at 2.80%. The final yield compares favorably with an initial lower price target that would lead to a yield of 3.0%, and a guidance of 2.9% yield. The issue matures on June 27, 2024 and bears a 2.750% fixed annual coupon.

From a historical point of view, this was the lowest coupon rate the Republic ever achieved in a benchmark bond debt issuance and reflects strong investor confidence towards the country's improving macroeconomic fundamentals. The previous 7-Y offer in July 2016 amounted to €1bn and was priced at 3.8% with a 3.75% coupon. Earlier, and within the first year of its MoU program, Cyprus was already a credible borrower and had made the fastest come-back to international markets among other Euro Area program countries. Cyprus had issued bonds three times in the international markets, once in June 2014 and then again in April 2015 and in October 2015.

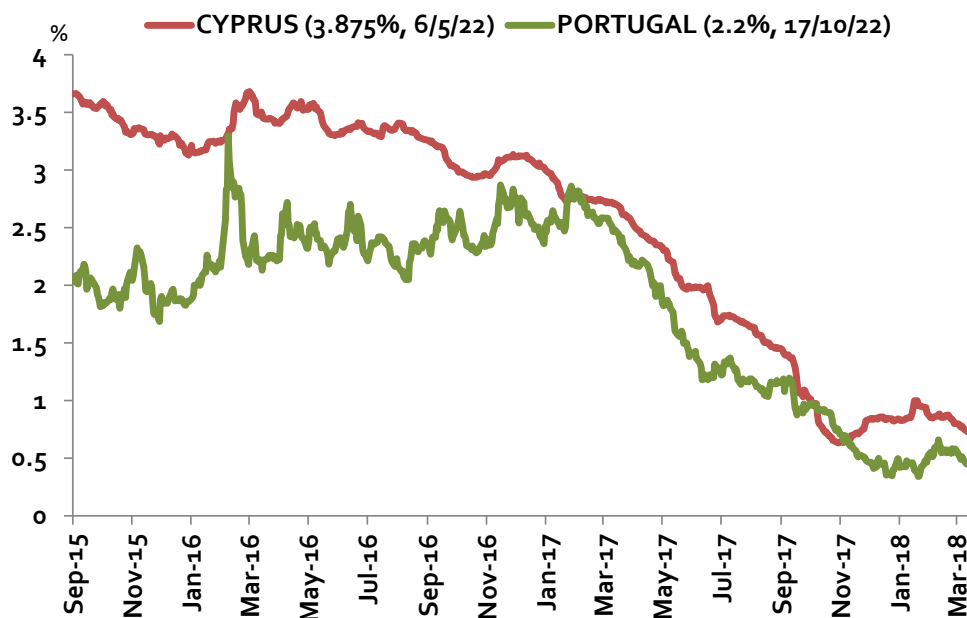
**Figure 1A: Annualized Yields to Maturity of outstanding Cypriot Government Bonds**



Source: Bloomberg, Eurobank Research

Note: The maturity of each bond declines as we move from left to right in the diagram. The first observation is on July 20, 2016 and the last on December 15, 2017. On that date, the longest 04/11/2025 bond had a maturity of 8 years. At the other end, the shortest 25/06/2019 bond had a maturity of 18 months.

**Figure 1B: Annualized Yields to Maturity of Government Bonds maturing in 2022: Cyprus vs. Portugal**



Source: Bloomberg, Eurobank Research

Note: The Cypriot bond matures in May 2022 and the Portuguese about six months later, in October 2022. Thus on December 15, 2017 the Cypriot bond had an approximate maturity of 4.5 years and the Portuguese 5 years.

New bond issuance allows for streamlining of debt repayments in 2019-2020. The proceeds from the latest tender will be used to repay more expensive debt outstanding, including the buyback of three outstanding securities with a combined face value of €1.4bn and higher yields. In this context, the government simultaneously proposed switch offers of 4.75% June 2019 notes, 4.625% February 2020 paper and 6.5% May 2020. The total aggregate amount accepted for the purchase of these securities by the Republic of Cyprus came in at €514.906mn, with the breakdown at €336.558mn, €101.994mn and €76.354mn, respectively.

Despite not participating in ECB's QE, the medium-term Cypriot bond yields are on a declining trend since March 2016 (Figures 1A-1B). Yet since last November Cypriot bond yields trade above those of Portugal despite the improvement in macroeconomic fundamentals.

## 1.2 Public finances surprise to the upside in an election year

- The budget execution has surpassed the most optimistic expectations for an election year. According to the latest data, the general government recorded a surplus of 1.9% of GDP in 2017, up from 0.5% of GDP in 2016. In addition, the general government primary surplus came at 4.5% of GDP in 2017 up from 3% of GDP in 2016. The aforementioned

performance is even more impressive taking into account an additional expenditure of 2% of GDP in the supplementary budget of the Ministry of Finance by the end of the outgoing year.

- On November 6, 2017, the Ministry of Finance repaid part of a 3.0% loan owed to the Central Bank of Cyprus. This early repayment amounts to €614.9mn plus €6.3mn accrued interest and represents a projected reduction of 3.2 ppts in the General Government Debt-to-GDP ratio. As this transaction was funded without any additional debt issuance by the already existing cash surpluses of the Government, it has brought the debt-to-GDP ratio further down to 98.4% of GDP at the end of 2017, compared to 107.8% at the end of 2016. More importantly, the projected cash reserves of the Government at year-end 2017 are estimated to fully cover the financing needs of 2018.
- This year's budget aims at a general government headline surplus of 1.3% of GDP and a primary surplus of 3.8% of GDP. The budget's macroeconomic assumptions are within reach: GDP growth is forecasted at 3%, annual average inflation at 1% and unemployment at 9.5%. Total revenues are budgeted to increase by 4% YoY so as to reach 39.9% of GDP in 2018, down from 39.7% of GDP in 2017. On the other hand, total expenditures are budgeted to increase by 3% YoY so as to reach 38.6% of GDP in 2018, down from 37.8% in 2017. The budget foresees no new loosening initiatives besides those adopted last year. The main loosening measures and their associated fiscal impact (in percent of GDP) adopted in 2016-2017 were: (a) elimination of the tax on immovable property, with full effect from 2017 on (0.5%); (b) expiration in 2017—as envisaged under the programme—of the temporary solidarity levy on wages introduced during the programme period (0.4%); and (iii) hiring additional military personnel in 2016 (0.2%)
- Current fiscal developments are in line with the earlier credible fiscal path. Recall Cyprus performed an impressive fiscal adjustment in 2013-2014, which outperformed initial targets. A general government primary surplus of 2.6% of GDP in cash terms was already achieved in 2014, two years ahead of schedule vs. a primary deficit of -1.8% in 2013 and -2.9% in 2012. Accordingly, the general government deficit declined on a cash basis from -5.8% of GDP in 2012 and -4.9% of GDP in 2013 to only -0.2% of GDP in 2014, and to a balanced position in 2015 (not including the Co-operatives capital injection).

### **1.3 Rating agencies acknowledge the improvement of macroeconomic fundamentals and assign a positive outlook on their individual long-term sovereign rating of Cyprus**

During the past year, all rating agencies acknowledged the improvement of Cyprus macroeconomic fundamentals. All major rating agencies upgraded their long-term sovereign rating of Cyprus, awarding at least one notch in their respective rankings. More importantly, they all have assigned a positive outlook on the long-term sovereign

rating, which implies there is high probability of further upgrades in the near future. The new round of reviews by the rating agencies has already started: S&P (March 17 & September 14), Fitch (April 20 & October 19), Moody's (February 2 & July 27), and DBRS (May 25 & November 2017).

**Standard and Poor's:** On March 17, 2017, S&P upgraded the sovereign rating of Cyprus by one notch (from BB to BB+) with a stable outlook. The decision confirmed the expectations of only 5 out of 11 economists' Stock-Watch poll. On September 15th, in line with expectations, S&P affirmed the long-term sovereign rating of Cyprus at BB+ but at the same time it changed the outlook from stable to positive.

On March 17, 2018, S&P affirmed the long-term sovereign rating of Cyprus at BB+ with a positive outlook. According to S&P, the positive outlook reflects that the agency could raise the ratings on Cyprus over the next 12 months if it observes greater momentum in reducing the country's vulnerabilities, particularly those related to the banking sector and the high indebtedness of the private sector, while economic growth continues to support a general government debt reduction. The agency currently forecasts GDP growth to average 2.8% in 2018-2021, supported by investment activity and service exports, while private consumption decelerates as households increase debt servicing. It is worthwhile pointing out that S&P was the first rating agency to downgrade Cyprus to junk status in January 2012.

**FITCH:** On October 20th, Fitch upgraded the long-term sovereign rating of Cyprus by one notch from BB- to BB with a positive outlook. According to Fitch, the decision reflects primarily the strong improvement in public finances' performance and outlook, coupled with an outperformance in GDP growth forecasts over recent years. Fitch now anticipates GDP growth to average 3.5% in 2017-2018, up from 2.5% a year ago when Cyprus was last upgraded to BB-. On the other hand, Fitch warns that the banking sector's exceptionally weak asset quality remains a key weakness and a material downside risk to the ongoing recovery. Further on, the agency concludes that future developments on NPEs reduction and private sector indebtedness are key factors that may lead to either a positive or a negative rating action in the future.

**MOODYS:** On July 28, 2017, Moody's upgraded the long term sovereign rating of Cyprus by one notch to Ba3 from B1. According to Moody's, the decision reflects two main drivers: First, improvements in economic resilience that have occurred over the past two years, which seem likely to continue in the medium term; second, a consistent fiscal outperformance and a continuing favorable fiscal outlook. The decision to maintain a positive outlook on the new rating of Cyprus reflects Moody's view that improvements in economic resilience and continuing fiscal outperformance are likely to be sustained, together with a reduction in the debt-to-GDP ratio, as well as a fall in the stock of non-performing loans held by the banks.

On November 17<sup>th</sup>, Moody's deferred its scheduled assessment, maintaining its earlier rating of Cyprus at Ba3 with a positive outlook. In its annual report, released on

November 27<sup>th</sup>, Moody's explained that Cyprus's credit profile reflects recent improvements in the country's economic resilience, robust growth momentum and strong fiscal performance. In Moody's view, Cyprus faces credit challenges arising from its small and relatively undiversified economy, as well as high levels of government, banking and household debt. The positive outlook on Cyprus' sovereign rating reflects Moody's view that improvements in economic resilience and fiscal strength are likely to be sustained. More recently, in the regular update on February 7<sup>th</sup>, Moody's left the sovereign credit rating unchanged, at Baa3 with a positive outlook.

**DBRS:** On June 2, 2017, DBRS upgraded the long-term sovereign rating of the Cypriot Republic by two notches (from B to BB low) with a stable outlook (trend). At that time, the DBRS rating decision - an upgrade by two notches - was more aggressive than anticipated. Hence today DBRS is no longer the rating agency that assigns the lowest rating. On December 1<sup>st</sup>, DBRS changed its outlook (they call it "trend") from stable to positive, yet confirmed the rating at BB (Low). According to DBRS' rationale, the change in trend reflects the agency's view that both Cyprus' solid fiscal and economic performances are likely to be maintained, leading to a further decline in the General Government Debt-to-GDP ratio.

DBRS expects the political commitment for prudent fiscal and debt management to be maintained throughout the electoral cycle. According to DBRS, Cyprus benefits from a stable political environment and solid institutions. The government demonstrated strong commitment to the economic adjustment programme, exceeding fiscal targets and making important efforts to obtain legislative support for reforms. This commitment is maintained since exiting the programme in March 2016. Despite delays in the outstanding reforms in Parliament due to the upcoming presidential election, DBRS expects after the election broad continuity on fiscal policy, the debt management strategy and on efforts to address banking sector vulnerabilities.

In sum, following the last round of assessments, there remains a slight divergence of views between the rating agencies on the sovereign rating of Cyprus (Table 3). The distance from government bond investment grade status is one notch for S&P (currently at BB+), two notches for Moody's (currently at Ba3), three notches for Fitch (currently at BB) and also three notches for DBRS (currently at BB Low). The lack of investment grade status prevents Cyprus from qualifying to join ECB's Quantitative Easing (QE) program. Earlier, when Cyprus was still in a Programme, an ECB waiver allowed participation in QE. The Programme and the waiver no longer exist.

**Table 1**  
**Foreign Currency Long Term Sovereign Ratings of Cyprus**

Moody's	S&P	Fitch	DBRS	Rating Description
Aaa	AAA	AAA	AAA	Prime
Aa1	AA+	AA+	AA High	High Grade
Aa2	AA	AA	AA	
Aa3	AA-	AA-	AA Low	
A1	A+	A+	A High	Upper Medium Grade
A2	A	A	A	
A3	A-	A-	A Low	
Baa1	BBB+	BBB+	BBB High	Lower Medium Grade
Baa2	BBB	BBB	BBB	
Baa3	BBB-	BBB-	BBB Low	
Ba1	BB+	BB+	BB High	Non-Investment Grade
Ba2	BB	BB	BB	
Ba3	BB-	BB-	BB Low	
B1	B+	B+	B High	
B2	B	B	B	
B3	B-	B-	B Low	
Caa1	CCC+	CCC+	CCC High	
Caa2	CCC	CCC	CCC	
Caa3	CCC-	CCC-	CCC Low	
Ca	CC	CC	CC High	
			CC	
			CC Low	
	C	C	C High	
			C	
			C Low	
C	SD	DDD	D	Default
C	D	DD		
C	D	D		

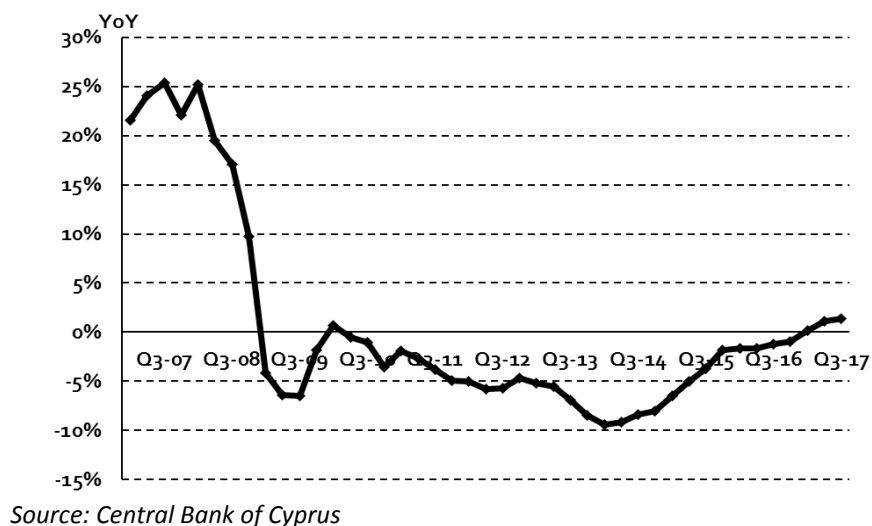
Source: Rating Agencies

(Upgrade within the last review is marked with green color. Affirmation is marked with grey color)

#### 1.4 The property market showed visible signs of revival

- **Construction:** Construction output has been expanding with double digits throughout 2017. On average, construction output was running at 27.7% YoY in 9M-2017, up from 5.1% YoY in 9M-2016 and a negative performance of -4.0% YoY in 9M-2015. The latest building permits release predisposes for a continuation in the construction output rebound. According to CYPSTAT, the total value of building permits issued in FY2017 increased by 48.6% YoY, while the total area of building permits rose by 47.3% YoY. During last year, 4,281 building permits were issued, up from 3,901 in the corresponding period of the previous year.

**Figure 2: RPPI Index: Property prices on the rise**



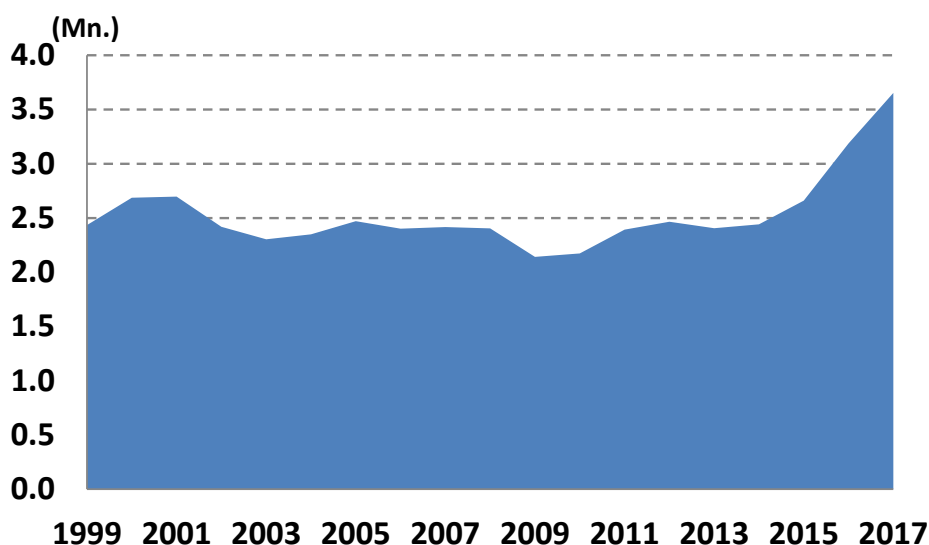
- **Real estate transactions & prices:** The number of real-estate market sale contracts has risen by 24% YoY in FY2017 (from 3,610 to 8,734). The reading of 1,537 in December 2017 only, was a new multi-year monthly high of the last six years (Department of Lands and Surveys). Property prices were on an increasing path in Q3-2017. The Residential Property Price Index (RPPI) recorded its fifth quarterly increase and the third annual increase in Q3-2017 since 2009 (Central Bank of Cyprus). The RPPI Index expanded by +0.4% QoQ/+1.4% YoY in Q3-2017 up from +0.5% QoQ/+1.1% YoY in Q2-2017, +0.3% QoQ/+0.2% YoY in Q1-2017 and +0.3% QoQ/-0.9% YoY in Q4-2016. The House Price Index (HPI), another metric calculated and published by CYPSTAT, is in positive territory since Q4-2016. The HPI came at -0.3% QoQ/+0.6% YoY in Q3-2017 compared to +3.1% QoQ/+3.6% YoY in Q2-2017 up from -3.0% QoQ /+2.4% YoY in Q1-2017 and 0.8% QoQ/+3.3% YoY in Q4-2016.

## 1.5 Cyprus tourism: 2017 was another record year in tourist arrivals

Tourist arrivals increased by +14.6% YoY in 2017 (3,652,073 vs. 3,186,531) reaching a new record in the history of the Republic. The highest increase was recorded in tourist arrivals from Israel (+76.1% YoY, 261,966), Germany (+52.2% YoY, 188,826) and Austria (+33.1% YoY, 40,743). Tourist arrivals from traditional and more sizeable markets such as Russia (+5.5% YoY, 824,494) and UK (+8.3% YoY, 1,253,839) fared relatively well.

In a similar vein, tourism revenues expanded also robustly by +11.7% YoY in January-December 2017 to €2.6bn, up from €2.4bn compared to the same period last year. The expenditure per person for the period of January – December 2017 reached €722.6 compared to €741.7 in the corresponding period of the previous year, recording a decrease of 2.6%. The expenditure per person/per day for the period of January – October 2017 compared to the period of January – October 2016 also recorded a decrease of 2.6% (from €78.1 to €76.1).

**Figure 3: Tourist arrivals 1999-2017**



Source: CYSTAT

## 1.6 Banking sector: Continued normalization, yet major challenges remain

- **Deposits expand on an annual basis for the second time in three years**

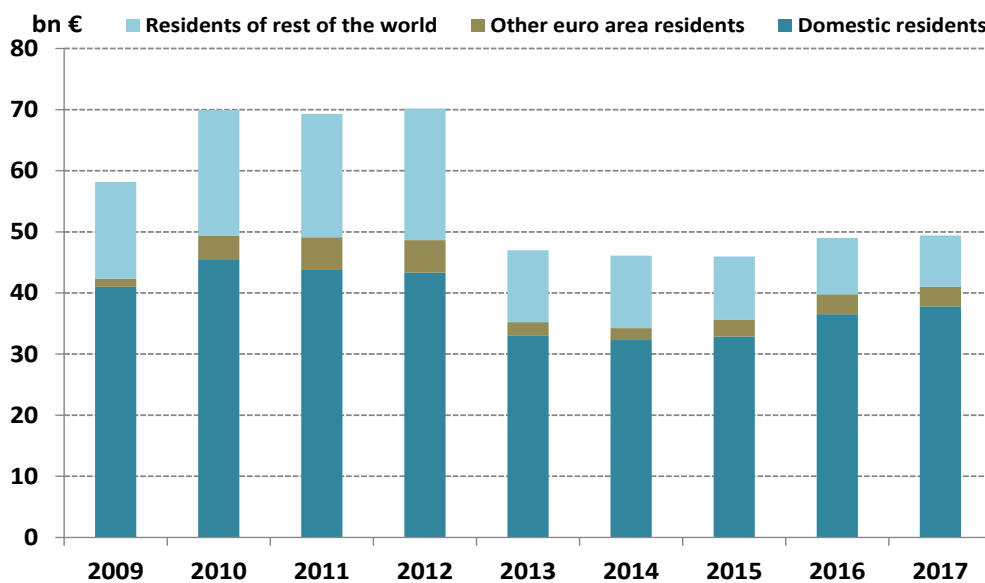
Cypriots seem to have recovered from the wounds of the crisis and have begun to trust their banking system. The stock of banking sector deposits in 2017 recorded the second increase on an annual basis in the last three years. The outstanding amount of deposits increased to €49.4bn at the end of 2017, up from €49.0bn in 2016, €46.0bn in 2015 and €47bn in 2013. Before the March 2013 crisis, at the end of 2012 they had reached €70.2bn. In the last two

years, the increase is driven by the rise of €1.3bn in the resident deposits segment (from €36.5bn in 2015 to €37.8bn in 2017).

The segment of other Euro area residents also increased by €0.5bn in 2017 from €2.7bn to €3.2bn (registering an increase by for a second consecutive year in a row on top of €0.8bn in 2016). Thus it seems all Europeans trust the domestic banking system.

On the other hand, deposits of non-residents from the rest of the world declined further by €1.1bn, down to €9.2bn in 2017 from €10.4 n in 2016. These were primarily the people affected by the bail-in in 2013. Summing up the two non-resident segments, the net change in the deposits of non-residents in the full year 2017 was negative. There was a net decrease of €0.9bn to €11.6bn at end-2017 from €12.5bn at end-2016.

**Figure 4: Domestic banking sector deposits in Cyprus**



Source: Central Bank of Cyprus, Eurobank Research

Note: Data refer to end-of-year levels

- **Despite the intense restructuring effort of the banks and the continuing decline in the stock of bad loans, NPEs remain the elephant in the room**

Despite the intense restructuring efforts of the banks on their portfolios, the ratio of non-performing exposures to total exposures remains at relatively high levels. According to the data released by the Central Bank of Cyprus,<sup>2</sup> the stock of non-performing exposures (NPEs)

<sup>2</sup> <https://www.centralbank.cy/el/announcements/aggregate-cyprus-banking-sector-data-non-performing-facilities-data-with-reference-date-31-august-2017>

declined by €285mn in November relative to October, bringing the stock of NPEs down by 18% in the period between December 2014 to November 2017. The decline in NPEs reflects three main factors: (i) increased repayments, (ii) the migration of successful restructurings to performing loans after the completion of the observance period, and (iii) write-offs and settlements through immovable property exchange.

Total loan exposures (performing plus non-performing) decreased by €2,102mn from €50,436mn in December 2016 to €48,334 in November 2017, which is a larger drop than the decrease in their non-performing component alone. This is due to the on-going deleveraging. Still the ratio of NPEs (non-performing to total exposures) declined a bit, from 45.0% in June 2017 to 43.7% in November 2017, compared to 47.2% in December 2016.

Recall that according to the EBA conservative definition, a restructured NPE is still classified as an NPE for a probation period of at least 12 months, even if it is properly serviced without incurring new arrears. As a result, a large fraction of the restructured loans are still classified as NPEs (€8.6bn out of €12.2bn in November 2017).

Overall, the NPE ratio remains extremely high and, as of September 2017, the ratio in Cyprus is the second highest in the Euro Area behind Greece<sup>3</sup>. It is important to note that the stock of NPEs is even larger when measured relative to the size of the economy. The NPEs as a percentage of GDP stood at 110% in November 2017 down from 130.7% in December 2016, compared to 150.3% in December 2014. This has not escaped the attention of the Central Bank of Cyprus, which noted there is a long road ahead towards the eventual resolution of the NPE problem.

- **The State initiated the privatization process of the Co-operative bank and placed a sizeable deposit in the bank to increase its liquidity**

On March 19th, Cyprus Cooperative Bank (CCB), the second largest bank in terms of assets in the domestic market, provided access to a virtual data room in order to attract private investors to the bank's equity, aiming to reduce the state's participation in its ownership structure. Currently there are two options for potential buyers to either subscribe additional capital, or to buy its assets and liabilities. According to press reports, the Minister of Finance Harris Georgiades said that on the basis of the information he has so far "there is investor interest and rather significant at that", but added it would be best to wait until the end of the process in order to have a full picture.

Meanwhile, on March 27th, Moody's placed on review with direction uncertain CCB's Caa2 long-term, local and foreign currency deposit ratings and downgraded the bank's baseline credit assessment (BCA) and adjusted BCA to ca from caa2. According to Moody's, the two-

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<sup>3</sup> <https://www.eba.europa.eu/documents/10180/1981506/EBA+Dashboard+-+Q3+2017.pdf/a7736ea3-6054-4397-a2b7-d34493dbc168> (page 13)

notch downgrade of the bank's BCA to ca from caa2 reflects the rating agency's view that the bank has a provision shortfall which will have to be filled either through a capital increase, with funds coming from private investors or the government, or through the sale of all or part of the bank's assets and liabilities. The rating agency pointed out that although the CCB currently satisfies all of its regulatory requirements, the bank's capital shortfall stems from weak solvency and limited progress to date in tackling its asset quality issues. The agency added that the stock of non-performing exposures (NPEs) stood at 59% of gross loans as of September 2017, down slightly from its peak of 60% while the bank's provision coverage, the ratio of loan loss reserves to NPEs, at 45%, remained low. Accordingly, it noted that the CCB's capital buffer, with a ratio of tangible common equity to risk weighted assets at 11.3% as of September 2017, is vulnerable owing to its high provision gap.

On April 4th, Cyprus issued a number of 15-20Y government bonds of total nominal value of €2.35bn at market terms with the right for early redemption. Thereafter, the government placed a deposit of €2.5bn in the Cyprus Cooperative Bank (CCB) and took in exchange €7.6bn in collateral for the deposit, which comprises of all non-performing loans from the bank's portfolio, equity participation of the CCB in various private and cooperative societies, and a number of real estate properties in both the southern and the northern parts of Cyprus. The Ministry of Finance (MoF) issued a statement<sup>4</sup> clarifying that the total value of the collateral is approximately €10bn if the real estate collateral of NPLs is taken into account. In addition, it stated that the transaction aimed at securing all depositors – who are primarily Cypriot residents – and fully guaranteeing all deposits from any theoretical risk. Finally, the MoF elaborated that the drastic strengthening of both assets and liabilities in the bank's balance sheet broadens the investment options for the CCB, which, according to the plan, are expected to be finalized during April.

## **2. The re-election of President Anastasiades ensures policy continuity over the next five years; yet the next term entails major new policy challenges**

Nikos Anastasiades was re-elected in the second round of Presidential elections as was broadly anticipated, renewing his mandate for another 5 years. The incumbent President, backed by the ruling right-wing DHSY, received 55.9% of the vote in the run-off election. The runner up, Stavros Mallas, who was backed by left wing AKEL scored 44.01%. The voters' turn-out in the second round stood at 73.97%, a tad above the first round's historical low of 71.9% for Presidential elections standards down from 83.1% in the previous elections in 2013 and 66.7% in the parliamentary elections in 2016.

Earlier on in the first round of Presidential elections held on January 28, no candidate had received the required 51% of the votes. President Anastasiades received 35.5% of

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<sup>4</sup> <https://bit.ly/2q4FdPM>

the popular vote and Mr. Mallas 30.25%, exceeding polls' expectations. Mr. Papadopoulos, whose candidacy received support from a coalition of centrist parties came third, receiving 25.75% of the vote and was disqualified from the second round. Further behind, came the far-right wing ELAM candidate with 5.6% and the Citizens' Alliance leader Mr. Lillikas who garnered 2.17%. The other four independent candidates received less than 1% of the popular vote. Overall, the results of the first round didn't confirm polls' expectations. First, President Anastasiades' margin of victory was not as wide as was implied by the last polls ahead of the elections. Secondly, the battle for the second place was not a close-call as polls had predicted earlier. The first round was a victory for Mr. Mallas against Mr. Papadopoulos with an unexpectedly more comfortable margin than the neck to neck fight implied even by the exit polls on the Election Day.

Recall that the government system in Cyprus is Presidential and thus the President has executive powers. Consequently, the re-election of President Anastasiades gives him a strong mandate to pursue the current government policies and ensures policy continuity. The re-election is an illustration of approval and acknowledgement of his achievements in the first term. From a market point of view, the re-election was well received by market participants. DBRS issued a report in which it expects policy continuity with Cyprus maintaining its solid economic and fiscal performance.

The second term entails challenges of different nature. The previous five year term was defined by the crisis and the effort to escape it. The fear of the crisis united the population and the Parliament behind the President. The new term may be defined by inflated public expectations, created by the earlier successes in escaping the crisis, the quick exit from the economic adjustment program and the gradual return to normality. So the issues of sustaining robust GDP growth rates and, more importantly, growth that can become more inclusive for all citizens are expected to dominate the political agenda.

Yet continued robust growth is not as straightforward as it may appear in the eyes of citizens. First, it requires reinvigorating the unfinished reform agenda, which delayed somewhat during the last year before Presidential elections. There is a number of important pending structural reforms in the areas of privatizations, public and health sectors. Continued reform implementation is an essential step towards increasing Cyprus' growth potential. Second, addressing the still extremely high bad loans' stock (NPEs ratio at 45% in June 2017) is not straightforward either. And if not cured fast enough, NPEs can seriously back-track the economy.

Another major domestic hurdle for the President is political in nature. He will have work harder than in his previous five-year term to achieve concessions from other parties in the parliament in order to pass legislation. Recall in the parliamentary elections held in May 2016, the ruling right-wing party DHSY gained 37.6% of the vote (18 seats), the main opposition left-wing party AKEL gained 25.7% (16 seats), and DHKO gained 14.5% (9 seats). DHKO can no longer be counted as a government partner, which explains at large the lower re-election approval rate of President Anastasiades. Five other smaller

parties, EDEK (6.2%, 3 seats), Citizens' Alliance (6.0%, 3 seats), Solidarity (5.2%, 3 seats), Green Party (4.8%, 2 seats) and far right-wing ELAM (3.7%, 2 seats) were allocated a number of 13 seats compared to only 8 in the previous elections in 2011.

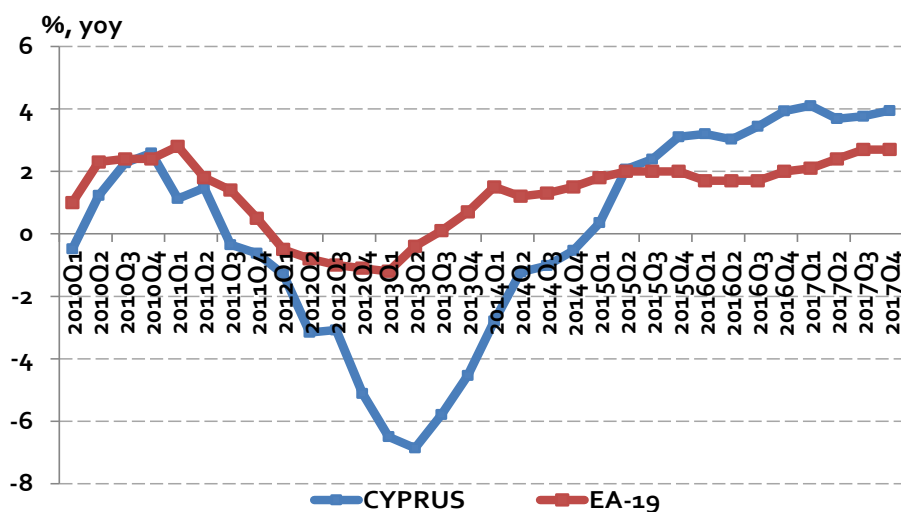
Finally, on top of these domestic economic and political challenges, another important and tough political issue with economic repercussions over the next five years is the revival of the reunification negotiations. The issue has become more complicated lately due to increased international geopolitical risks, apparently prompted by the discovery of natural gas in the area.

### 3. The latest GDP estimate of Q4-2017 surpassed the most optimistic forecasts bringing the latest full year projection to 3.9% in 2017, the highest post-Lehman annual increase

#### 3.1 The overall growth picture

The second and latest estimate of CYSTAT about the seasonally adjusted Q4 GDP reading confirmed the flash estimate of 1.2% QoQ/3.9% YoY. This strong reading compares to 0.8% QoQ/3.8% YoY in Q3-2017, 0.8% QoQ/3.7% YoY in Q2-2017 and 1.1% QoQ/4.1% YoY in Q1-2017, up from 1.0% QoQ/3.9% YoY in Q4-2016. Real GDP growth marked the 11th consecutive positive reading on a both quarterly and annual basis after a previous three-year recession. The GDP growth rate in Q4 is among the highest in EA-19 and EU-28, both on a quarterly and an annual basis (Figure 6 & 7) and above that of EA-19 for an eleventh consecutive quarter in a row (Figure 5).

**Figure 5: GDP growth (YoY) in Cyprus above that in EA19 since Q4-2015**

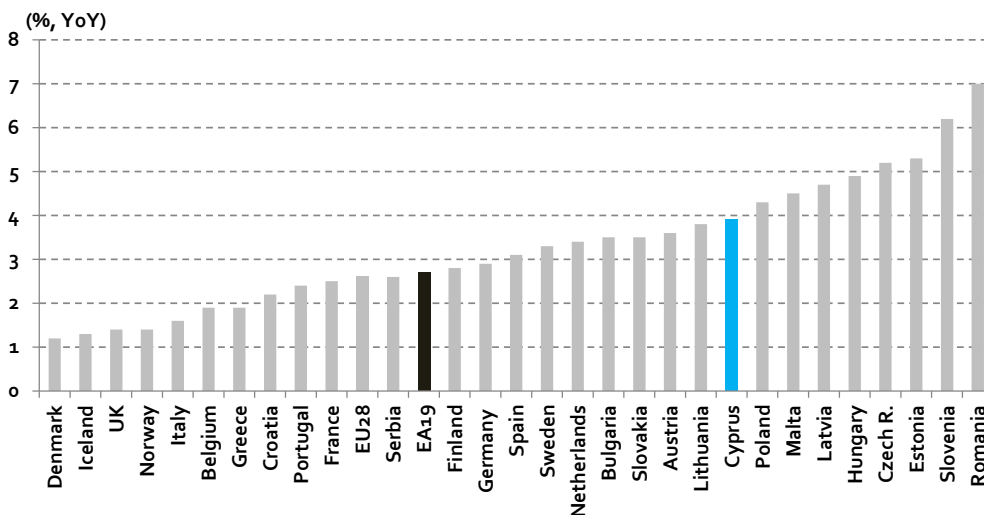


Source: Eurostat, CYSTAT, Eurobank Research

The output performance of the fourth quarter is now the second highest during the post-Lehman period, bringing and surpassing analysts' expectations and international organizations full year initial and revised forecasts. This latest statistic signals that the economy has embarked on a faster growth path than previously envisaged. CYSTAT also revised upward the national accounts of 2016 in both nominal and real terms.<sup>5</sup>

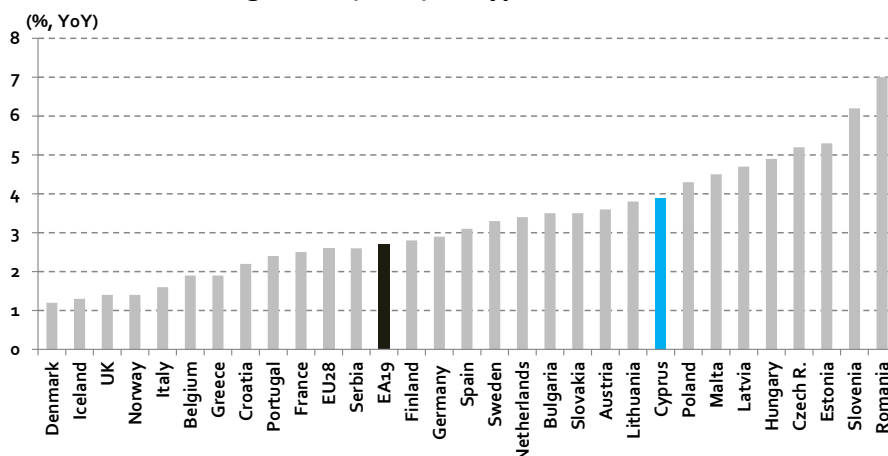
The revision showed that the economy rebounded even faster in 2016 than previously thought: the Statistical Service revised the real GDP growth rate of FY2016 from 3% to 3.4%. As a result, the level of GDP in 2017 in constant prices stood only 1.7% below that in 2008 and 1.6% above that of 2012. Therefore, the level of GDP in 2018 is expected to surpass the level of 2008 under any conservative assumption of real GDP growth scenario.

**Figure 6: Fourth Quarter GDP growth (YoY) in Cyprus among the highest in EA19 & EU28**



Source: Eurostat, CYSTAT, Eurobank Research

**Figure 7: Fourth Quarter GDP growth (QoQ) in Cyprus above EA19 & EU28**



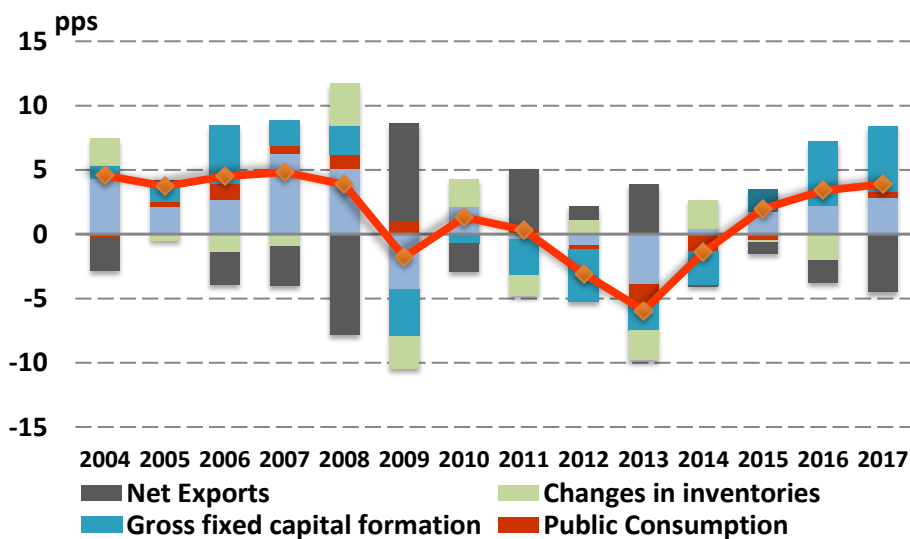
Source: Eurostat, CYSTAT, Eurobank Research

<sup>5</sup><http://www.cystat.gov.cy/mof/cystat/statistics.nsf/All/A875EF7C036ED39BC22581B10031AD93?OpenDocument&sub=1&sel=1&e=&print>

### 3.2 Investments have taken over as the principal driver in FY2017

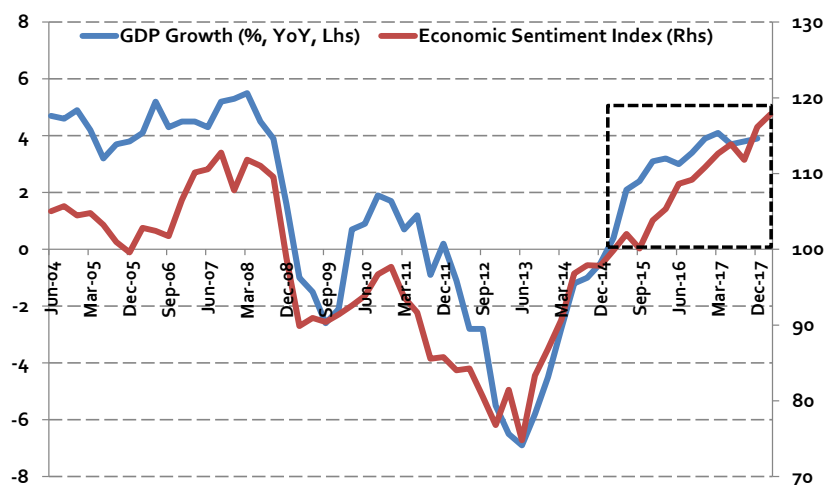
From a demand point of view, the consumption rebound continued throughout 2017, making a total contribution of +3.3ppts to growth. The contribution of final consumption consists of the contribution of public consumption (+0.4ppts in FY2017 vs. -0.1ppts in FY2016), which was positive for the first time since 2011, and that of private consumption (2.9ppts in FY2017 vs. 2.3ppts in FY2016). Private consumption accelerated to 4.2% YoY in 2017, up from 3.3% YoY in 2016. Public consumption expanded by 2.7% YoY in 2017 switching from -0.3% YoY in 2016.

**Figure 8: GDP growth driven by domestic demand in 2015-17**



Source: Eurostat, CYSTAT, Eurobank Research

**Figure 9: Economic Sentiment & Economic Growth in Cyprus**



Source: Eurostat, CYSTAT, Eurobank Research

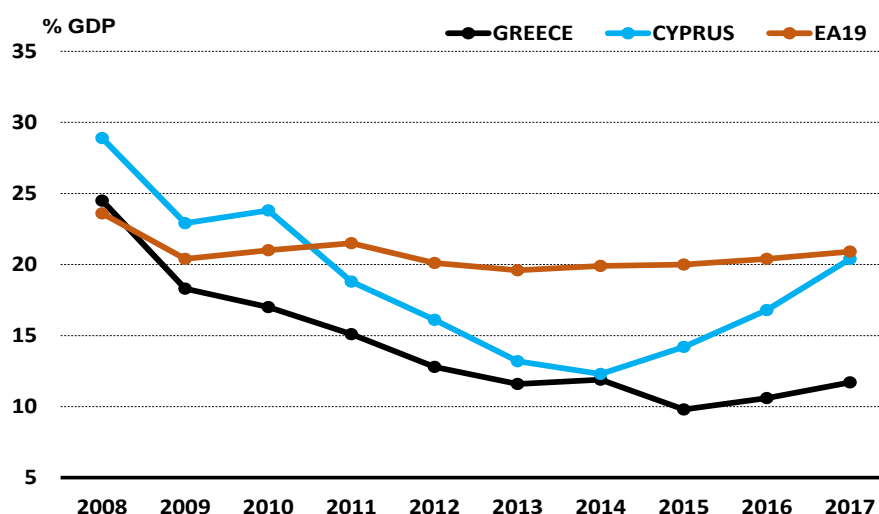
The consumption rebound is underpinned by a number of factors, namely the strong sentiment improvement mirroring the earlier lasting progress within the programme, a

flourishing tourism sector, improved labor market conditions, further property market stabilization, the impact from fiscal relaxation, and the further normalization of banking sector conditions.

As far as other growth components are concerned, higher imports of transportation equipment – likely due to ship & airplane purchases - weighed heavily on the imports side (imports: +10.1% YoY in FY2017 vs. 6.8% YoY in FY2016). The latter in combination with the small deceleration of exports (exports: 3.4% YoY in FY2017 vs. 4.0% YoY in FY2016) resulted in net exports having a negative contribution of -4.5ppts in FY2017 (vs. -1.7 ppts in FY2016).

Finally, investment spending expanded by 27.8% YoY in 2017 on top of 35.0% YoY in 2016, thereby having the most positive contribution to GDP growth (5.1ppts in 2017 vs. 4.9ppts in 2016). Investments received support from all segments (construction 24.9% YoY, machinery and equipment 40.9% YoY, transport equipment 20.2% YoY). As a result, the investments to GDP ratio climbed to 20.4% in 2017 - close to the EA19 average - up from 16.8% in 2016 and only 12.3% in 2014, 13.2% in 2013 and a pre-crisis high at 28.9% in 2008.

**Figure 10: Investments to GDP ratio**



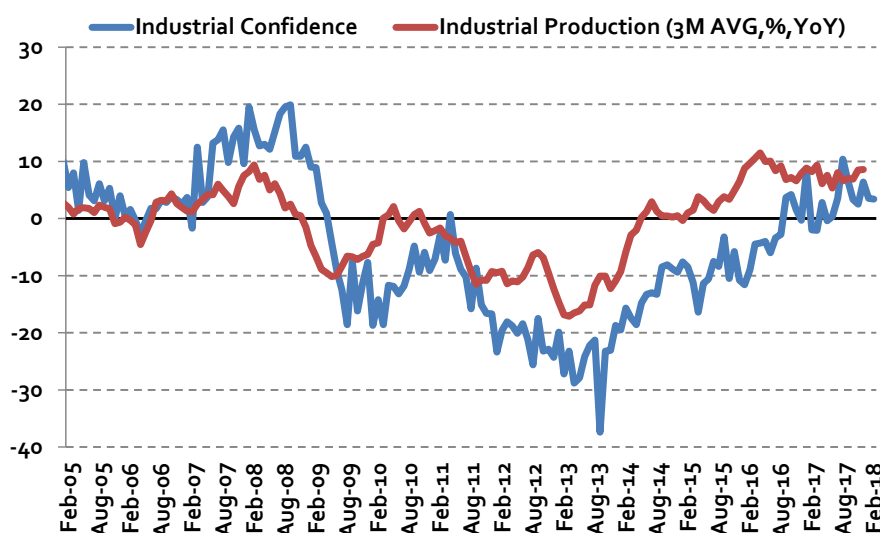
Source: Eurostat, CYSTAT, Eurobank Research

On the supply side, GDP dynamics were shaped by the steady performance of key sectoral pillars of the economy. Output in the combined sectors of “accommodation and food service activities,” expanded by 9.0% YoY in 2017 compared to 10.7% YoY in 2016 and 2.0% YoY in 2015. The performance of these national accounts items reflects largely the contribution of the flourishing tourism industry. Accordingly, the “wholesale and retail trade” sector expanded by 4.8% YoY in 2017 compared to 2.9% YoY in 2016 and 2.4% YoY in 2015.

Manufacturing accelerated to 7.5% YoY in 2017, up from 6.3% YoY in 2016 vs. 5.9% YoY in 2015. In contrast, professional services slowed down to 4% YoY in 2017, compared to 5.8%

YoY in 2016 vs. 4.7% YoY in 2015. Furthermore, construction accelerated its dynamic double-digit recovery, expanding by +25% YoY in 2017 compared to 9% YoY in 2016 and -1.9% YoY in 2015.

**Figure 11: Industrial Production & Confidence in Cyprus**



Source: Eurostat, CYSTAT, Eurobank Research

Financial Services is the exception to the upward momentum: They remained a drag on economic recovery, recording negative growth for a second consecutive year in a row. Nevertheless, the pace of contraction has slowed down in 2017. Financial services contracted by -1.5% YoY in 2017 compared to -2.0% YoY in 2016, down in absolute terms from +7.8% YoY in 2015 (which most probably is owed to the capital injection to the Co-operatives) from -4.6% YoY in 2014, and compared to -6.6% YoY in 2013. The negative contribution to GDP growth by the financial sector in the last couple of years reflects largely the bank restructuring activities (debt to asset swaps), write-offs and the ongoing deleveraging.

## 4. Prospects for 2018

### 4.1 IMF upgraded further its latest GDP growth projection for 2018 to 4-4.25% in late March up from 3.75% previously, yet highlighted downside risks for the medium-term outlook and the need to address legacy issues

On March 30th, IMF published the concluding statement of the second post-program monitoring IMF mission (in co-ordination with the post-program surveillance mission of the European Commission and the ECB, and the early warning system of the ESM) in Cyprus<sup>6</sup>.

<sup>6</sup> <http://www.imf.org/en/News/Articles/2018/03/30/ms033018-cyprus-staff-concluding-statement-of-the-second-post-program-monitoring-mission>

The mission findings praised the sizeable improvement in macroeconomic fundamentals and fiscal metrics and favorable labor market developments. However, the findings emphasized that private sector indebtedness and non-performing loans levels mirroring weak payment discipline remain high. According to IMF, GDP growth is now expected to climb further to 4-4.25% in 2018 compared to the previous mission forecast<sup>7</sup> of 3.75%. GDP growth is going to receive support from mainly foreign-funded, large construction projects, notwithstanding some deceleration in private consumption growth dynamics mirroring better households' compliance to their contractual debt obligations. Over the medium term, GDP growth is projected to ease to 2.5% as construction projects are gradually completed. Finally, the mission findings identified three areas of improvement that would help preserve financial stability, protect the downward trajectory of public debt, and support balanced and durable growth: strengthening payment discipline, avoiding pro-cyclical policies and adopting macro-critical structural reforms.

The above optimistic growth forecasts of the IMF mission were not present in the IMF's most recent flagship publication, the October World Economic Outlook (WEO). In the October WEO, the full year GDP growth in 2017 was projected at 3.4%, up from 2.5% last April (Table 2) and closer to reality. Yet, its GDP growth forecast of the following year was very conservative. GDP growth was expected to ease to 2.6% in 2018, up from 2.3% in the April forecast. In the same publication, unemployment is forecasted to further decline from a projected 11.8% in 2017 to 10.7% in 2018. After staying in negative territory in 2016 at -1.0%, average inflation is projected to average at 0.8% in 2017 and stay subdued at 0.7% in 2018.

**Table 2: IMF World Economic Outlook Forecasts for Cyprus**

IMF WEO	2017		2018	
	April Forecast	October Forecast	April Forecast	October Forecast
<b>GDP growth</b> (%, YoY)	2.5	3.4	2.3	2.6
<b>Consumer Prices</b> (%, average)	1.5	0.8	1.4	0.7
<b>Unemployment</b> (% of Labour Force)	11.3	11.8	10.2	10.7
<b>Current Account Deficit</b> (% of GDP)	-2.5	-3.8	-2.5	-2.7

Source: IMF World Economic Outlook April & October 2017

<sup>7</sup> The concluding statement of the IMF mission to Cyprus in early October, which took place as part of the article IV report consultation and was endorsed by the IMF Board in mid-December, contained a GDP forecast of 3.75% on average in 2017-2018 (<http://www.imf.org/en/News/Articles/2017/12/14/pr17494-imf-executive-board-concludes-2017-article-iv-consultation-with-cyprus>).

**Table 3: EU Commission Forecasts for Cyprus**

IMF WEO	2017		2018	
	Spring Forecast	Autumn/Winter Forecast	Spring Forecast	Autumn/Winter Forecast
<b>GDP growth</b> (%, YoY)	2.5	3.5/3.8	2.3	2.9/3.2
<b>Consumer Prices</b> (%, average)	1.2	1.0/0.7	1.1	1.1/1.2
<b>Unemployment</b> (% of Labour Force)	11.7	11.0	10.6	10.0
<b>Current Account Deficit</b> (% of GDP)	-5.9	-5.4	-6.3	-6.2

Source: EU Commission Autumn (Nov 2017) & Winter (Feb2018) forecasts

## 4.2 Macroeconomic Outlook 2018 - Our view

In our view, solid growth momentum is expected to continue in 2018. The primary question is whether current year's GDP growth rate is going to higher or lower than that of the previous year. There are very good arguments and forecasts for both sides of the spectrum.

On the one hand, GDP growth dynamics are likely to have peaked in 2017 and thus are broadly expected to embark on a decelerating path that will bring them close to more sustainable levels in 2018-2019. Accordingly, there is a consensus among most private and official forecasters that the Cypriot economy is about to or has most probably passed its cyclical peak: a slightly lower GDP growth is the baseline scenario for 2018. The question is how big will the slowdown could be if that happens. Given the progress recorded so far in the previous years, we suspect the slowdown will not be a sharp one.

On the other hand, the opposite view is that GDP growth is about to peak later, perhaps in 2018. Although the economy cannot be running above its potential for many consecutive years, the optimists could argue that there are still a lot of unused resources in the economy and momentum in utilizing them, thus pushing potential GDP dynamics even higher.

Finally, proponents on both sides could argue that the exact growth figure next year is not the primary concern of the day. After all, the growth momentum continues to be favorable and presents an opportunity for Cyprus to address legacy issues and ensure sustainable growth in the medium-term, namely:

- maintain solid fiscal performance in order to bring down public indebtedness
- clean up the problems in cooperative banks and speed up the reduction of the still high NPL ratio, which is the single largest vulnerability of the economy
- push for the remaining structural reforms of the MoU

In view of the above, we anticipate the main trends for this year to be:

- **Sustained private consumption dynamics.** Private consumption is expected to receive support from strong sentiment improvement, reflecting the turn-around of the economy in the past three years, further labour market tightening as unemployment is now projected to reach single-digit levels and the protracted impact of earlier fiscal relaxation, reflecting the abolishment of the property tax and the levy on personal tax.
- **Investments continue expanding.** After skyrocketing by 25.5% YoY on average in 2015-2017, investments are broadly expected to register a lower, yet still relatively strong expansion rate in 2018. We do believe that the investment performance is going to be the most crucial input for the GDP growth dynamics in 2018. Ceteris paribus, under the assumption of double digit rise in investment, it is highly likely that GDP growth could reach or even surpass previous year's levels. Recall that a number of investment projects are already in the pipeline including a number of residential, commercial and mixed developments, including the two marinas in Paralimni and Ayia Napa, a number of luxury hotels and the casino. However, the stabilization of the property market, the further normalization of banking sector conditions plus the incentives provided by the government in the areas of capital investments (citizenship by investment program) could provide a further upside boost to investments. On top, the reinvigoration of the privatization program could be another source of attracting investment particularly from abroad.
- **Exports** are expected to be supported by the flourishing tourism sector and the favourable external environment. Sustained strong revenues from the flourishing tourism industry, mirroring the enrichment of its tourist product and the evolving geopolitical crisis in the neighbouring competing countries.
- **Imports** are expected to surpass exports' growth for two reasons. Firstly, the private consumption acceleration has been accompanied by a concomitant imports recovery. Secondly, in the case of Cyprus, the investment cycle recovery drives up imports of machinery equipment and transportation.

**Factoring in all the above, our baseline scenario is for GDP growth to remain robust at the previous year's levels around 3.9% in 2018.** Risks and challenges to our forecast view do exist. On the upside, they originate from investment. On the downside, risks stem from:

- **High NPEs ratio & High private indebtedness:** Lack of speed in their reduction may undermine confidence in the financial sector and subsequently threaten the investment climate if vulnerabilities are not fully and quickly addressed.
- **Reforms fatigue:** There is a substantial unfinished reform agenda, which the government may be unable to pursue if domestic politics turns sour.
- **Risks to macroeconomic policy:** Backtracking from prudent macroeconomic policies could result from the lack of majority in Parliament.
- **Brexit:** Cyprus is among the EU countries with significant trade ties with UK.
- **Political risks of a geopolitical event** in the Eastern Mediterranean sea.

**Table 3**  
**Time line of Event in Cyprus 2008-2018**

Jan 1st, 2008	Cyprus enters EMU
Feb 17 <sup>th</sup> , 2008	First Round of Presidential Elections in Cyprus
Feb 24 <sup>th</sup> , 2008	Run off round between DISY candidate Kasoulidis and AKEL candidate Christofias. Christofias elected President with 53.36% of the vote
Jan 13 <sup>th</sup> , 2011	Moody's places Cyprus on negative watch for the first time
Jan 17 <sup>th</sup> , 2011	Fitch places Cyprus on negative watch for the first time
Feb 24 <sup>th</sup> , 2011	Moody's downgrade to A2
Mar 30 <sup>th</sup> , 2011	S&P downgrade to A-
May 16 <sup>th</sup> , 2011	Moody's places Cyprus on negative watch again
May 31 <sup>st</sup> , 2011	First Fitch downgrade to A-
July 11 <sup>th</sup> , 2011	Ammunitions explosions in Naval Base Mari. 50% of the power generation capacity is destroyed
July 27 <sup>th</sup> , 2011	Moody's downgrade to Baa1
Oct 27 <sup>th</sup> , 2011	EU leaders summit decision on 50% haircut on Greek public debt
Aug 10 <sup>th</sup> , 2011	Fitch downgrade to BBB
Nov 4 <sup>th</sup> , 2011	Moody's downgrade to Baa3
Dec 16 <sup>th</sup> , 2011	Fitch places Cyprus on negative watch again
Jan 13 <sup>th</sup> , 2012	S&P downgrade to BB+, the first rating agency to rank Cyprus below investment grade
Jan 27 <sup>th</sup> , 2012	Fitch downgrade to BBB-
Mar 13 <sup>th</sup> , 2012	Moody's downgrade to below investment grade (Ba1)
May 3 <sup>th</sup> , 2012	Panicos Dimitriades took office as the new Central Bank governor to replace Orphanides
Jun 13 <sup>th</sup> , 2012	Moody's downgrade to Ba3
Jun 25 <sup>th</sup> , 2012	FITCH downgrade to BB+, below investment grade
Jun 25 <sup>th</sup> , 2012	Cyprus application to ESM
Jul 1 <sup>st</sup> , 2012	Begins Cyprus Presidency of the European Union Council
Jul 25 <sup>th</sup> , 2012	Troika submitted the terms of the bail-out program for Cyprus. The Cypriot government expressed disagreement over those terms and continued negotiations with Troika
Sep27 <sup>th</sup> , 2012	Central Bank of Cyprus commissions PIMCO to carry out the an independent due diligence exercise
Nov16 <sup>th</sup> , 2012	Moody's downgrade to B3
Nov21 <sup>st</sup> , 2012	FITCH downgrade to BB-
Nov22 <sup>nd</sup> , 2012	Statement on the European Commission website on behalf of Troika claims progress towards agreement on key policies of a macroeconomic adjustment program
Nov 30 <sup>th</sup> , 2012	Christofias administration announced agreement reached with Troika on bail-out terms with only the financial sector package pending
Dec 13 <sup>th</sup> , 2012	Euro-Group statement took notice of the progress made at the staff level
Jan 10 <sup>th</sup> , 2013	Moody's downgrade to Caa3
Jan 25 <sup>th</sup> , 2013	FITCH downgrade to B
Feb 17 <sup>th</sup> , 2013	First Round of Presidential Elections in Cyprus
Feb 24 <sup>th</sup> , 2013	Run off round between DISY candidate Anastasiades and AKEL candidate Mallas. Anastasiades elected President with 57.48% of the vote
Feb 28 <sup>th</sup> , 2013	Anastasiades administration is sworn in
Mar 15-16 <sup>th</sup> , 2013	First Euro-Group: agreement to impose a levy on all (insured & uninsured) depositors (6.7% < 100,000 9.9 > 100,000 to collect €5.8bn) in all banks- Capital controls imposed
Mar 19 <sup>th</sup> , 2013	Parliament rejects the bank levy bill, part of the bail-out agreement conditionalities, with a majority of 36 MPs against, 19 MPs abstained, 1 absent
Mar 25 <sup>th</sup> , 2013	Second Euro-Group: agreement to bail-in the uninsured depositors of Laiki and Bank of Cyprus only, resolve Laiki and fold the good bank into Bank of Cyprus. Program money will not be utilized to recapitalize the domestic banking sector except for a provision of 1.5bn for Co-operative sector.
Mar 26 <sup>th</sup> , 2013	Fitch places Cyprus on negative watch again
Apr 2-3 <sup>rd</sup> , 2013	Michalis Sarris resigns from the post of Minister of Finance; Harris Georgiades appointed Minister.
Apr 24 <sup>th</sup> , 2013	ESM Board of Directors grants stability support to Cyprus
May 13 <sup>th</sup> , 2013	ESM disbursement of €2bn in cash
Jun 3 <sup>th</sup> , 2013	FITCH downgrade to B-
Jun 26 <sup>th</sup> , 2013	ESM disbursement of €1bn in cash
Jun 28 <sup>th</sup> , 2013	Interim report of the Independent Commission on the future of the Cypriot banking sector

# QUARTERLY ECONOMIC MONITOR

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Jul 9 <sup>th</sup> -15 <sup>th</sup> , 2013	ESM disbursement of €600mn & €100mn in cash
Jul 30 <sup>th</sup> , 2013	Bank of Cyprus exit from resolution status, recapitalized with 47.5% conversion of uninsured deposits to equity
July 31 <sup>st</sup> , 2013	Staff teams from the Troika visited Nicosia during July 17-31 for the 1st quarterly review
Aug 8 <sup>th</sup> , 2013	Ministry of Finance announcement on a capital restrictions roadmap removal in agreement with official lenders
Sep 5 <sup>th</sup> , 2013	IMF appoints a resident representative in Cyprus
Sep 10 <sup>th</sup> , 2013	General Meeting of the new shareholders in Bank of Cyprus convenes to elect a new Board of Directors
Sep 12 <sup>th</sup> , 2013	Cyprus and Russia agreement on the restructuring of the 2011 bilateral €5bn loan
Sep 16 <sup>th</sup> , 2013	IMF Completes First Review Under EFF Arrangement and Approves €84.7 Million Disbursement
Sep 27 <sup>th</sup> , 2013	ESM disbursement of 1.5bn in floating rate notes
Nov 7 <sup>th</sup> , 2013	Staff teams from the Troika visited Nicosia during October 29-November 7 for the 2nd quarterly review
Dec15 <sup>th</sup> -19 <sup>th</sup> , 2013	ESM disbursement of 350mn & 100mn in cash
Dec20 <sup>th</sup> , 2013	IMF Completes Second Review Under EFF Arrangement for Cyprus and Approves €83.5 mn Disbursement
Feb 11 <sup>th</sup> , 2014	Staff teams from the Troika visited Nicosia during January 29-February 11 for the 3rd quarterly review
Mar10 <sup>th</sup> -11 <sup>th</sup> , 2014	Panicos Dimitriadis resigns from Governor-Chrystalla Georgiadis announced as successor
Mar 28 <sup>th</sup> , 2014	IMF Completes Third Review Under the EFF and Approves €83.3mn Disbursement
Apr4 <sup>th</sup> , 2014	ESM disbursement of 150mn in cash
Apr 25 <sup>th</sup> , 2014	S&P upgrade to B
May 17 <sup>th</sup> , 2014	Staff teams from the Troika visited Nicosia during May 6-17 for the 4th quarterly review
Jun 30 <sup>th</sup> , 2014	IMF Completes Fourth Review Under the EFF for Cyprus and Approves €84mn Disbursement
Jul 25 <sup>th</sup> , 2014	Staff teams from the Troika visited Nicosia during July 15-24 for the 5th quarterly review
Jul 29 <sup>th</sup> , 2014	Successful €1bn rights issue of Bank of Cyprus with the participation of EBRD and Wilbur Ross
Sept 6 <sup>th</sup> , 2014	The Parliament endorsed the foreclosure bills with a majority of 47 votes and 7 against
Oct 24 <sup>th</sup> , 2014	S&P upgrade to B+
Oct 25 <sup>th</sup> , 2014	IMF Executive Board Concludes the 2014 annual Article IV Consultation with Cyprus
Oct 26 <sup>th</sup> , 2014	Announcement of the comprehensive SSM assessment results of four systemic Cyprus banks
Nov 14 <sup>th</sup> , 2014	Moody's downgrade to B3
Feb 6 <sup>th</sup> , 2015	Staff teams from the Troika visited Nicosia during January 27-February 6 for the quarterly review (no staff level agreement was reached given the suspension of an effective application of the foreclosures framework)
Apr 06 <sup>th</sup> , 2015	Full lift of capital controls
Apr 18 <sup>th</sup> , 2015	The Parliament endorsed the insolvency framework bills with a majority of 33 votes and 23 against
Apr 26 <sup>th</sup> , 2015	Election of Mustafa Akinci in the post of Turkish-Cypriot leader
May 20 <sup>th</sup> , 2015	Based on the recent Troika visit in the island staff-level agreement has been reached on policies that could serve as a basis for completion of the pending reviews.
Jun 19 <sup>th</sup> , 2015	IMF Completes Fifth, Sixth & Seventh Reviews of Cyprus' EFF and Approves €278.4 mn Disbursement
Jul 27 <sup>th</sup> , 2015	Staff teams from the Troika visited Nicosia during July 14-24 for the 8 <sup>th</sup> quarterly review
Aug 15 <sup>th</sup> , 2015	CYSTAT announced the flash estimate of Q2-2015 which showed the second positive QoQ growth
Sep8 <sup>th</sup> , 2015	S&P upgrade to BB-
Sep23 <sup>rd</sup> , 2015	IMF Completes Eighth Review of Cyprus' EFF and Approves €126mn Disbursement
Sep 25 <sup>th</sup> , 2015	S&P upgrade to BB-
Oct10 <sup>th</sup> , 2015	ESM disbursement of €500mn in cash
Oct23 <sup>th</sup> , 2015	FITCH upgrade to B+
Nov15 <sup>th</sup> , 2015	Moody's upgrade to B1
Nov16 <sup>th</sup> , 2015	Staff teams from the Troika visited Nicosia during November 3-13 for the 9th quarterly review
Jan27 <sup>th</sup> , 2016	IMF Completes Ninth Review of Cyprus' EFF and Approves €126.3mn Disbursement
Mar7 <sup>th</sup> , 2016	Ministry of Finance asks IMF for the early termination of EFF arrangement & Euro-Group supports Cyprus graduation from the economic adjustment program. The last prior action of the completion of the review (CYTA corporatization) was not satisfied
May22 <sup>nd</sup> , 2016	Parliamentary elections: The ruling right-wing party DHSY gained 37.6% (18 seats), the main opposition left-wing party AKEL gained 25.7% (16 seats), and DHKO gained 14.5% (9 seats)
Sep16 <sup>th</sup> , 2016	S&P upgrade to BB
Sep30 <sup>th</sup> , 2016	Draft Budget Plan submitted to the Parliament
Oct21 <sup>st</sup> , 2016	FITCH upgrade to BB-
Oct 17 <sup>th</sup> , 2016	Draft Budget Plan of 2017 submitted to EU Council of Ministers
Oct 25 <sup>th</sup> , 2016	EU Commission sends a letter to the Cypriot Minister of Finance expressing its concern over a significant fiscal relaxation of the fiscal stance next year
Oct 27 <sup>th</sup> , 2016	The Cypriot Minister of Finance replies to the EU Commission rebutting its arguments on fiscal relaxation and the calculation of the output gap in the case of Cyprus

Nov 11 <sup>th</sup> , 2016	Moody's affirmed sovereign long-term rating at B1 but changed the outlook from stable to positive
Nov 15 <sup>th</sup> , 2016	EU Commission adopts an official opinion on the Cypriot budget of 2017 assessing that it is at risk of non-compliance with the requirements of the SGP
Dec 6 <sup>th</sup> , 2016	Eurogroup agrees with the EU Commission assessment and welcomes the commitments of Cyprus, in such circumstances, to implement the measures necessary to ensure that the 2017 budget will be compliant with the rules of the preventive arm of the SGP
Dec 7 <sup>th</sup> , 2016	Parliament approved the Budget of 2017 with 28 votes for and 25 against
Dec 18 <sup>th</sup> , 2016	Municipal elections
Mar 17, 2017	S&P affirmed the long-term sovereign rating of Cyprus at BB+ with a positive outlook
June 2 <sup>nd</sup> , 2017	DBRS upgraded the long-term sovereign rating of Cyprus Republic by two notches (from B to BB low) with a stable outlook (trend)
June 11 <sup>th</sup> , 2017	Cyprus tapped international markets with a new 7Y-Eurobond for the second time after exiting the economic adjustment program at a yield of 2.8%
July 28 <sup>th</sup> , 2017	Moody's upgraded the long-term sovereign rating of Cyprus by one notch from B1 to Ba3 with a positive outlook
Sep 15 <sup>th</sup> , 2017	S&P affirmed the long-term sovereign rating of Cyprus at BB+ but at the same time it changed the outlook from stable to positive
Oct 20 <sup>th</sup> , 2017	Fitch upgraded the long-term sovereign rating of Cyprus by one notch from BB- to BB with a positive outlook
Nov 6 <sup>th</sup> , 2017	The Ministry of Finance repaid part of a loan held by the Central Bank of Cyprus bringing the public debt to GDP ratio down to 98.4%-below 100% for the first time since 2012- in 2017
Dec 13 <sup>th</sup> , 2017	Parliament approved the Budget of 2017 with 30 votes for and 25 against
Dec 14 <sup>th</sup> , 2017	IMF Executive Board Concludes 2017 Article IV Consultation with Cyprus
Jan 28 <sup>th</sup> , 2018	First round of Presidential elections: the incumbent President Anastasiades backed by DHSY received 35.5%, Mr. Mallas backed by AKEL received 30.25%, and Mr. Papadopoulos supported by a coalition of centrist parties received 25.75%. Further behind came the ELAM candidate with 5.6% and the Citizen's Alliance leader Mr. Lillikas with 5.6% of the vote. The voter's turn out stood at 71.9% a historic low for Presidential elections
Feb 4 <sup>th</sup> , 2018	Second round of Presidential elections: Nikos Anastasiades received 55.9% of the vote and was re-elected President for another five year term. The runner up Stavros Mallas received 44.01%. The voter's turn-out in the second round stood at 73.97%
Feb 7 <sup>th</sup> , 2018	Moody's affirmed the long-term sovereign rating of Cyprus at Ba3 with a positive outlook
Feb 12 <sup>th</sup> , 2018	Italian oil & gas company ENI announced a "promising" gas discovery in Cyprus' Block 6, noting that the discovery confirms the extension of the "Zohr like" play in Cyprus' Exclusive Economic Zone (EEZ).
Mar 16 <sup>th</sup> , 2018	S&P affirmed the long-term sovereign rating of Cyprus at BB+ with a positive outlook
Mar 16 <sup>th</sup> , 2018	CYSTAT announced the provisional national accounts data for FY2017. Real GDP growth recorded the highest reading in the post-Lehman Brothers era
Mar 19 <sup>th</sup> , 2018	The Co-operative Central Bank announced that it resumes the process to attract private investors in shareholder's capital and reduce state ownership. The bids process has two options, either for the fully licensed bank entity, or all or part of CCB's assets and liabilities
Mar 23 <sup>th</sup> , 2018	Statement by the staff of the European Commission and the ECB following the fourth post-programme surveillance (PPS) mission to Cyprus
April 4 <sup>th</sup> , 2018	Cyprus issued a number of 15-20Y government bonds of total nominal value of €2.35bn at market terms with the right for early redemption. Thereafter, the government placed a deposit of €2.5bn in the Cyprus Cooperative Bank (CCB) and took in exchange €7.6bn in collateral for the deposit, which comprises of all non-performing loans from the bank's portfolio, equity participation of the CCB in various private and cooperative societies, and a number of real estate properties in both the southern and the northern parts of Cyprus

## Eurobank Cyprus Research

Economic Indicators	Description	Source	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
<b>National Accounts</b>															
Population	Number	Eurostat	722,893	733,067	744,013	757,916	776,333	796,930	819,140	839,751	862,011	865,878	858,000	847,008	848,319
GDP (%YoY)	Constant Prices	Eurostat	4.6	3.7	4.5	4.8	3.9	-1.8	1.3	0.3	-3.1	-5.9	-1.4	2.0	3.0
Households and NPISHs Final Consumption Expenditure (YoY%)	Constant Prices	Eurostat	7.2	3.5	4.4	10.2	7.9	-6.4	3.3	-0.7	-1.3	-5.9	0.7	2.6	3.3
General Government Final Consumption Expenditure (YoY%)	Constant Prices	Eurostat	1.2	2.8	7.0	3.3	5.7	6.4	1.2	2.1	-1.8	-8.1	-7.2	-2.8	-0.4
Gross Fixed Capital Formation (YoY%)	Constant Prices	Eurostat	4.7	6.9	21.0	7.8	8.8	-13.6	-2.6	-12.1	-20.5	-12.9	-17.5	13.6	35.0
Exports of Goods and Services (YoY%)	Constant Prices	Eurostat	2.3	2.1	1.3	5.3	-0.7	-4.1	4.5	5.6	-2.7	2.1	4.2	6.3	3.9
Imports of Goods and Services (YoY%)	Constant Prices	Eurostat	6.9	1.6	5.7	10.5	12.5	-15.0	8.0	-3.0	-4.4	-4.8	4.6	8.1	6.6
GDP	Current Prices, SA ,mil	Cyprus Statistical Service	13856.3	14822.3	15999.9	17511.6	19006.0	18673.5	19299.5	19731.1	19489.7	18140.5	17605.9	17742.0	18122.5
GDP (%YoY)	Current Prices, SA ,mil	Cyprus Statistical Service	7.9	7.0	8.0	9.5	8.5	-1.8	3.4	2.2	-1.2	-6.9	-3.0	0.8	2.1
<b>Labour Market</b>															
Unemployment Rate	% active population	Eurostat	4.6	5.3	4.6	3.9	3.7	5.4	6.3	7.9	11.9	15.9	16.1	15.0	13.0
Labor Productivity	Real, Per employee, % Change	Eurostat	0.6	0.1	2.6	0.4	0.3	-1.8	0.8	0.3	0.0	0.0	0.2	-0.2	0.1
Unit Labor Costs	Index, 2010=100	Eurostat	82.3	87.7	89.1	90.4	93.0	100.2	100.0	101.8	103.3	97.7	93.8	92.9	92.3
Unit Labour Cost Growth Total Economy	YoY%	Eurostat	1.6	6.5	1.6	1.5	2.9	7.7	-0.2	1.8	1.5	-5.4	-4.0	-0.9	-0.7
<b>Short-term business statistics</b>															
Economic Sentiment Index (ESI)	EoP, SA	EU Commission	106.3	99.8	108.1	108.4	97	93.8	97.1	85.7	76.6	89.6	102.7	106.7	113.3
Industry	EoP, SA	EU Commission	-36.4	-26.2	-31.8	-40.8	-39.2	-40.5	-46.7	-61.3	-43.9	-20.2	-10.0	-4.0	-0.4
Construction	EoP, SA	EU Commission	-4.4	-32.7	2.7	-7.9	-27.5	-38.8	-44	-51.5	-56.5	-54.5	-49.8	-30.3	-27.4
Retail trade	EoP, SA	EU Commission	3.3	5.2	0.7	11.2	-12.8	-22.5	-22.6	-29.0	-31.8	-19.1	-10.6	-1.6	8.5
European Commission Services Confidence Indicator Cyprus	EoP, SA	EU Commission	14.4	6.1	15	8.7	1.8	-3.6	3.6	-25.2	-40.7	-24.2	11.4	8.2	28.4
Industrial Production General Index	NSA	Cyprus Statistical Service	103.2	102.7	103.5	111.0	109.9	102.8	100.3	92.5	75.2	69.9	72.8	77.3	84.5
Industrial Production General (%YoY)	NSA	Cyprus Statistical Service	3.7	-0.5	0.8	7.2	-1.0	-6.5	-2.4	-7.8	-18.7	-7.0	-9.6	7.8	8.7
European Commission Capacity Utilization Cyprus SA	SA	Cyprus Statistical Service	70.0	72.6	66.8	71.3	69.4	63.0	63.9	58.1	53.7	50.8	54.5	61.1	59.6
<b>Housing and Real Estate</b>															
Building Permits	Number	Cyprus Statistical Service	8252.0	9098.0	9794.0	9521.0	8896.0	8950.0	8777.0	7506.0	7172.0	5341.0	4933.0	5014.0	5354.0
Value of permits	mil €	Cyprus Statistical Service	1994.6	2288.9	2473.4	2782.3	2904.6	2815.8	2639.5	2065.1	1632.3	1141.0	859.5	1071.4	1157.6
Area of permits	(Thousand Sqm)	Cyprus Statistical Service	3015.7	3417.0	3507.5	3612.8	3689.1	3136.5	2917.9	2253.0	1499.9	1044.8	784.9	881.1	1047.1
Dwelling Units	Number	Cyprus Statistical Service	15743.0	18770.0	18915.0	20486.0	20082.0	16688.0	14312.0	8839.0	5879.0	4141.0	2855.0	3197.0	2348.0
<b>Personal/Household Sector</b>															
Credit for Consumption	mil €	ECB MFIs Statistics		2,577	2,848	3,118	4,261	4,770	3,390	3,371	3,341	3,039	2,794	2,792	2,583
Lending for House Purchase	mil €	ECB MFIs Statistics		4,140	5,450	6,989	8,584	10,492	12,033	12,658	12,772	11,943	11,747	11,735	11,587
Other Lending Cyprus	mil €	ECB MFIs Statistics		5,645	5,676	6,111	6,366	5,600	7,381	7,855	8,025	7,558	7,433	7,099	6,736
Total MFI Loans to Non-MFIs Domestic Residents	Monetary & Financial Statistics	Central Bank of Cyprus		25,005	27,511	33,995	43,452	45,681	49,403	52,870	53,936	50,082	49,583	51,201	45,310
Gross Household Saving Rate	% of Gross Disposable Income	Eurostat	7.9	10.7	10.8	5.9	4.8	8.9	6.7	6.4	3.6	-3.3	-7.9	-5.7	N/A
<b>International Trade &amp; Balance of payments</b>															
Current account balance (%GDP)	BMP6	Eurostat					-15.5	-7.7	-11.3	-4.1	-6.0	-4.9	-4.3	-2.9	-5.3
Current Account, Goods & Services Net Balance (%GDP)	BMP6	Eurostat					-12.8	-5.4	-7.3	-2.9	-1.5	1.8	2.1	0.3	0.0
Current Account, Primary Income Net Balance (%GDP)	BMP6	Eurostat					-2.5	-1.3	-3	0	-3	-4.7	-3.6	-0.3	-2.7
Current Account, Secondary Income Net Balance (%GDP)	BMP6	Eurostat					-0.3	-1.0	-1.0	-1.1	-1.4	-2.1	-2.8	-2.9	-2.6
Imports of Goods (%GDP)	BMP6	Eurostat					42.2	34.7	36.8	35.5	33.7	31.2	32	32	35.1
Exports of Goods (%GDP)	BMP6	Eurostat					12.0	13.1	13.9	15.3	15.6	15.0	16.0	14.1	13.6
Imports of Services (%GDP)	BMP6	Eurostat					20.7	19.4	20.7	20.4	21.3	25.7	28.1	28.9	28.0
Exports of Services (%GDP)	BMP6	Eurostat					38.1	35.7	36.3	37.6	37.9	43.7	46.2	47.2	49.5
Financial Account (%GDP)	BMP6	Eurostat					-18.5	-8.4	-8.6	-1.2	-2.1	-1.9	-7.1	2.0	-5.9
<b>Government Finance &amp; Debt</b>															
General Government Deficit (-) or Surplus (+) (% GDP)	including Coops banks' recap	Cyprus Statistical Service	-3.7	-2.2	-1.0	3.2	0.9	-5.4	-4.7	-5.7	-5.6	-5.1	-8.8	-1.2	0.4
General Government Debt EDP Procedure (% GDP)		Cyprus Statistical Service	64.1	62.8	58.7	53.5	44.7	53.4	55.8	65.2	79.3	102.2	107.1	107.5	107.8
<b>Prices</b>															
CPI (%YoY)	Annual Average	Cyprus Statistical Service	2.3	2.6	2.5	2.4	4.7	0.3	2.4	3.3	2.4	-0.4	-1.4	-2.1	-1.4
Cyprus HICP All Items (% YoY)	Annual Average	Eurostat	1.9	2.0	2.2	2.2	4.4	0.2	2.6	3.5	3.1	0.4	-0.3	-1.5	-1.2
<b>Tourism</b>															
Tourist & Excursionist Arrivals	Number	Cyprus Statistical Service	2,349,007	2,470,057	2,400,919	2,416,075	2,403,744	2,141,187	2,172,993	2,392,223	2,464,903	2,405,387	2,441,231	2,659,400	3,186,531
Revenue From Tourism	mil €	Cyprus Statistical Service	1,678,419	1,718,302	1,755,252	1,858,106	1,792,787	1,493,246	1,549,801	1,749,306	1,927,600	2,082,400	2,023,400	2,112,100	2,363,400
<b>Market Indicators</b>															
10Y Gov Bond Yield Rate	% EMU criterion series	Eurostat	6.3	4.1	4.3	4.6	4.6	4.6	4.6	7.0	7.0	6.0	6.0	3.9	3.6
Cyprus Stock Exchange Index	EoP, Composite Index		1012.27	1704.76	3900.39	4820.72	1101.42	1597.23	1055.21	295.94	114.86	103.31	85.70	67.75	66.40