

## MACROECONOMIC MONITOR OF CYPRUS

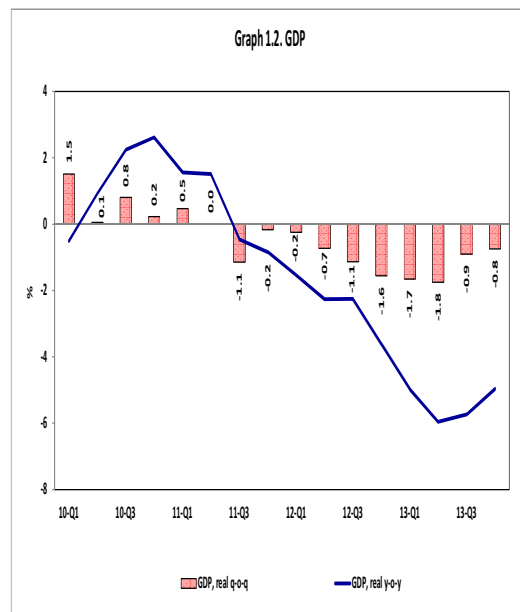
*Updated on 22 April 2014*

- In 2013, GDP contracted by -5.4% (see graphs 1.1-1.2). The contraction was mainly due to the subdued performance of the secondary sector (construction, manufacturing). From the expenditure side, the contraction was more pronounced in investments of construction, while net exports made a positive contribution (see graphs 3.1-3.4 and 6.1-6.2).
- GDP contraction by -5.4% in 2013, compares favourably with initial market expectations following the deposit haircut in March 2013. However, the business operating environment remains constraint, given that lending to non-financial corporations is subdued and interest rates are still relatively high. We maintain our view that growth in 2014 will remain negative, around -4.5%, and we assume rebound in 2015 with a gradual restoration of lending at affordable rates.
- Developments are currently driven, mainly by lower domestic demand (see graphs 2.1-2.4) that compares favourably to the anticipated lower levels expected originally.
- The economic sentiment indicator by CypERC presents a less negative picture, as it increased by 1.3 points in March 2014 compared to February 2014, although still remaining at negative levels (see graph 1.3). Expectations in services and construction showed an improvement albeit from low levels.
- Exports of goods decreased by 3.7% in January-February 2014 compared to the same period in 2013. Exports of agricultural products increased by 19.1% in January 2014 compared to January 2013.
- In January-March 2014 tourist arrivals decreased by 7.8% compared to the same period in 2013 (see graph 6.3). The decline was mainly due to the fact that the Catholic Easter in 2014 was in April while in 2013 it was in March. A decrease of 14.5% was recorded in arrivals from the United Kingdom and 12.9% decrease in arrivals from Greece, while an increase of 8.5% was recorded in arrivals from Russia. Revenues from tourism in January 2014 decreased by 0.5% compared to January 2013.
- Employment is also affected by the slowdown, showing an expected adjustment to the conditions of lower economic growth (see graphs 4.1 and 4.4). Employment in persons (FTE) decreased by 5.4% in 2013 compared to 2012. The decrease was more pronounced in construction, trade and manufacturing.
- Labour market developments exhibited flexibility and are adjusting accordingly to the new environment. This led to an increase in profitability of business and at the same time this allowed business to offer goods and services at reduced prices.
- Labour Force Survey (LFS) unemployment, in monthly seasonally adjusted figures, increased significantly from 14.7% in February 2013 to 16.7% in February 2014, reflecting the effect of a protracted slowdown in economic activity (see graphs 4.2-4.3). The category mostly affected is youth. Particularly worrying is also the rapid increase in long-term unemployment. The level of unemployment is expected to rise to about 18.2% in 2014 compared to a forecast of 19.2% of the 3<sup>rd</sup> review.

- Compensation per employee in 2013 declined by 5.9% compared to 2012, contributing to a decline of nominal unit labour cost and improving cost competitiveness (see graphs 5.3-5.5). The observed wage adjustment is expected to help containing the upward pressure on unemployment.
- Inflation as measured by the HICP, decreased at a rate of -0.9% in March 2014 compared to -1.3% in February 2014 and for 2014 so far it stands at -1.2% (see graph 5.1). Core HICP inflation decreased at a rate of -0.3% in January-March 2014 (see graph 5.2). All subcategories of HICP presented a decrease except for alcoholic beverages and tobacco, clothing and footwear, transport, communication and restaurants and hotels which presented an increase.
- The current account balance in 2013 recorded a deficit of €310 mn (1.9 of GDP) compared with a deficit of €1.217 mn (6.9% of GDP) in 2012 (see graph 6.4). This development was mainly due to the improvement in the goods account.
- The income account recorded a deficit of €451,9 mn in 2013 compared with a deficit of €456 mn in 2012 (see graph 6.4).
- The international investment position of Cyprus (see graph 6.5) recorded a small improvement in 2013, reaching -€14.138,3 mn compared with -€14.594,1 mn in 2012, thus remaining in a net liability position (Cyprus' liabilities exceed the respective assets).
- In January-March 2014, the budget balance recorded a deficit of €31,6 mn (0.2% of GDP) compared to a deficit of €5,3 mn (0.03% of GDP) in January-March 2013.
- Monetary Financial Institutions (MFI) loans to domestic residents (private sector), declined with an annual rate of 7% in February 2014, affecting both households and enterprises (see graphs 8.2-8.4). This is reflecting low demand and tight lending conditions (see graphs 8.7-8.8).
- Deposits of domestic residents held with MFIs (private sector) exhibited a substantial fall presenting an annual decline of 15% in February 2014, reflecting the negative climate of confidence (see graph 8.1).
- Overall the lending and deposit interest rates in Cyprus have declined compared to last year levels and the levels prevailing during the period prior to the bail-in of creditors. However, the decline in deposit rates is much bigger than the decline in lending rates (see graph 8.5). In February 2014, deposit interest rates for maturity up to 1 year and deposits up to 3 months remained broadly the same with the previous month. The lending interest rates to households for house purchase exhibited a decrease, whereas the rate for other loans up to €1 mn for businesses exhibited a small increase. The rate for bank overdrafts to non-financial corporations exhibited a significant decrease. A significant deviation of the Cypriot interest rates, compared to the euro area average is still observed.
- The CBC's residential property price index declined by 8.7% in the 4<sup>th</sup> quarter of 2013 on an annual basis. Cumulative from the 1<sup>st</sup> quarter of 2008 it has declined by around 22% (see graph 7.1), revealing a modest adjustment to the conditions of lower domestic and foreign demand.
- According to the Department of Lands and Surveys, new sale contracts were 6.4% lower and property transfers were 14.5% higher in January-March 2014 compared to the same period in 2013 (see graph 7.3). MFI loans to domestic residents for housing declined with an annual rate of 5.4% in February 2014 (see graph 7.2).

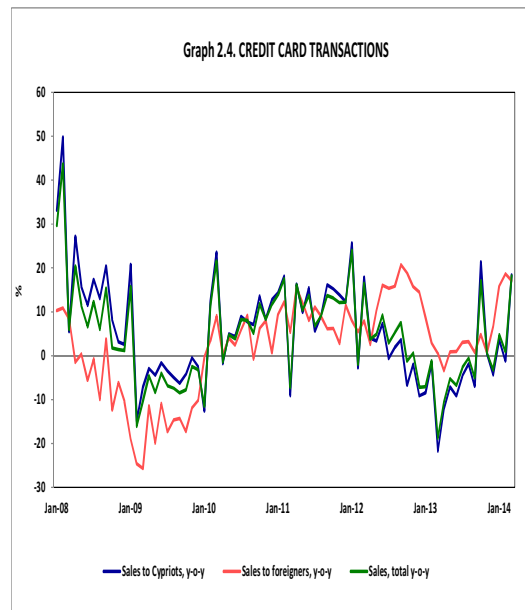
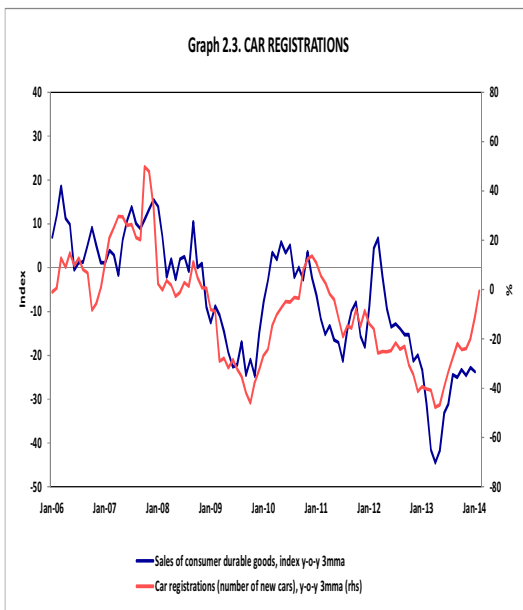
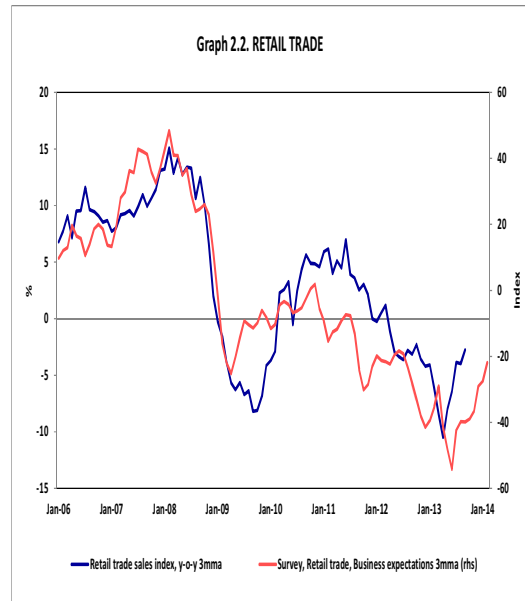
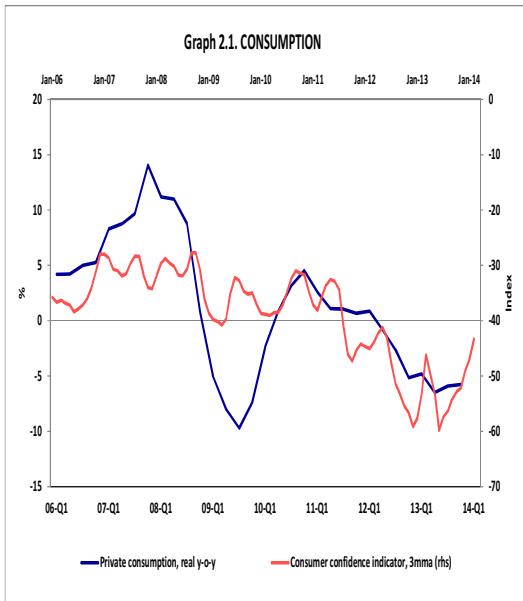
- The Cyprus Government bond spread compared to the German Government bond, decreased further in April 2014 compared to March 2014 to around 350 basis points above the German bond on 22/04/2014 (see graph 8.6, yields refer to the bonds maturing in 2020).

## 1. OUTPUT



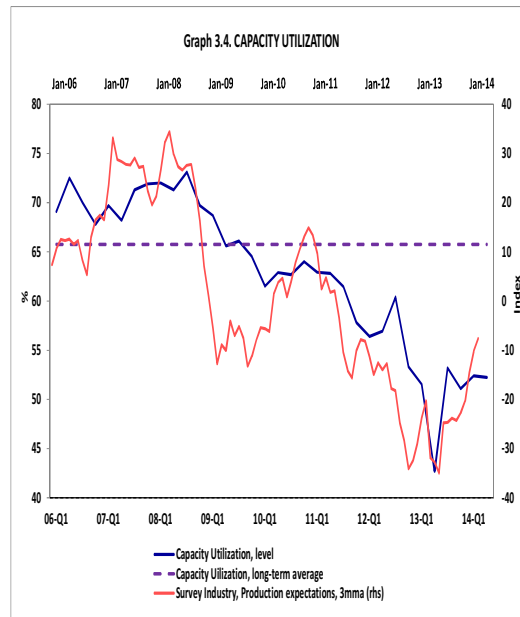
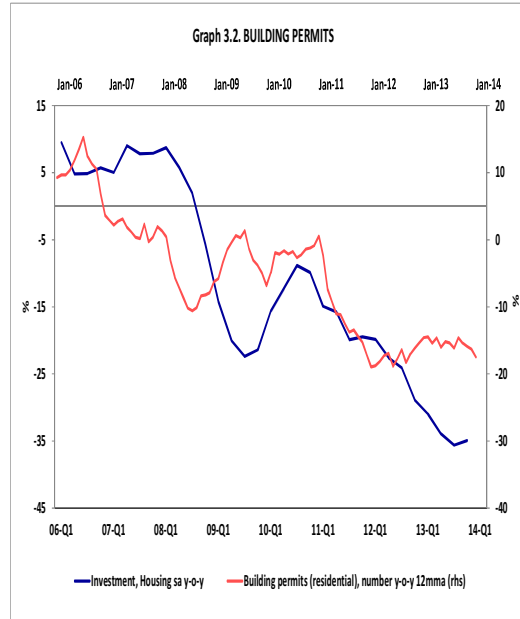
Sources: Eurostat, DG ECFIN, Cystat

## 2. CONSUMPTION



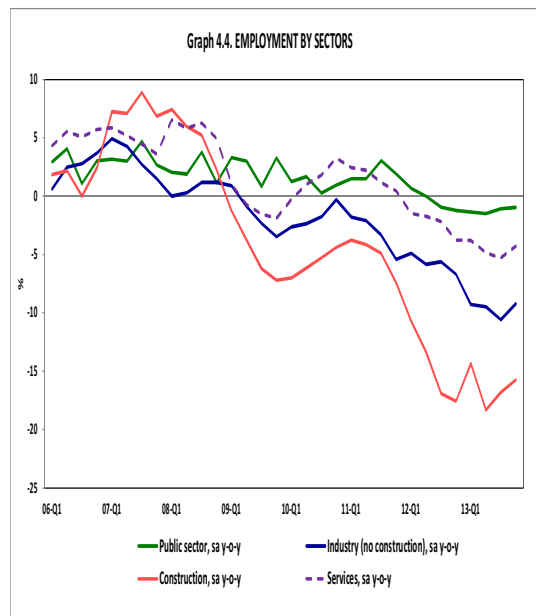
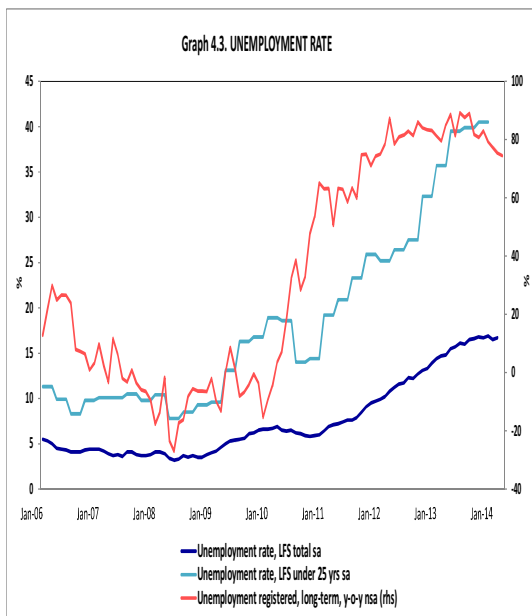
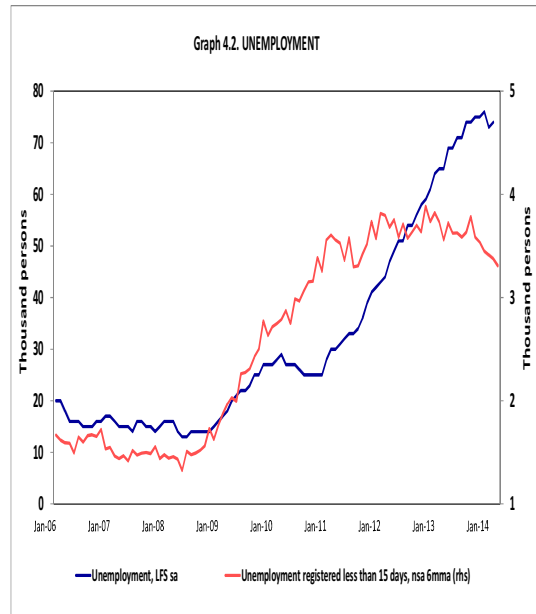
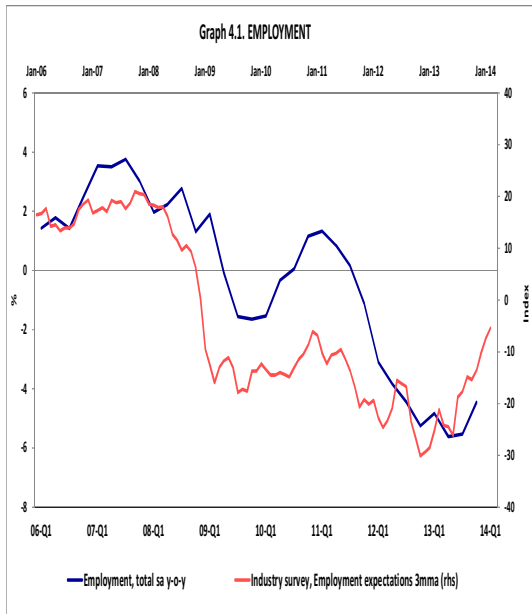
Sources: Eurostat, DG ECFIN, Cystat, JCC Payment Systems Ltd

### 3. INVESTMENT



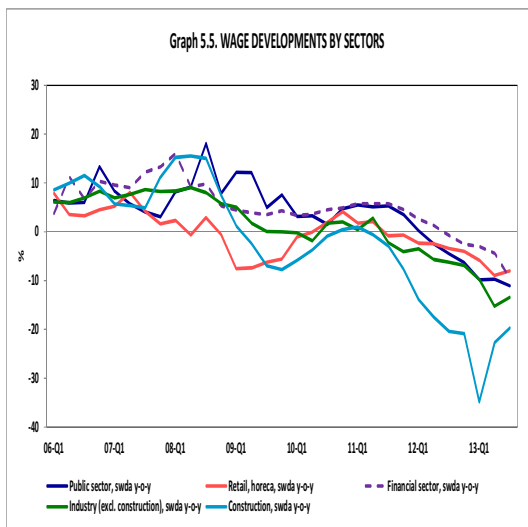
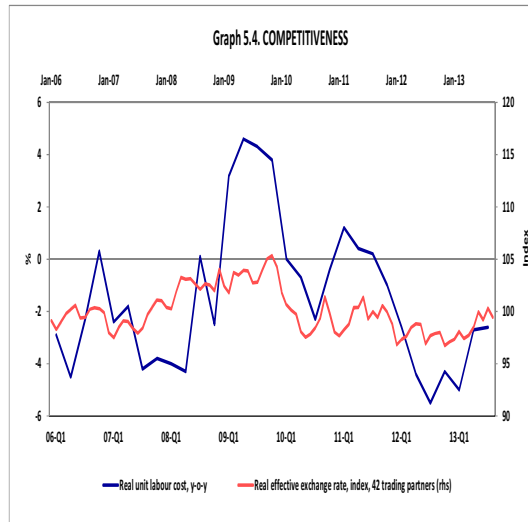
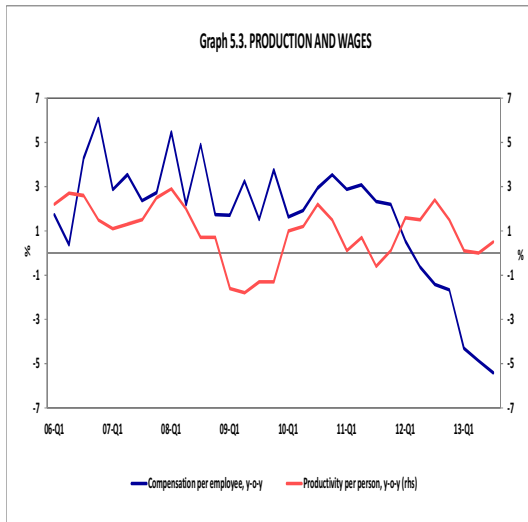
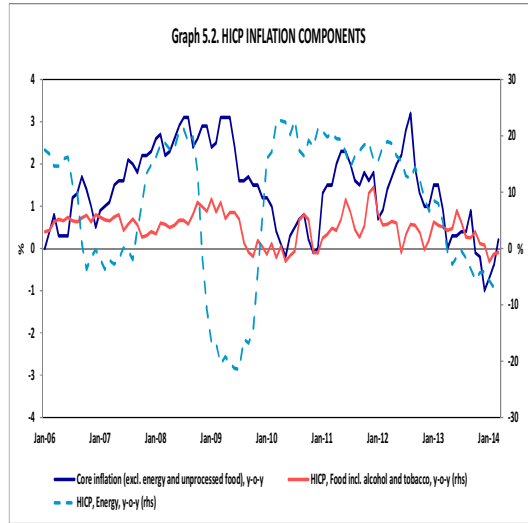
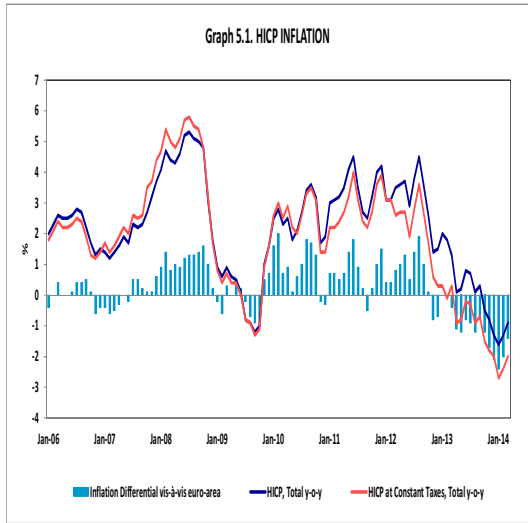
Sources: Eurostat, DG ECFIN, Cystat

## 4. LABOUR MARKET



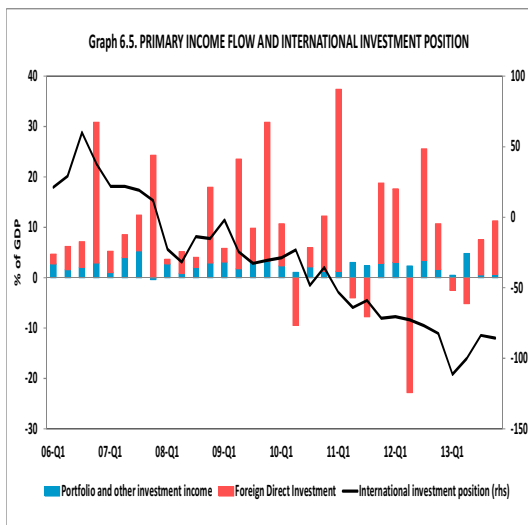
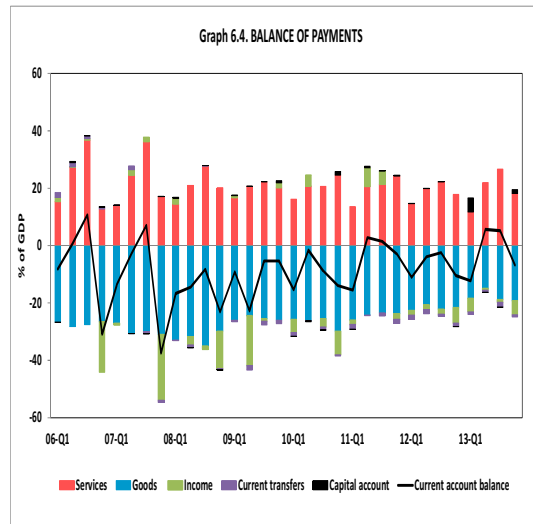
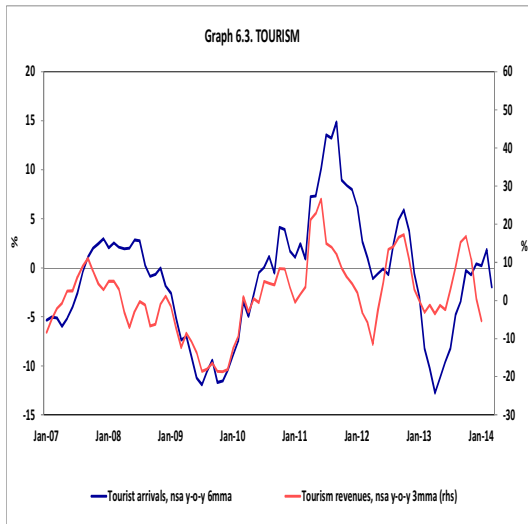
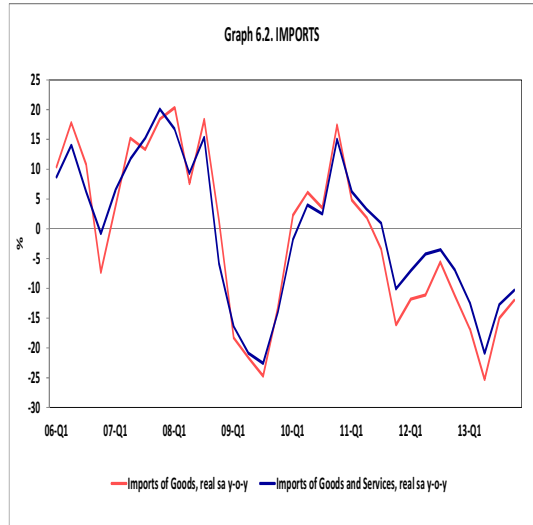
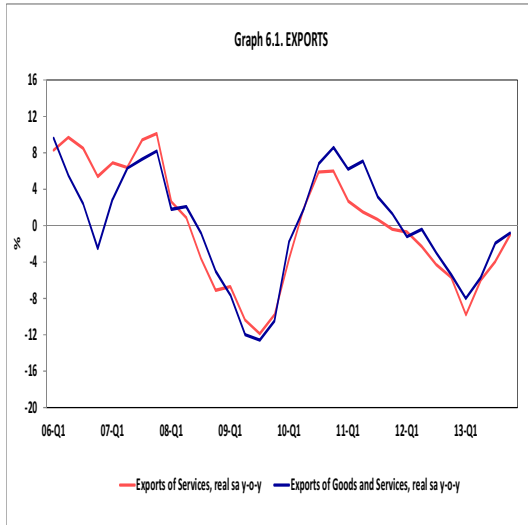
Sources: Eurostat, DG ECFIN, Cystat

## 5. INFLATION, WAGES



Source: Eurostat

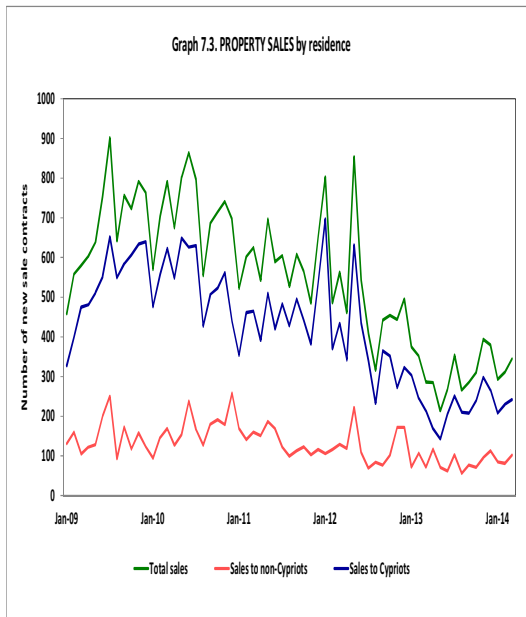
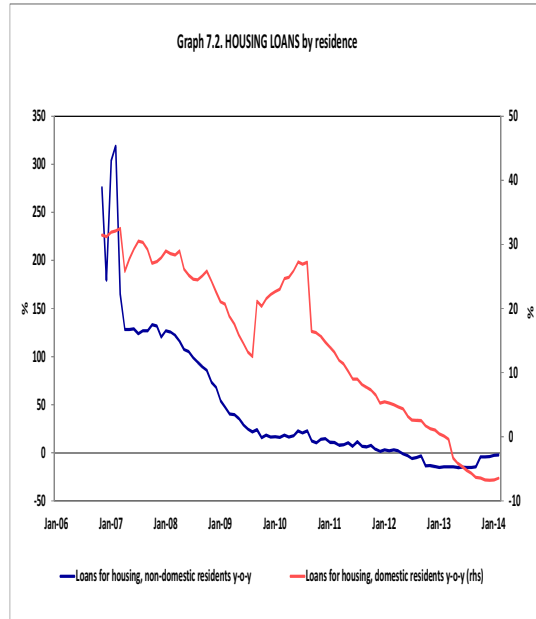
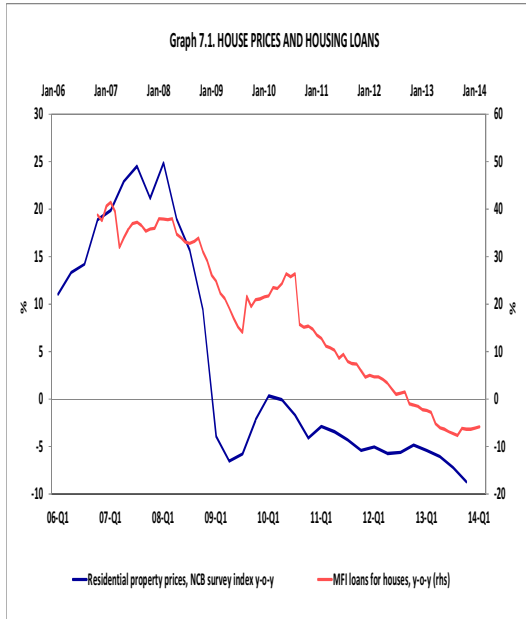
## 6. EXTERNAL SECTOR



Sources: Eurostat, Cystat, ECB, CBC

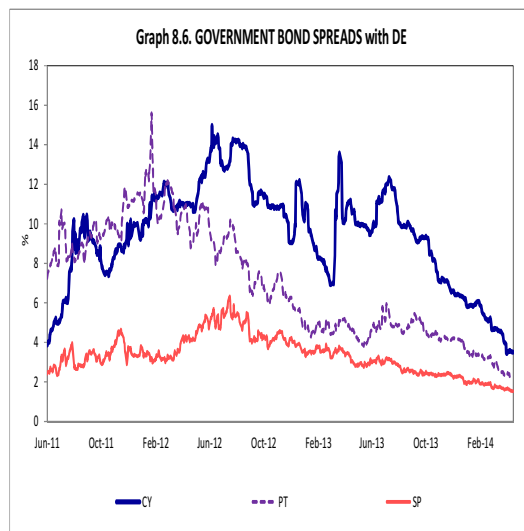
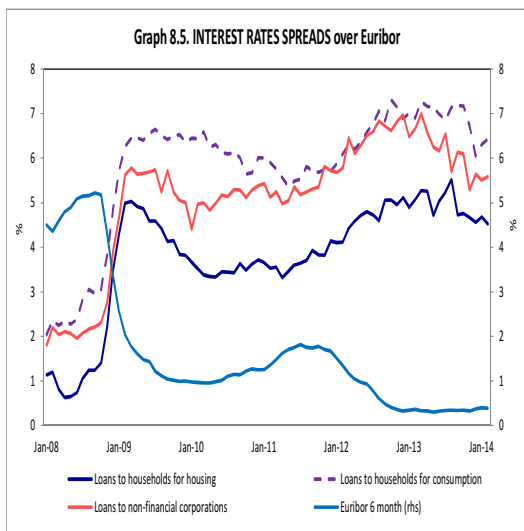
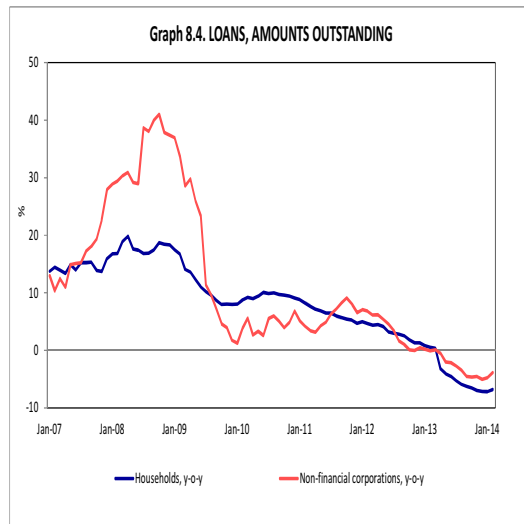
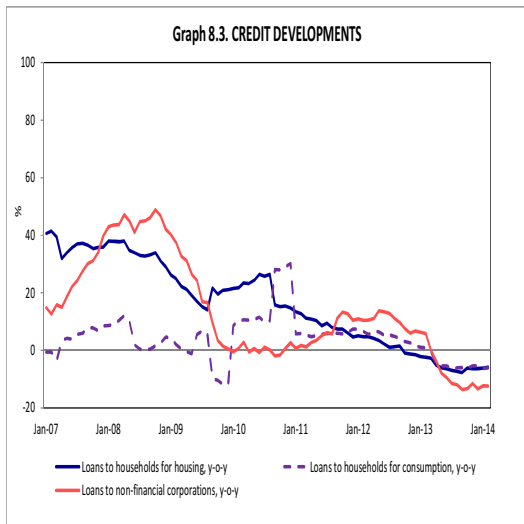
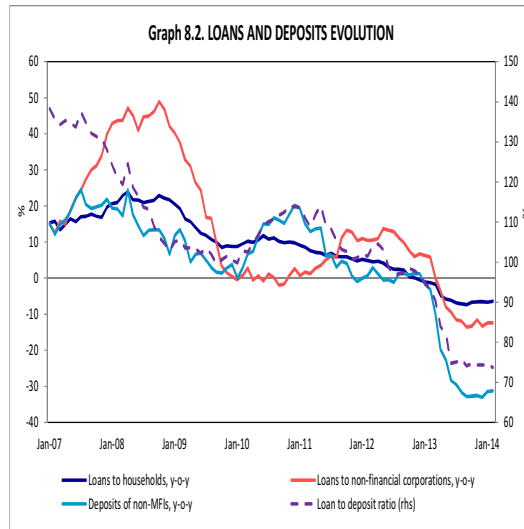
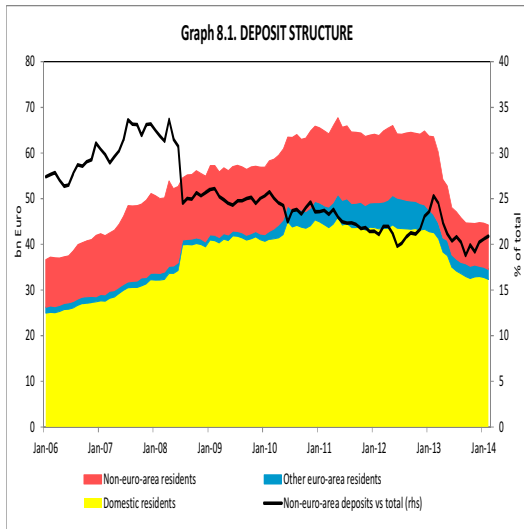


## 7. HOUSING



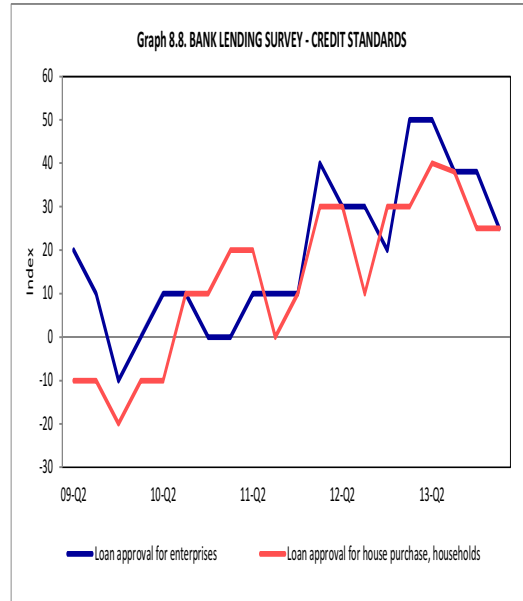
Sources: ECB, CBC, Dep. of Lands and Surveys

## 8. FINANCIAL SECTOR



Sources: ECB, CBC, Bloomberg

## 8. FINANCIAL SECTOR – cont.



Source: ECB