

MACROECONOMIC MONITOR OF CYPRUS

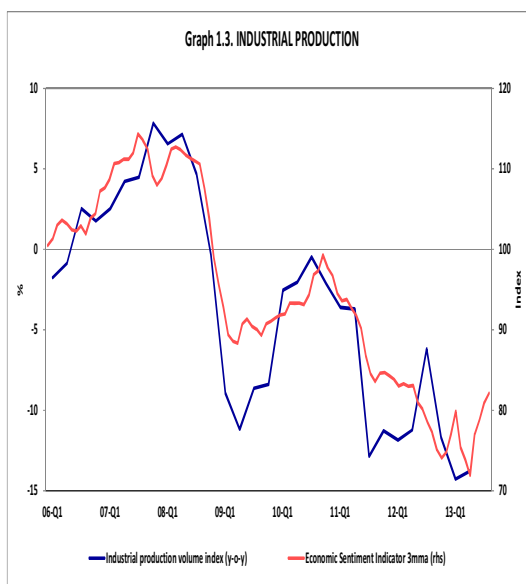
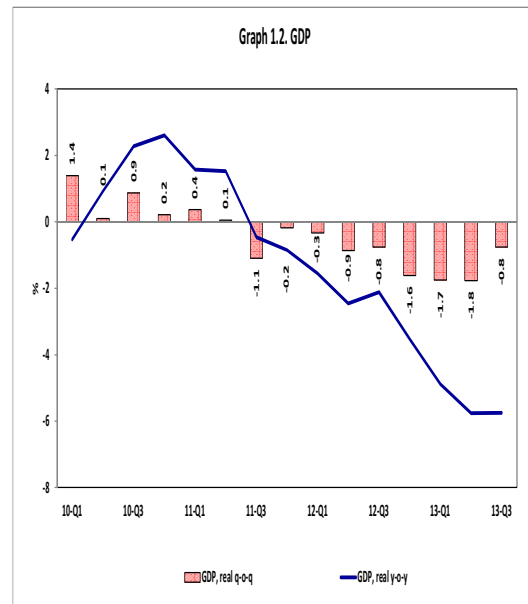
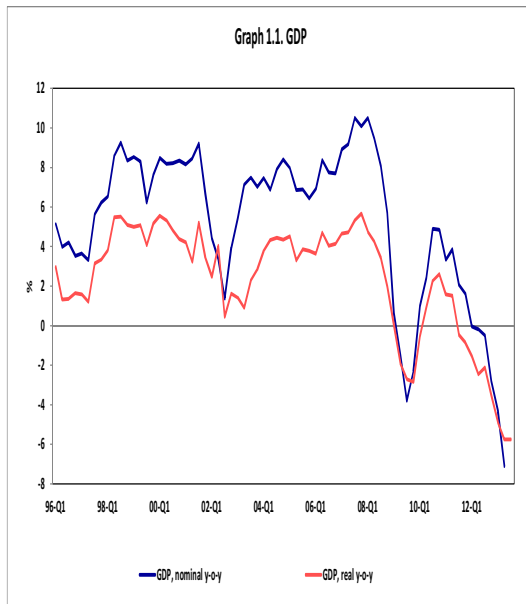
Updated on 15 November 2013

- In the 3rd quarter of 2013, GDP contracted by -5.7% on an annual basis and -0.8% on a quarterly basis (see graphs 1.1-1.2). The contraction was mainly due to the subdued performance of the secondary sector (construction, industry). 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). For the first nine months of 2013 GDP contracted by -5.5%, which suggests that the decline for the whole 2013 will be around -6%. Nevertheless, the business operating environment remains constraint given that lending to non-financial corporations is subdued and interest rates are still high. We maintain our view that developments in 2014 will be slightly more negative than expected in the first MoU, around -4.5% to -5%, and we assume rebound in 2015 with restoration of lending at affordable rates.
- Developments are currently driven by lower domestic demand (see graphs 2.1-2.4).
- The economic sentiment indicator by CypERC presents a less negative picture, as it increased by 2 points in October 2013 compared to September 2013, although still remaining at negative levels (see graph 1.3). Expectations in some sectors showed an improvement from low levels, but it is too early to draw any conclusions.
- Exports of goods increased substantially by 11.4% in the period January-September 2013 compared to the same period in 2012, mainly due to the increase in the exports of pharmaceutical products, cement, potatoes and halloumi cheese.
- Tourist arrivals declined by 2.5% in the period January-October 2013 compared to the same period in 2012 (see graph 6.3). Per capita spending shows a noticeable improvement while revenues from tourism show a small increase.
- Employment is also affected by the slowdown and it is adjusting (see graphs 4.1 and 4.4). Employment in persons (FTE) decreased by 5.6% in the 1st half of 2013 compared to the 1st half of 2012. The decrease was more pronounced in construction, trade and manufacturing.
- Labour Force Survey (LFS) unemployment, in monthly seasonally adjusted figures, increased steeply from 12.7% in September 2012 to 17.1% in September 2013, 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.
- Compensation per employee in the 1st half of 2013 declined by 4.6% compared to the 1st half 2012, contributing to a decline of nominal unit labour cost and improving cost competitiveness especially in manufacturing (see graphs 5.3-5.5). The nominal unit labour cost declined by 4.6% in the 1st half of 2013 compared with the 1st half of 2012. The observed wage adjustment is expected to help containing the upward pressure on unemployment.

- Inflation remains subdued. As measured by the HICP, it decreased at a rate of -0.5% in October 2013 compared to 0.3% in September, and for the period January-October it stood at 0.7% compared to the same period in 2012 (see graphs 5.1-5.2).
- The current account balance in the 1st half of 2013 was in deficit of €150,3 mn (0.9% of GDP) compared to a deficit of €652,7 mn (3.7% of GDP) in the 1st half of 2012 (see graph 6.4). This is mainly due to the improvement of the goods account.
- The income account recorded a deficit of €95,2 mn in the 1st half of 2013 compared with a deficit of €145,6 mn in the 1st half of 2012 due to the reduction in expenditure which exceeded the reduction in revenues for this category (see graph 6.4).
- The international investment position of Cyprus (see graph 6.5) recorded an improvement in June 2013, reaching €17.126 mn compared with €18.817 mn in March 2013, thus remaining in a net liability position (Cyprus' liabilities exceed the respective assets).
- During the first nine months of 2013, the budget balance (on a cash basis) recorded a deficit of €383 mn (2.33% of GDP) as compared to a deficit of €582,3 mn (3.26% of GDP) during the same period of 2012. The relatively good performance in public finances is associated with formidable expenditure constraint in the context of the implementation of the MoU as well as to further discretionary spending cuts, beyond those foreseen in the MoU. Nevertheless, public debt increased substantially, reflecting the steep decline of GDP as well as pre-financing of government operations.
- Monetary Financial Institutions (MFI) loans to domestic residents (private sector), declined with an annual rate of 6% in September 2013, affecting both households and enterprises (see graphs 8.2-8.4). This is reflecting low demand and very tight lending conditions (see graphs 8.7-8.9).
- Deposits of domestic residents held with MFIs (private sector) exhibited a substantial fall presenting an annual decline of 15.3% in September 2013, 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 levy on deposits. However, the decline in deposit rates is much bigger than the decline in lending rates (see graph 8.5). In September 2013, deposit interest rates overall remained constant compared to the previous month, whereas lending rates for loans to corporations up to €1 mn and for loans for house purchase exhibited an increase. A significant deviation of the Cypriot interest rates, compared to the euro area average is still observed, mainly in relation to loans to businesses.
- The CBC's residential property price index declined by 6.1% in the 2nd quarter of 2013 on an annual basis and cumulative from the 1st quarter of 2008 it has declined by around 18.1% (see graph 7.1).
- According to the Department of Lands and Surveys, new sale contracts were 43.8% lower and property transfers were 30.9% lower in January-October 2013 compared to the same period in 2012 (see graph 7.3). MFI loans to domestic residents for housing declined with an annual rate of 4.6% in September 2013 (see graph 7.2).

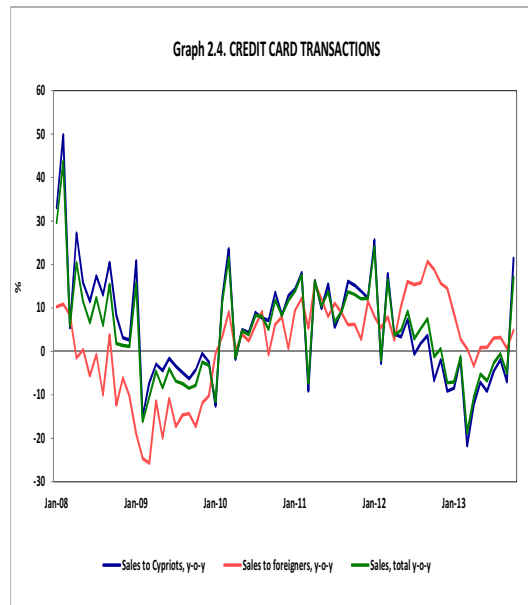
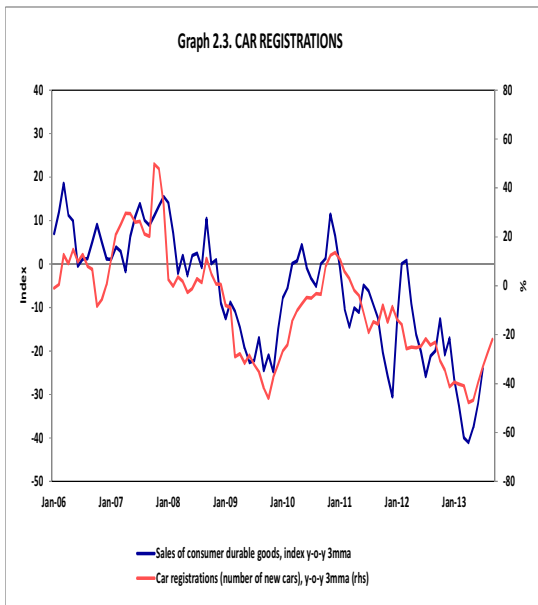
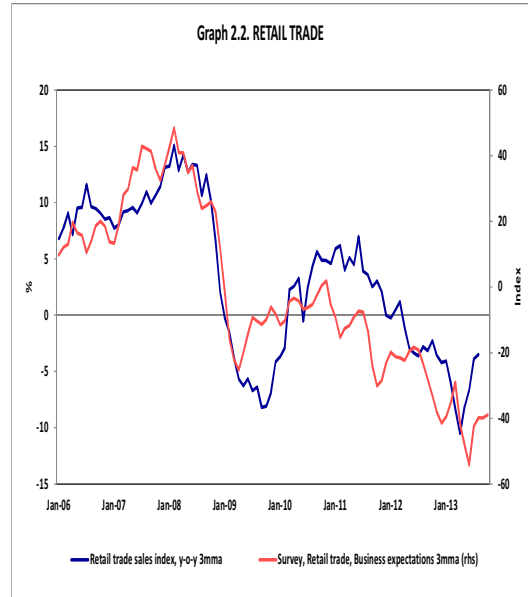
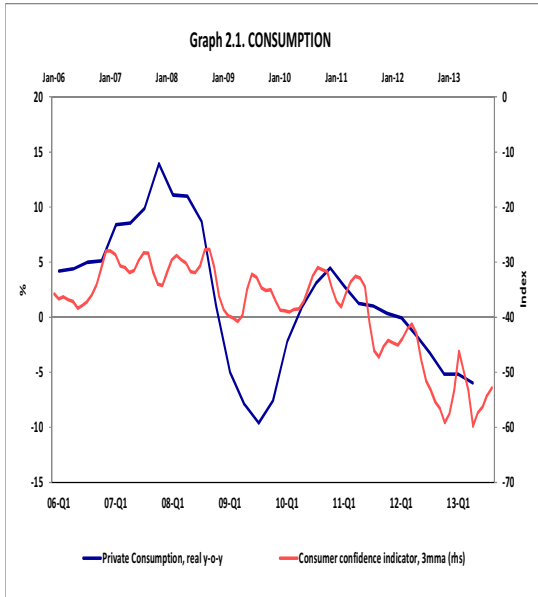
- The Cyprus Government bond spread compared to the German Government bond, in the first 10 days of November 2013 has decreased compared to October 2013 (see graph 8.6, yields refer to the bonds maturing in 2020).

1. OUTPUT



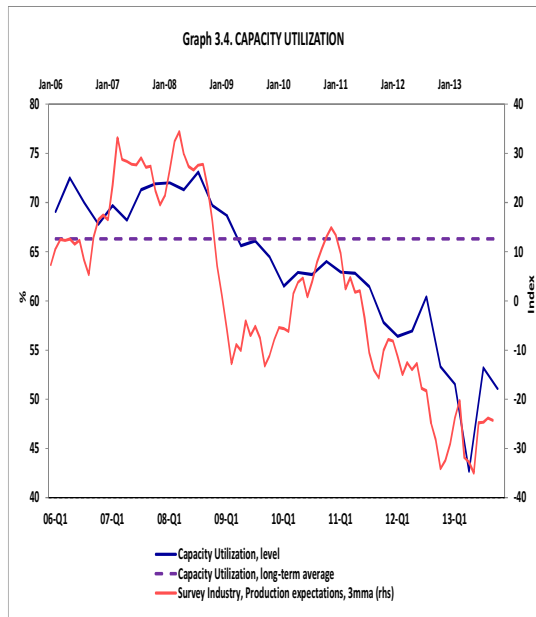
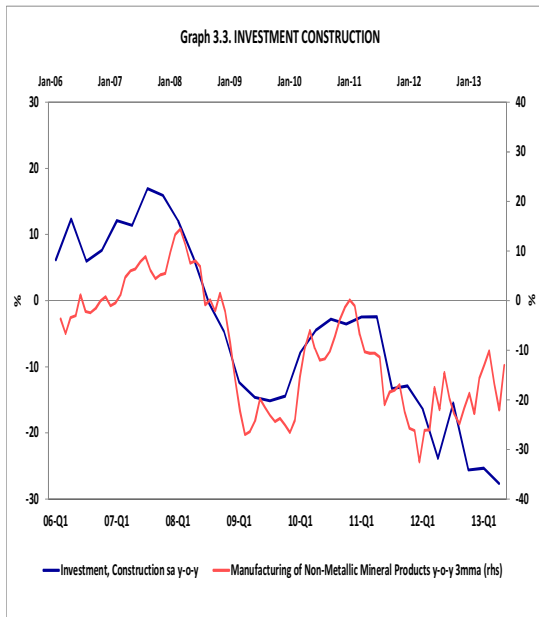
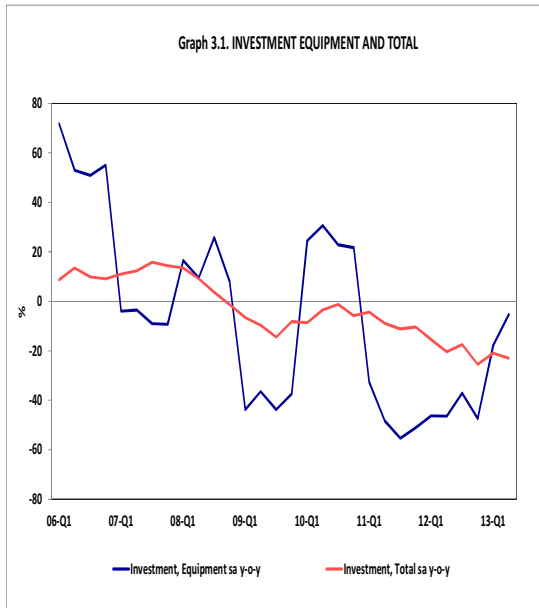
Sources: Eurostat, DG ECFIN

2. CONSUMPTION



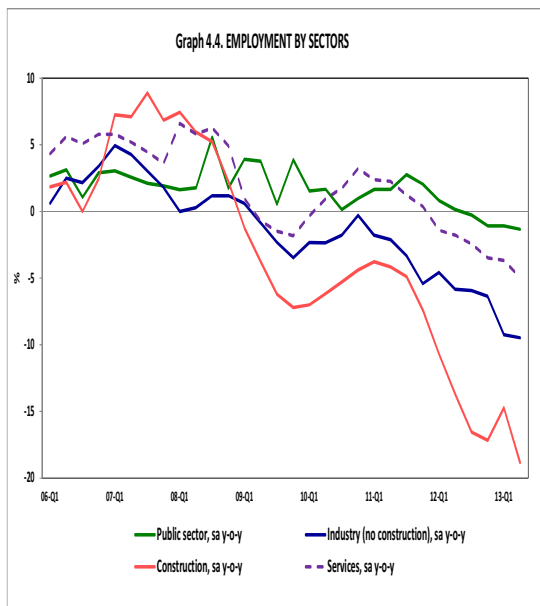
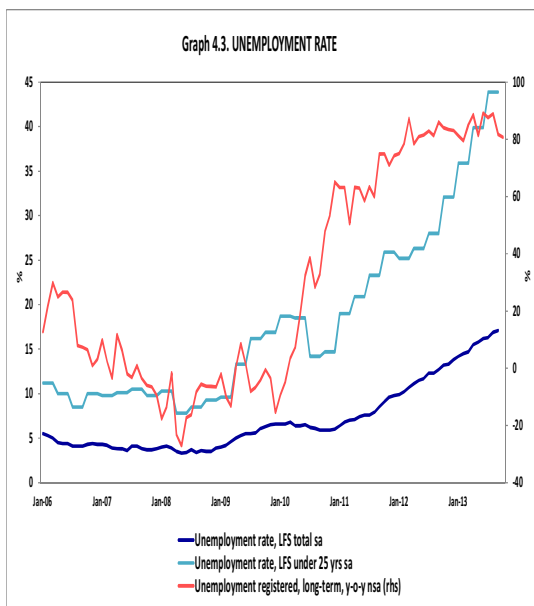
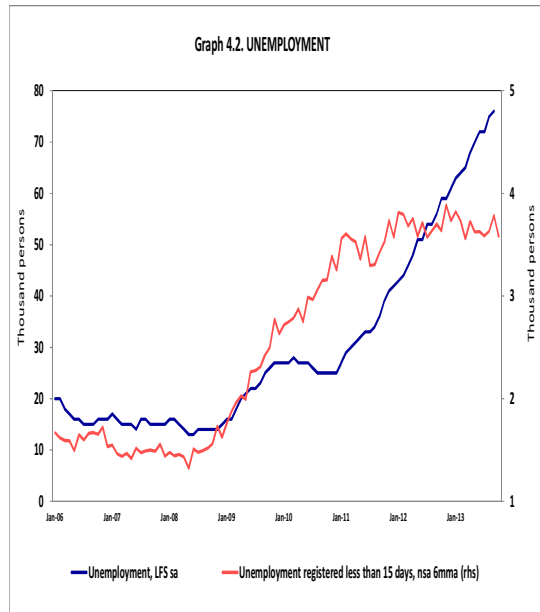
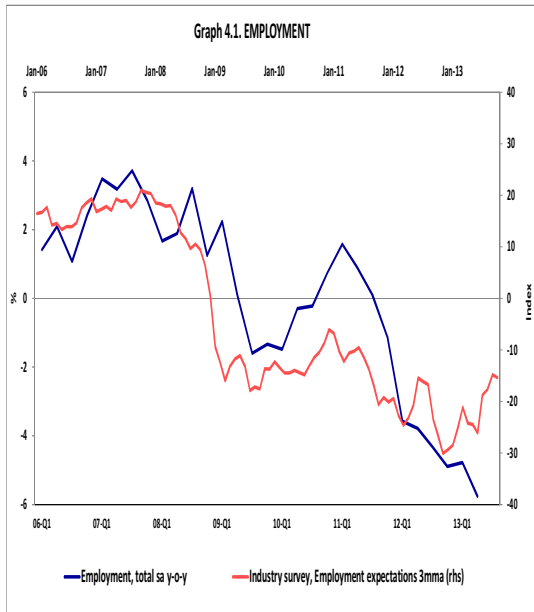
Sources: Eurostat, DG ECFIN, Cystat, JCC Payment Systems Ltd

3. INVESTMENT



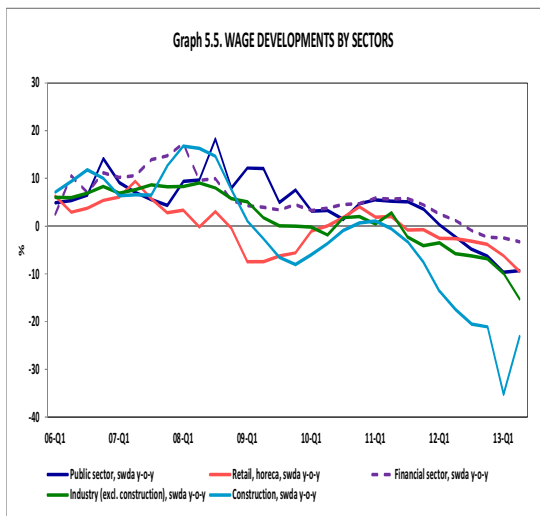
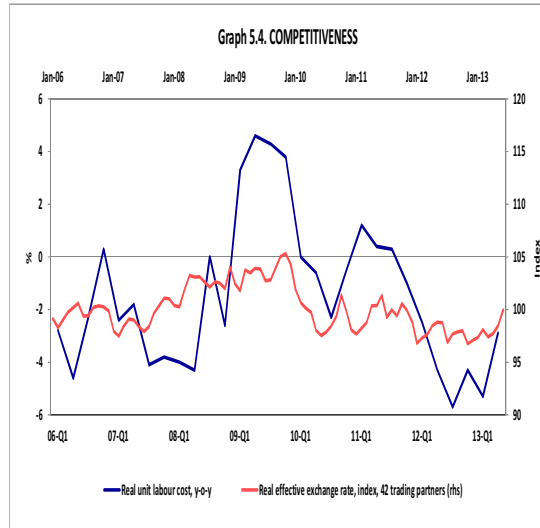
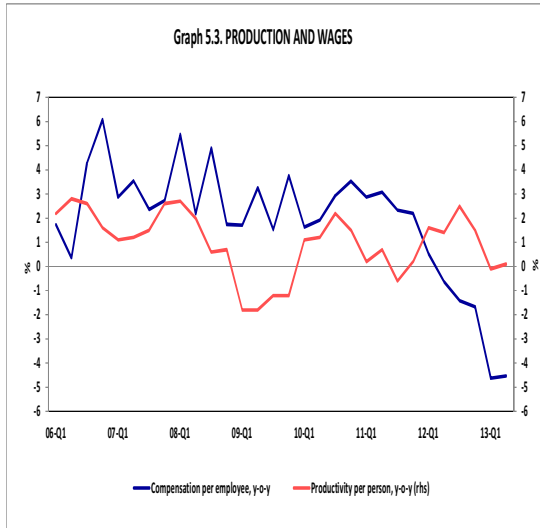
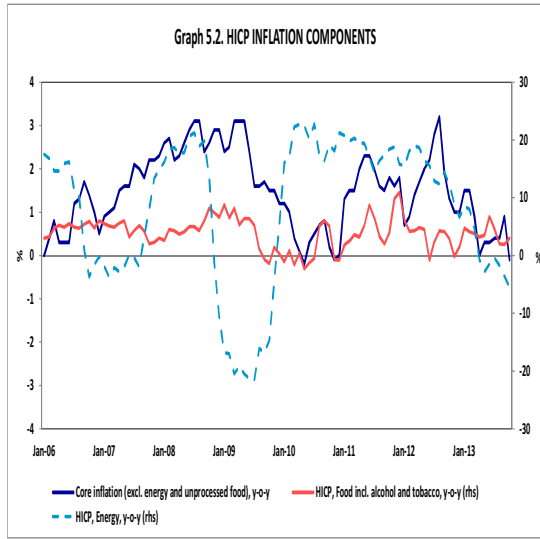
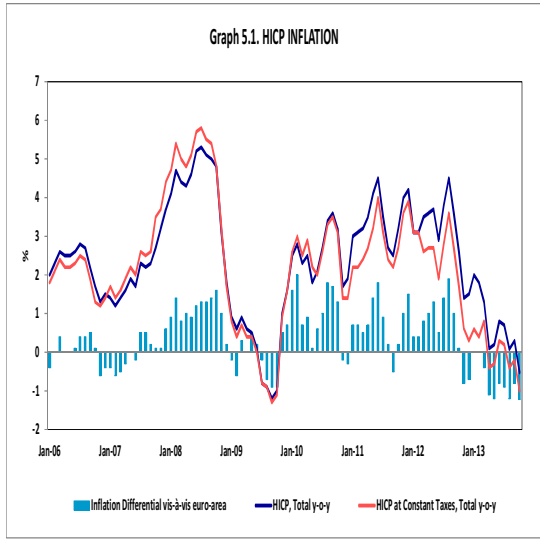
Sources: Eurostat, DG ECFIN, Cystat

4. LABOUR MARKET



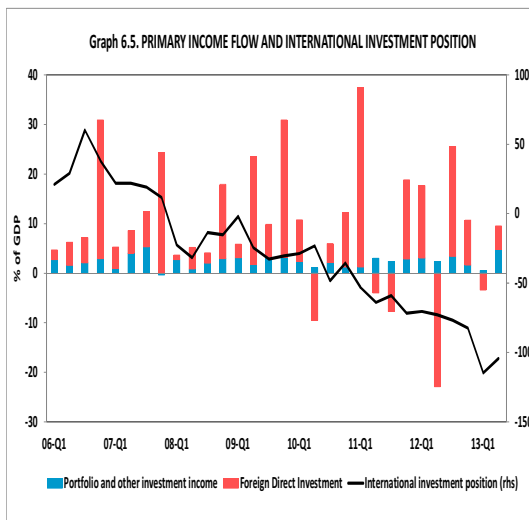
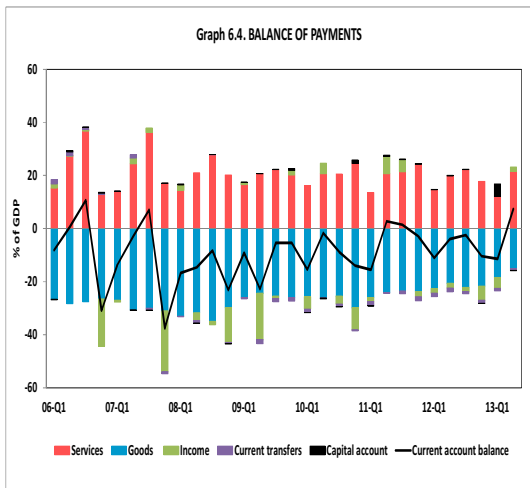
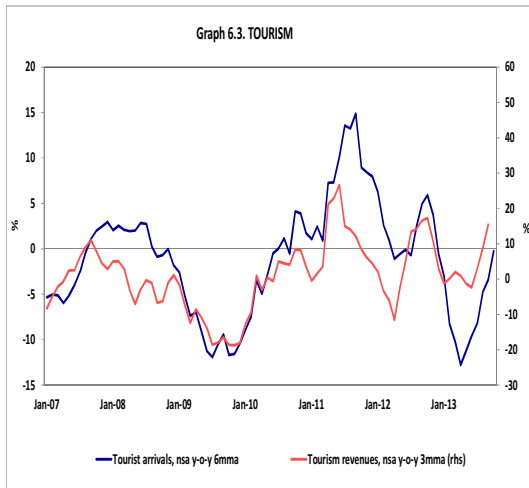
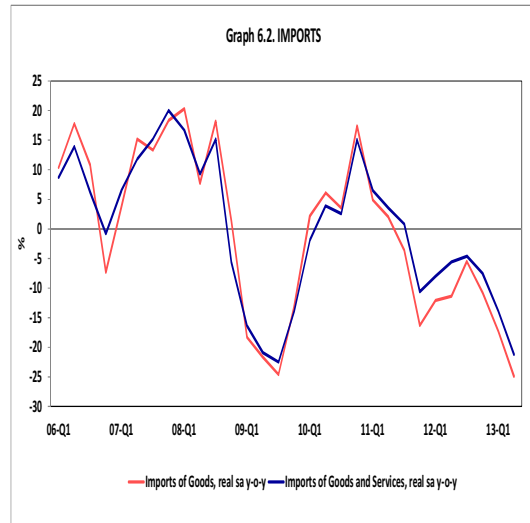
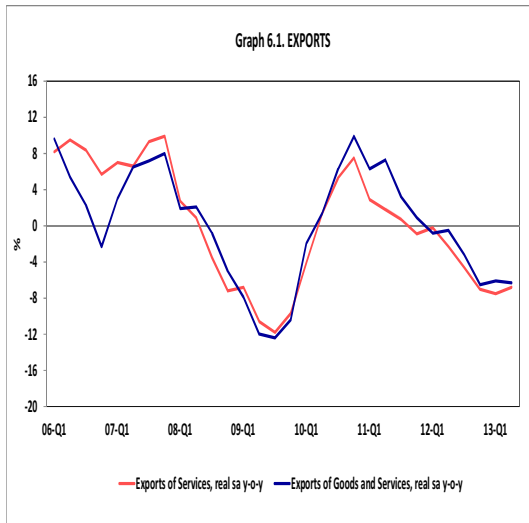
Sources: Eurostat, DG ECFIN, Cystat

5. INFLATION, WAGES



Source: Eurostat

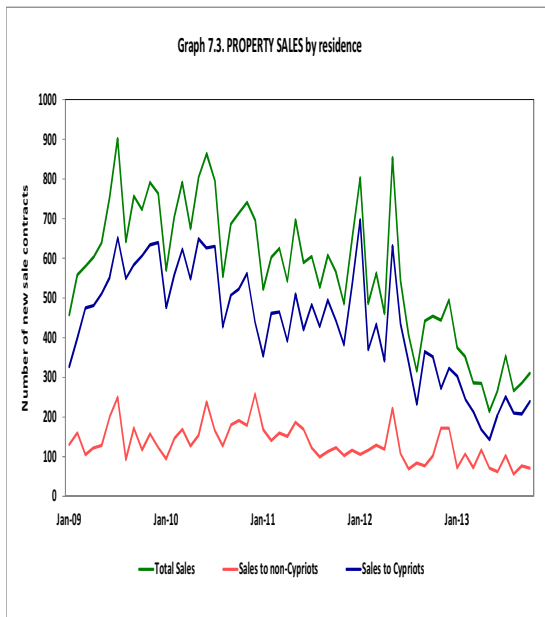
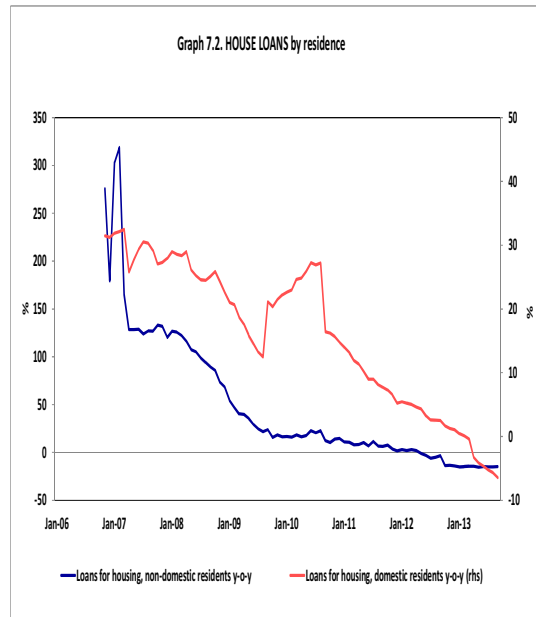
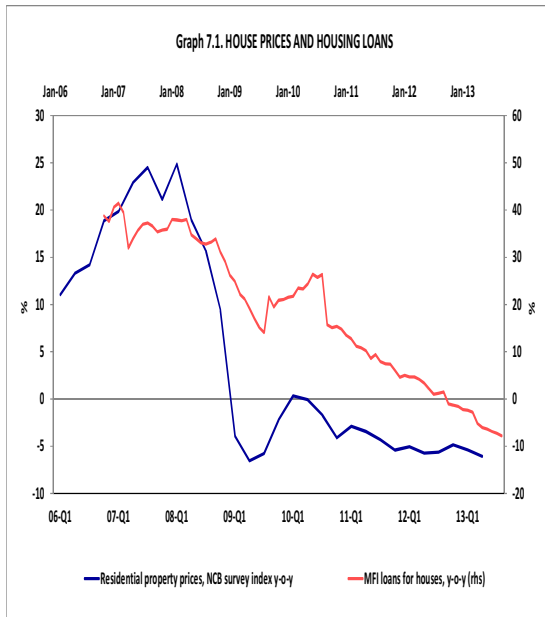
6. EXTERNAL SECTOR



Sources: Eurostat, Cystat, ECB, CBC

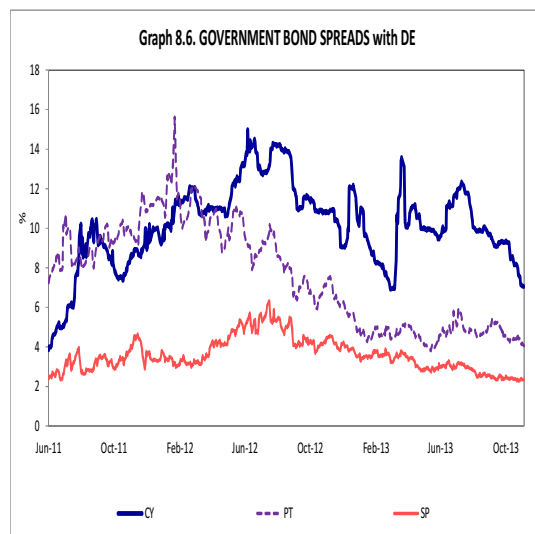
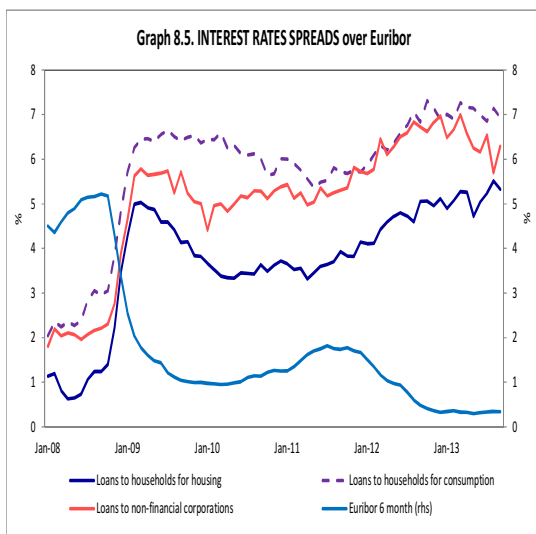
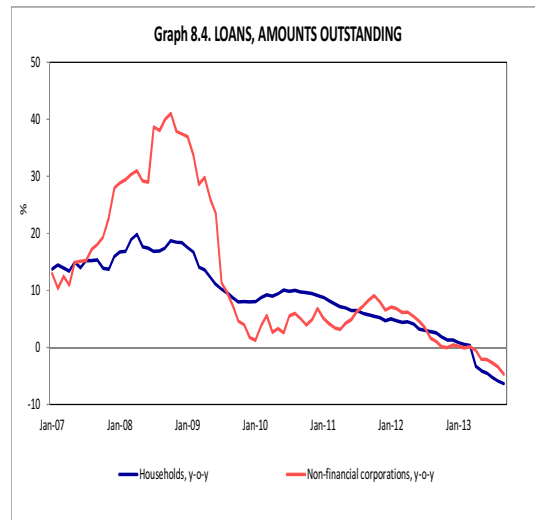
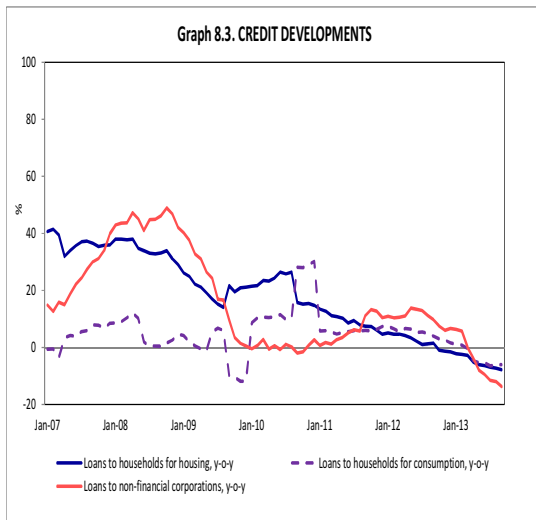
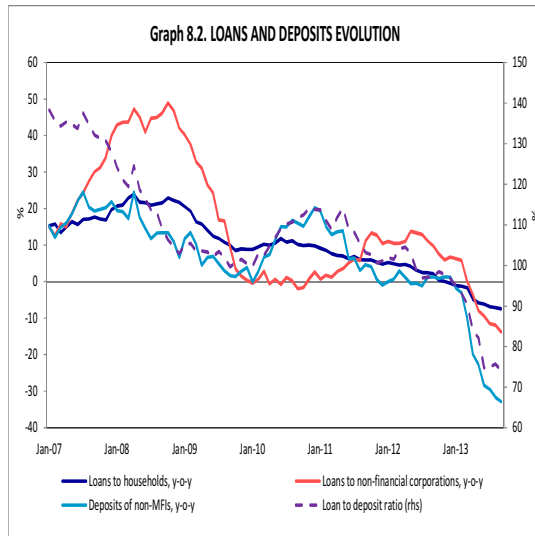
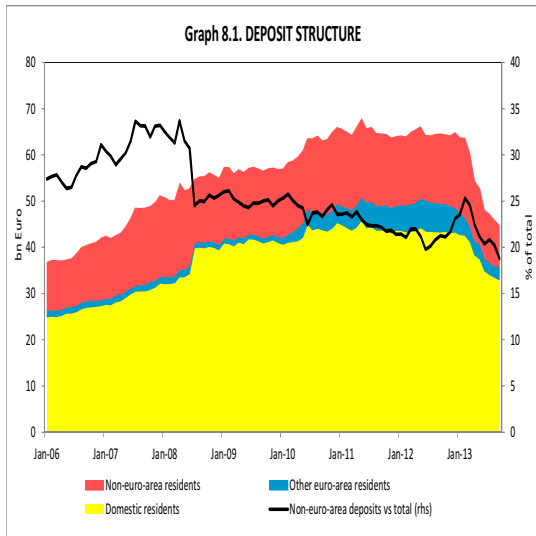
Note: In graph 6.3, data for tourism revenues for January 2013 is based on estimations by the MoF.

7. HOUSING



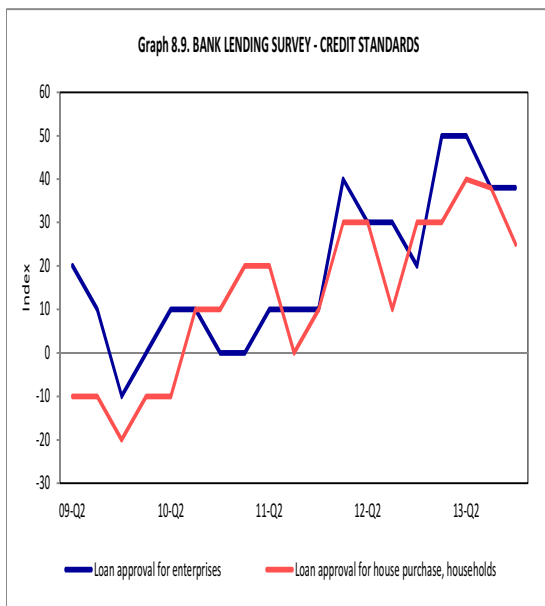
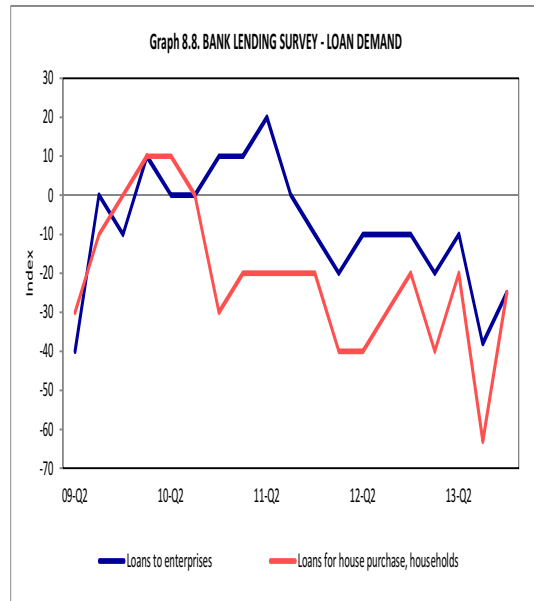
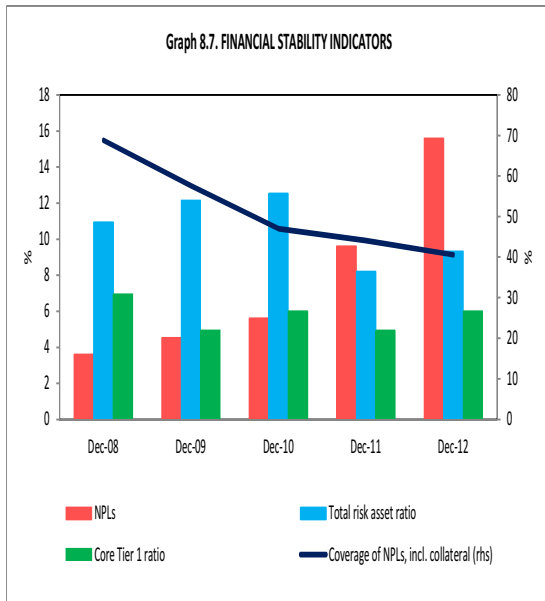
Sources: ECB, CBC, Dep. of Lands and Surveys

8. FINANCIAL SECTOR



Sources: ECB, CBC, Bloomberg

8. FINANCIAL SECTOR – cont.



Sources: CBC, ECB disseminated April 2013