



MACROECONOMIC MONITOR OF CYPRUS

February 2019

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Updated on 25 February 2019

Macro economy

- **In the 4th quarter of 2018, GDP** (in seasonally adjusted terms) **recorded a positive rate of growth of 3.9%, compared to 3.7% in the 3rd quarter of 2018** on an annual basis (see graphs 1.1-1.2). The increased activity is mainly attributed to the sectors: hotels and restaurants, retail and wholesale trade, construction, manufacturing, transport and storage, professional, scientific and technical activities and administrative and support service activities. Negative growth rate was recorded by the sector financial and insurance activities (see graphs 3.1-3.4 and 6.1-6.2).
- Developments are currently driven by increases in **private consumption and net exports** (see graphs 2.1-2.4).
- The economic sentiment indicator (ESI-CypERC) in January 2019 decreased by 3.8 points compared with December 2018 (see graph 1.3). The decline was mainly driven by confidence losses in services and industry. Economic confidence in construction remained unchanged, while confidence in retail trade changed only marginally. Consumer confidence, measured by the revised Consumer Confidence Indicator, strengthened slightly.
- In January 2019 **tourist arrivals increased at a rate of 8%** compared to January 2018 (see graph 6.3). An increase of 35.4% was recorded in tourist arrivals from Germany, a 17.6% increase from the UK, a 2% decrease from Greece and a 27.3% decrease from Russia.
- **Employment** developments reflect conditions of strong economic activity (see graphs 4.1 and 4.4). Employment in persons recorded an **increase of 4.1%** in the first nine months of 2018 compared to the first nine months of 2017. Increases were recorded mainly in construction, accommodation and food service activities, wholesale and retail trade, manufacturing and professional, scientific and technical activities.
- **Labour Force Survey (LFS) unemployment**, in monthly seasonally adjusted terms, **decreased to 8.8% in December 2018 compared to 10.3% in December 2017** (see graphs 4.2-4.3). The most affected segment of the population is youth unemployment, although it has been on a downward trend since the 3rd quarter of 2013 falling to 18.7% in 2018Q3 from a peak of 40.5% in the 3rd quarter of 2013.
- **Compensation per employee** recorded an increase of 1.5% in the first nine months of 2018 compared to the first nine months of 2017 (see graphs 5.3-5.5).
- **Inflation (HICP)** in January 2019 recorded an increase of 2.1% compared to an increase of 1.0% in December 2018 (see graph 5.1). Core HICP 1.1% in January 2019 (see graph 5.2). All subcategories of HICP presented an increase except categories alcoholic beverages and tobacco, furnishings, household equipment and supplies, transport and communication.
- **Imports of goods recorded an increase of 10.7%** in January-December 2018 compared to January-December 2017. The increase in imports is affected by developments in imports of transport equipment (aircrafts and vessels). Imports of goods, excluding imports of aircrafts and vessels, exhibit an increase of 13.7%.
- **Exports of goods recorded an increase of 43%** in January-December 2018 compared to January-December 2017 due to exports of transport equipment (aircrafts and vessels) occurring in 2018. Exports of goods, excluding exports of aircrafts and vessels, exhibit an increase of 27.1%.

External Sector

- The **current account (CA)** balance (see graph 6.4) recorded an improvement in 2018/9m, with the deficit declining to €339.2 mn (1.6% of GDP), from €446.3 mn in 2017/9m (2.3% of GDP). This development is mainly attributed to an improvement in the trade balance, which recorded a surplus in 2018/9m of €338.5 mn (1.6% of GDP) compared to a surplus of €226.1 mn (1.2% of GDP) in 2017/9m. Primary and secondary income accounts contributed to the current account deficit by 3.3% of GDP in 2018/9m compared to 3.4% of GDP in 2017/9m. The CA balance for 2018/9m, adjusted to exclude imports/exports of Special Purpose Entities (SPEs) that primarily operate in the shipping industry (ship registration/deregistration) with a small footprint on the economy, recorded a deficit of 1.6% of GDP compared to a deficit of 1.3% of GDP the same period the year before.
- The **international investment position (IIP)** (see graph 6.5) recorded a small improvement in 2018Q3, showing a net liability position at €22,382.5 mn, compared with €22,582.7 mn the previous quarter. The decrease in Cyprus' net liabilities was due to the improvement in direct investment and other investment. This was mitigated by the worsening recorded in portfolio investment and derivatives.
- The **gross external debt** reached €103,957.2 mn in 2018Q3, compared with €101,246.8 mn in 2018Q2. All main categories of external debt increased with those of general government, other sectors and monetary financial institutions (excluding the CBC) recording the higher increases.

Public Finances

- **General government budget balance (GGBB)** continued to be in surplus in January-November 2018, of the order of €779.6 mn (3.7% of GDP) compared to a surplus of €477.1 mn (2.4% of GDP) during the corresponding period the year before (see graph 9.1).
- **General government primary balance (GGPB)** also recorded a surplus in January-November 2018, of the order of €1,211 mn (5.8% of GDP) compared to a surplus of €934.4 mn (4.9% of GDP) during the corresponding period the year before (see graphs 9.1-9.2).
- **Total revenue** exhibited a positive rate of growth of about 7.8%, reaching €7,064.9 mn in January-November 2018, compared to €6,551.8 mn during the corresponding period the year before (see graph 9.3).
- **Total expenditure** exhibited a positive rate of growth of about 3.5%, reaching €6,285.3 mn in January-November 2018, compared to €6,074.7 mn during the corresponding period the year before (see graph 9.3).

Property Market

- Eurostat's **house price index** for Cyprus recorded an increase of 1.7% in the 3rd quarter of 2018 compared to the 3rd quarter of 2017.
- The CBC's **residential property price index** recorded an increase of 0.3% in the 2nd quarter of 2018 compared to the 1st quarter of 2018 and an increase of 1.7% compared to the 2nd quarter of 2017. Cumulative from the 1st quarter of 2008 it has exhibited a decline of 27.3% (see graph 7.1), revealing an adjustment to the conditions of lower domestic and foreign demand.
- According to the Department of Lands and Surveys, new sale contracts were up by 10.2% while, transfers of property were down by 1.8% in January 2019 compared to January 2018 (see graph 7.3).
- MFI mortgage loans to domestic residents for housing decreased with an annual rate of 0.3% in December 2018 (see graph 7.2).

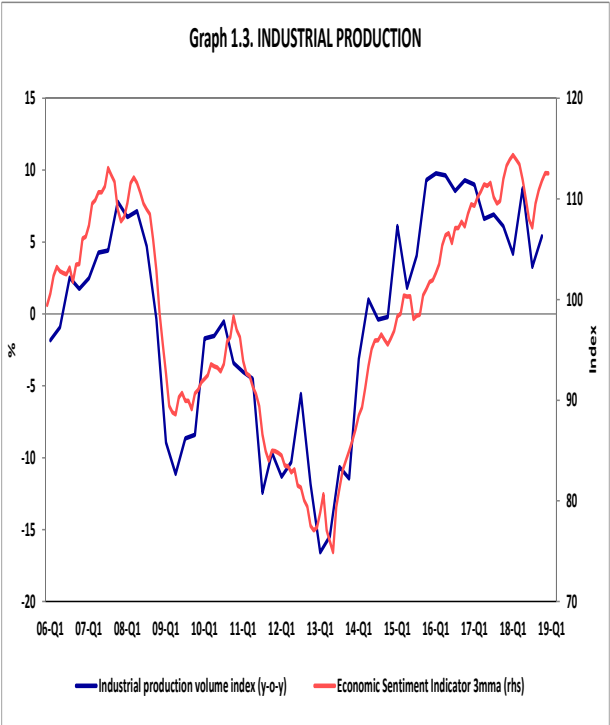
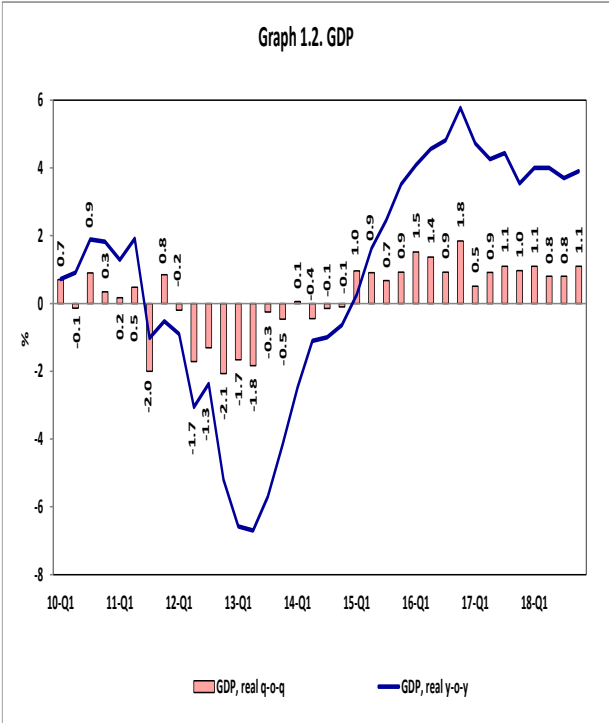
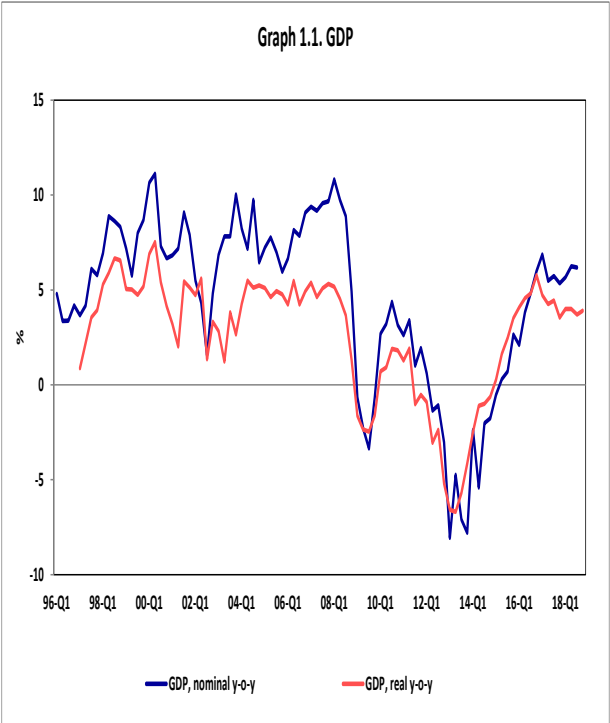
Banking Sector Developments

- Monetary Financial Institutions (MFI) **loans to domestic residents** (private sector), **increased at an annual rate of 0.4%** in December 2018, (see graphs 8.2-8.4). This reflects the still tight lending conditions (see graphs 8.6-8.7).
- **Deposits of domestic** residents held with MFIs (private sector) exhibited a decrease with an **annual rate of 0.1%** in December 2018 (see graph 8.1).
- Overall **lending and deposit interest rates** in Cyprus continue to decline, creating an environment conducive to growth (see graph 8.5). In December 2018, **deposit interest rates** for maturity of up to 1 year and of up to 3 months decreased compared with the preceding month. The **lending interest rates** to households for primary residence and the rate for other loans up to €1 mn for businesses decreased. The interest rate for bank overdrafts to non-financial corporations also decreased.
- NPEs represent the remaining legacy challenge currently faced by the Cyprus economy, amounting to approximately 32.0% of total lending in September 2018 compared to 42.5% in December 2017.
- NPEs in absolute terms are on a downward trend, falling to €11.2 bn in September 2018, representing a decrease of €9.7 bn in 2018.
- The significant decrease of NPEs in the first 9 months of 2018, is mainly attributed to the transfer of €5.7 billion NPEs of CCB to the Residual Entity and the sale of NPE portfolios (including the sale of €2.7 bn NPEs by Bank of Cyprus in June 2018 to Apollo Fund), as well as increased repayments, restructurings successfully completed and reclassified as performing facilities, write-offs and settlement of debt through swaps with immovable property.
- NPEs are classified based on the harmonised definition of the European Banking Authority, which includes loans that have been restructured and, even despite meeting their revised repayment schedule, retain the NPE status for at least 12 months after restructuring before being reclassified as performing.
- Accumulated provisions rose to 52.3% of NPEs in September 2018, compared to 47.3% as at the end of 2017, thus facilitating restructuring activity with a view to cure NPEs of viable customers.
- On 24/01/2019, Moody's upgraded Bank of Cyprus and Hellenic Bank Public long-term deposit ratings to B3 from Caa1, and their long-term Counterparty Risk Ratings (CRRs) to B1 from B2. At the same time, Hellenic Bank's baseline credit assessment (BCA) and adjusted BCA were upgraded to caa1 from caa2, and its long-term Counterparty Risk Assessment (CRA) to B1(cr) from B2(cr). The outlook on both banks' long-term deposit ratings is positive.

Credit ratings

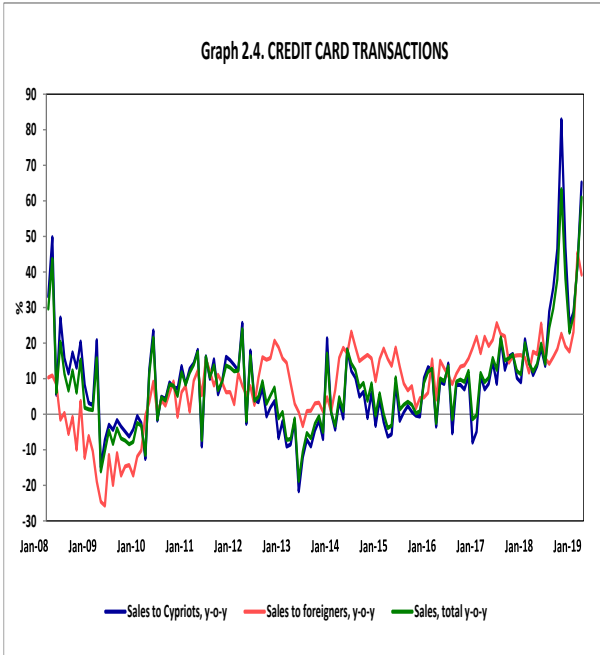
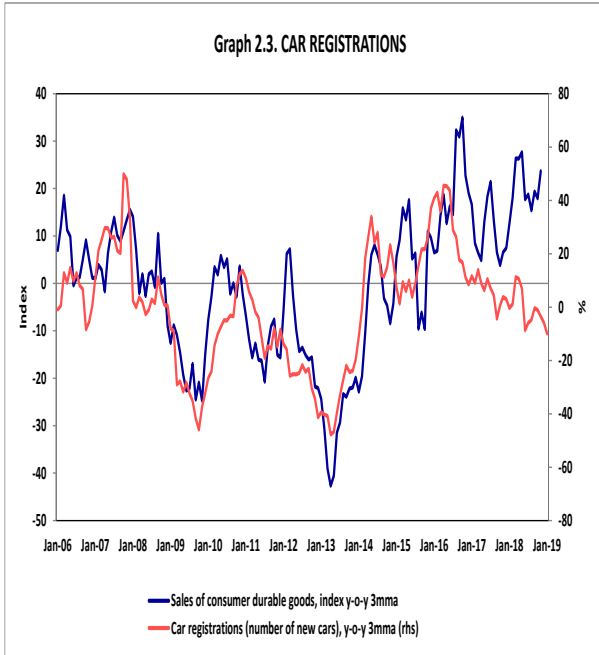
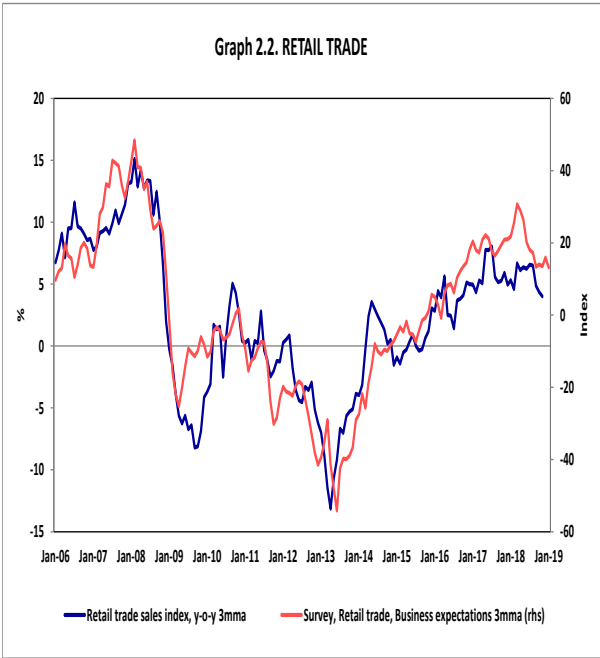
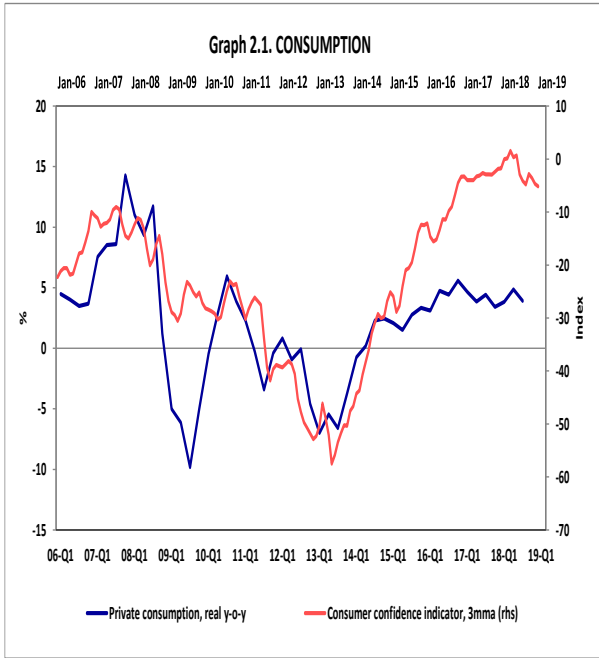
- On 14/09/2018, S&P Global Ratings raised Cyprus long- and short-term foreign and local currency sovereign credit ratings on Cyprus to 'BBB-/A-3' from 'BB+/B' placing it back to investment grade with a stable outlook.
- As a result of this upgrading, Cyprus government bonds are again accepted as collateral for Eurosystem credit operations. At the same time, they are again eligible under the Public Sector Purchase Program (PSP) for the procurement of public sector assets in the secondary markets.
- Furthermore, on 19/10/2018 Fitch Ratings upgraded Cyprus's Long-Term Foreign-Currency Issuer Default Rating (IDR) to 'BBB-' from 'BB+' placing it back to investment grade with a stable outlook.
- Additionally, on 23/11/2018, DBRS Ratings upgraded Cyprus's Long-Term Foreign and Local Currency-Issuer Ratings from 'BB' to 'BBB (low)' placing it to investment grade with a stable outlook.

1. OUTPUT



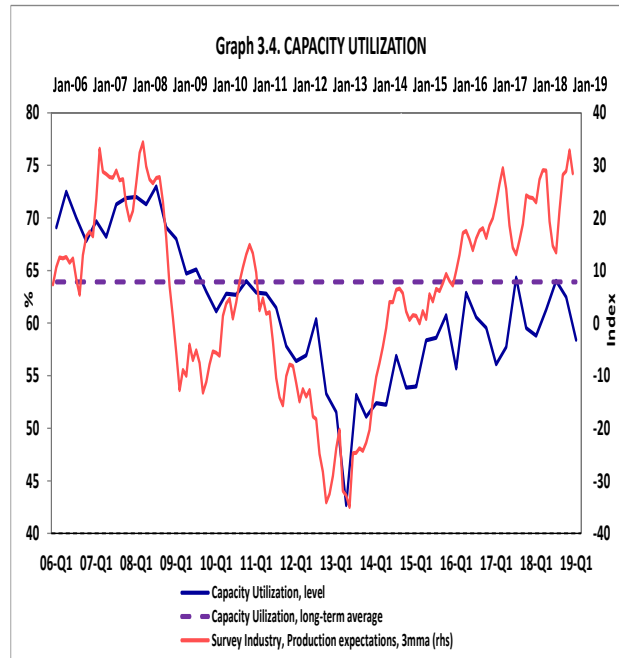
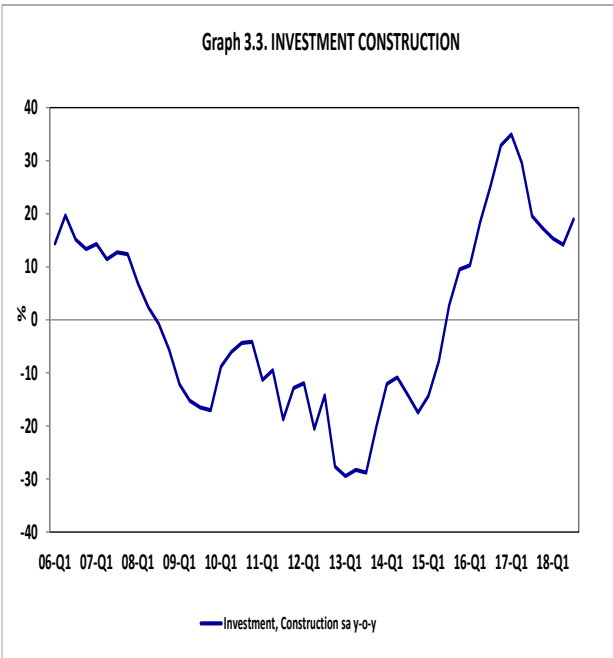
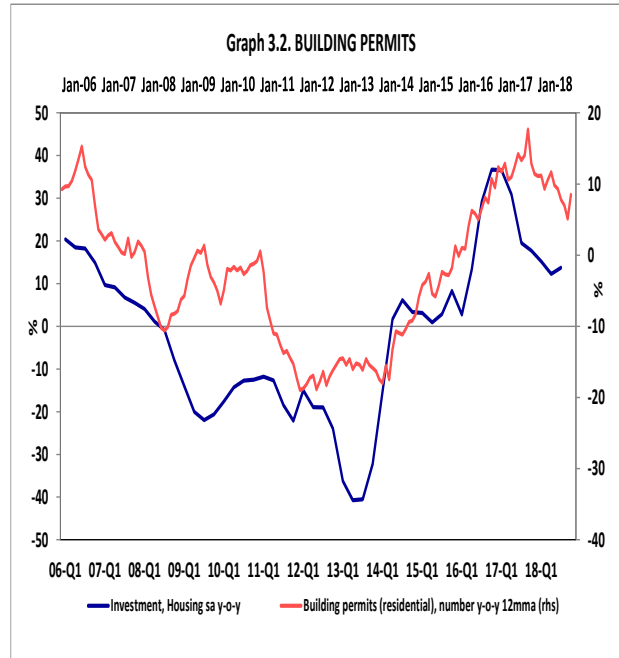
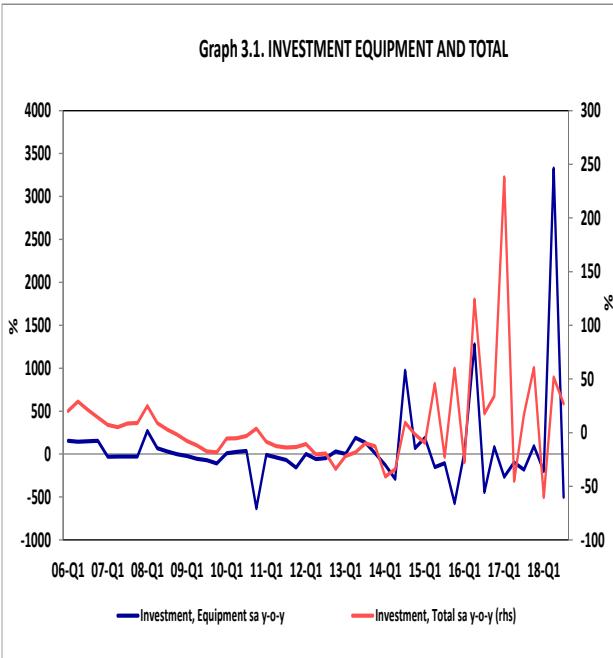
Sources: Eurostat, DG ECFIN, Cystat

2. CONSUMPTION



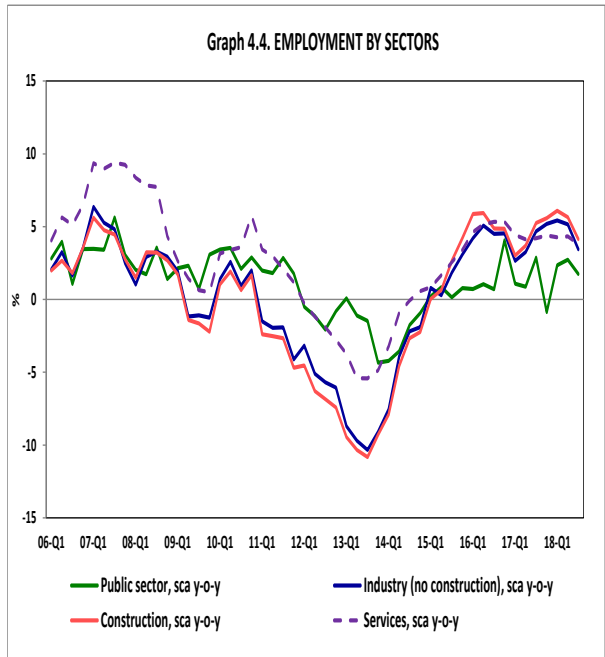
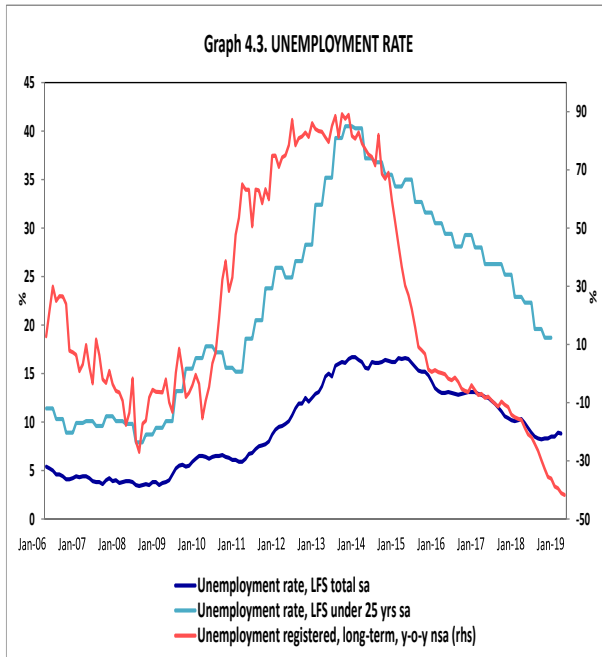
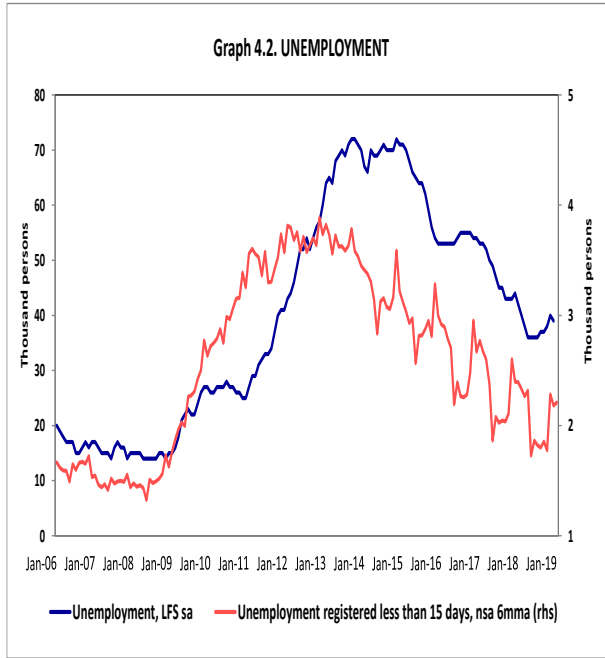
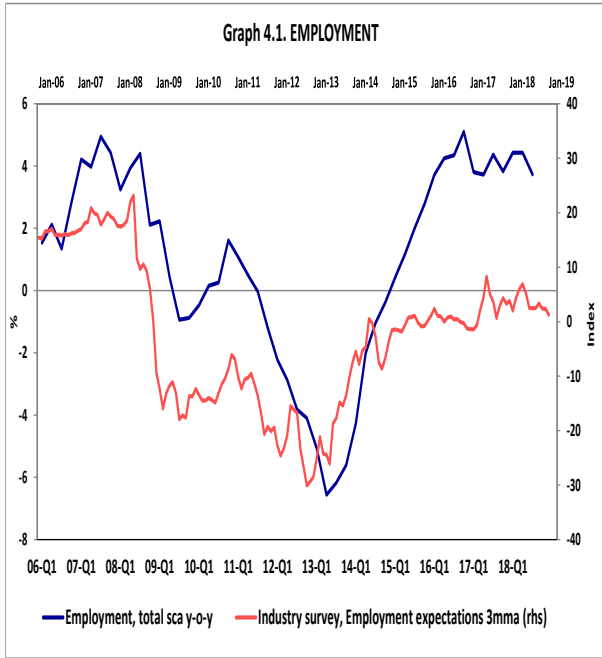
Sources: Eurostat, DG ECFIN, Cystat, JCC Payment Systems Ltd

3. INVESTMENT



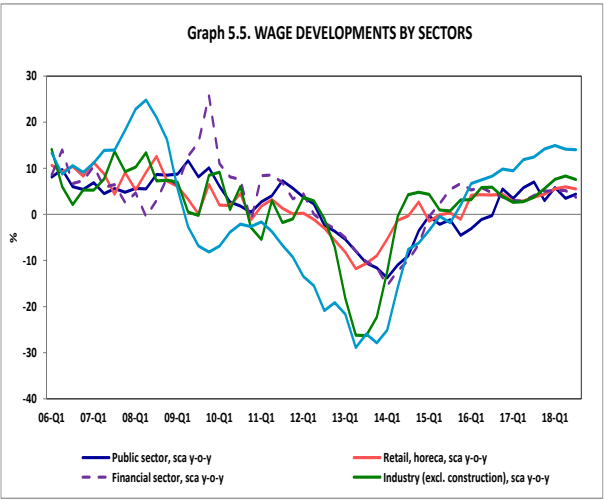
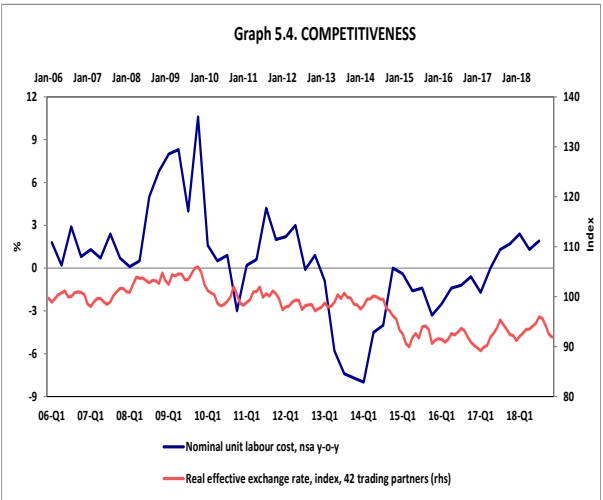
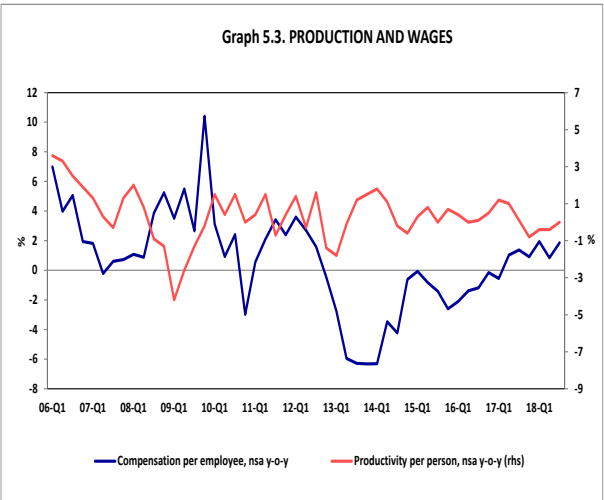
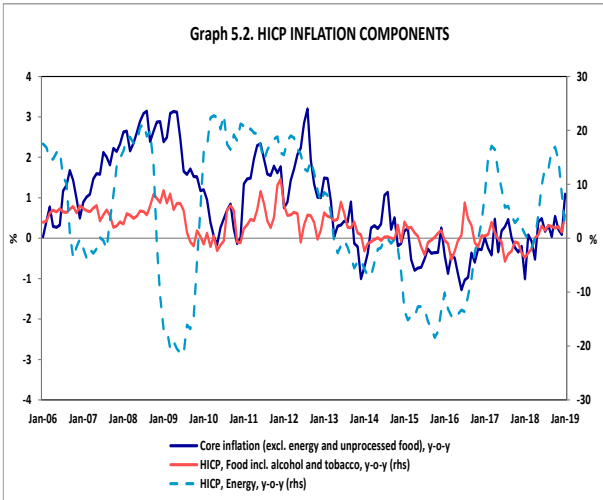
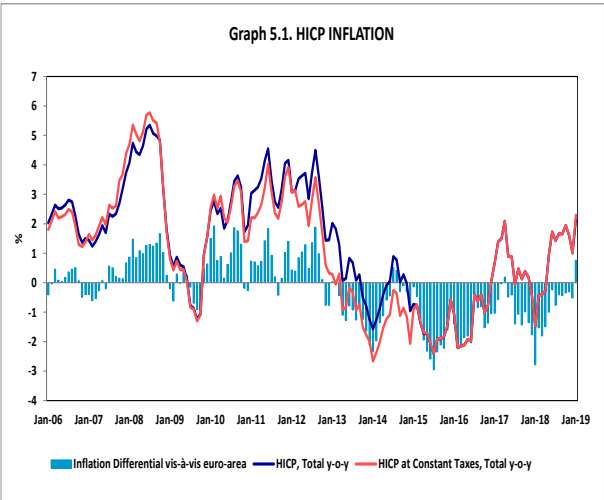
Sources: Eurostat, DG ECFIN, Cystat

4. LABOUR MARKET



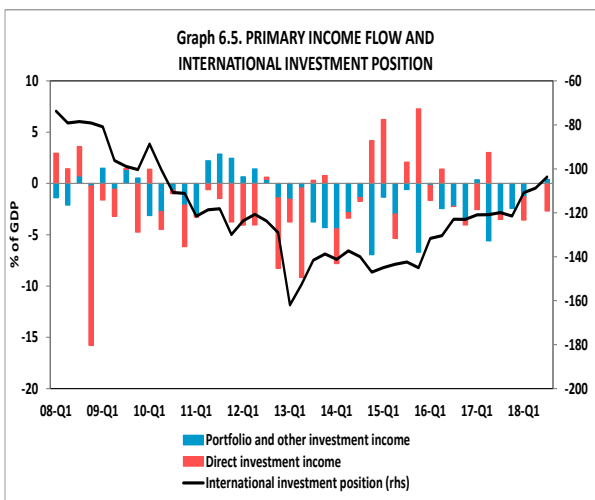
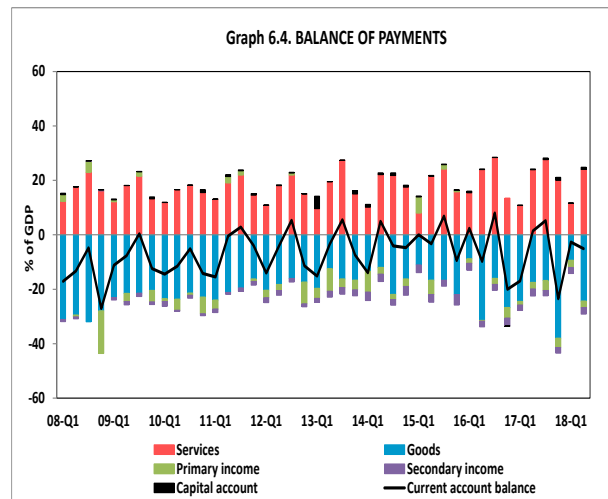
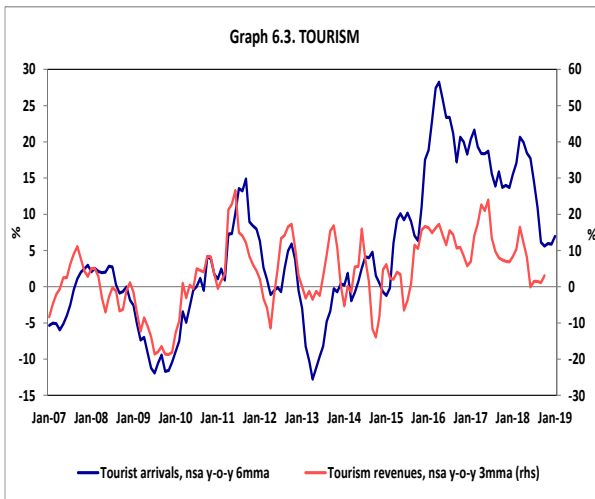
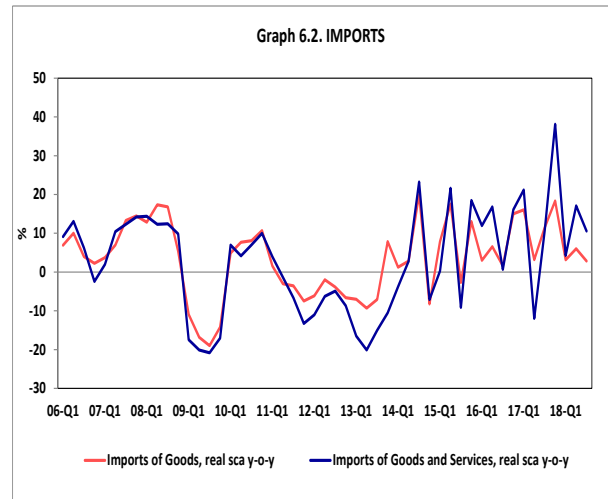
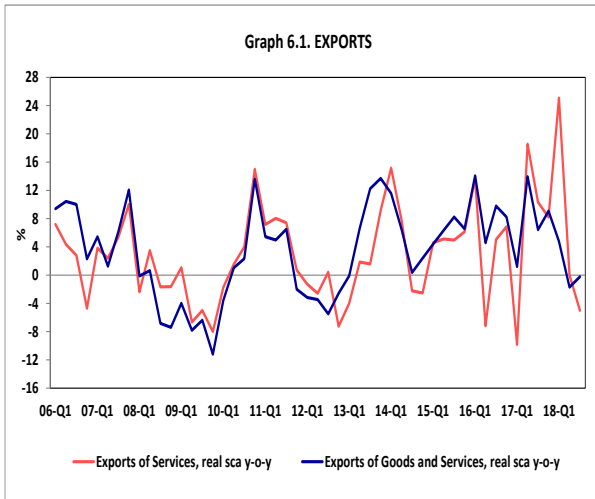
Sources: Eurostat, DG ECFIN, Cystat

5. INFLATION, WAGES



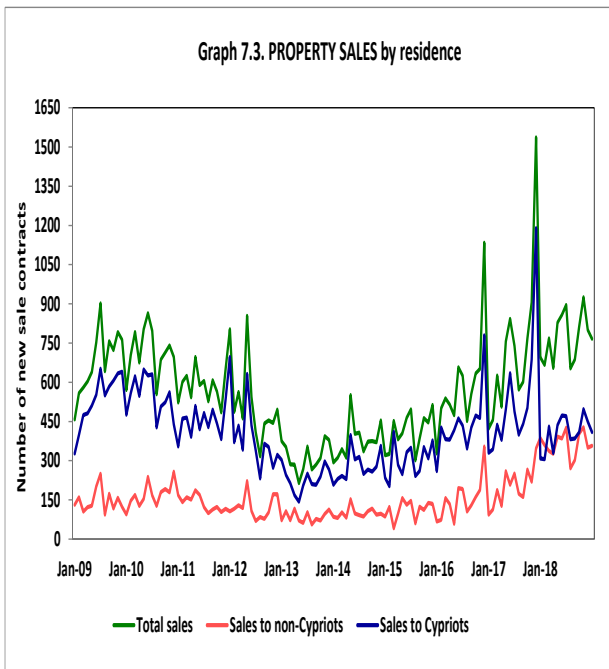
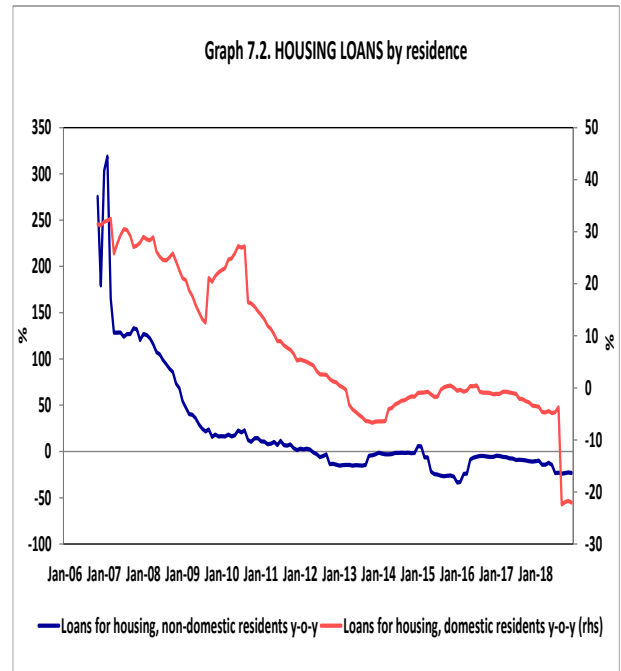
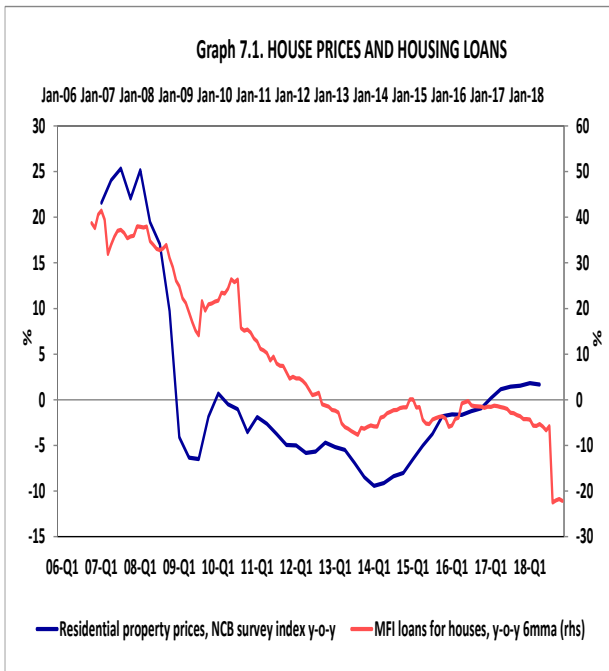
Source: Eurostat

6. EXTERNAL SECTOR



Sources: Eurostat, Cystat, ECB, CBC

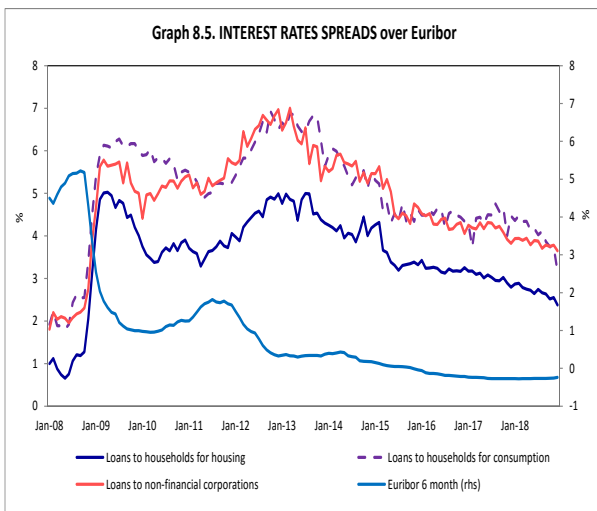
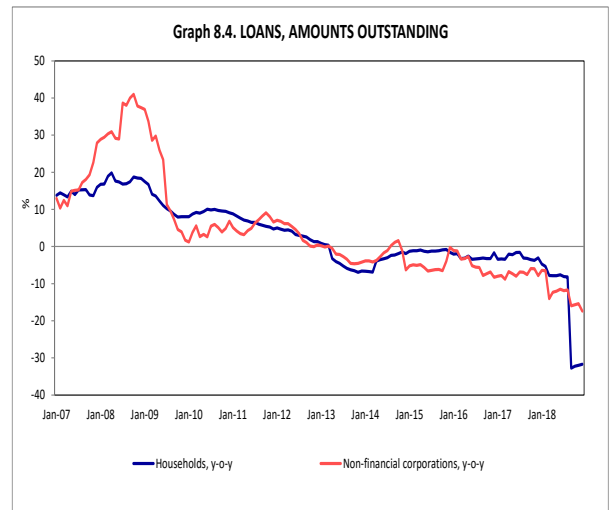
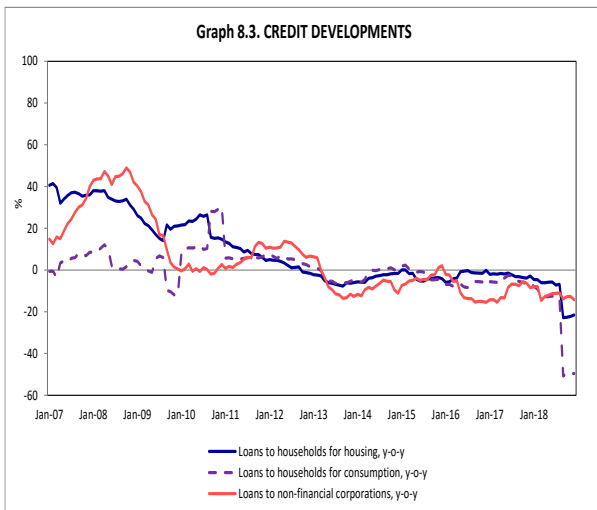
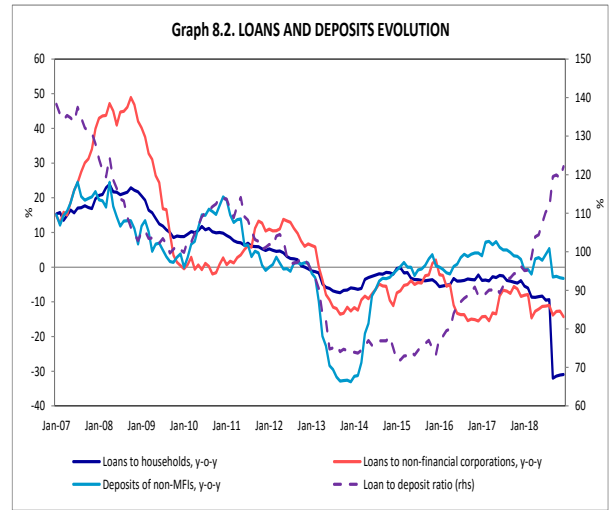
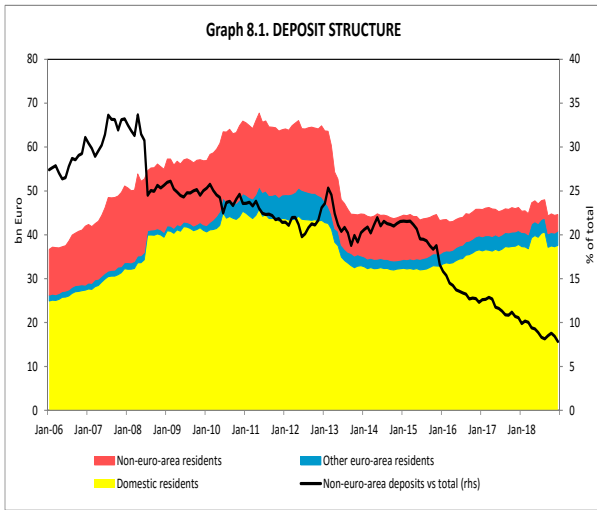
7. HOUSING



Note: According to the relevant modifications to the codification of the term "Alien" in the Land Information System, the way the statistics are presented has been modified. Therefore, the suggestion of the Department of Lands and Surveys is to avoid the comparison of the specific data from 2018 onwards, with the data of the previous years.

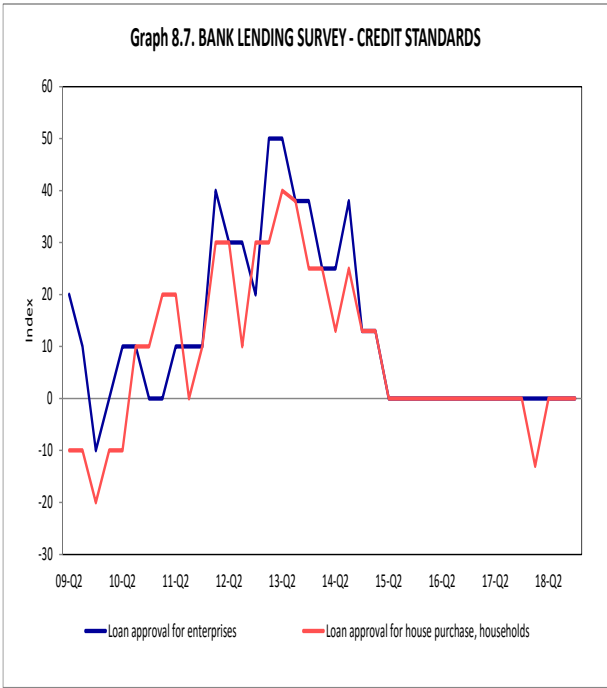
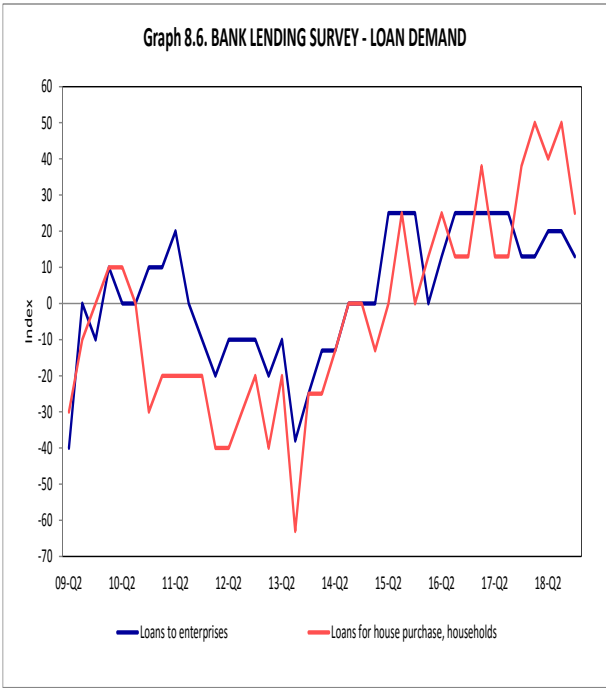
Sources: ECB, CBC, Dep. of Lands and Surveys

8. FINANCIAL SECTOR



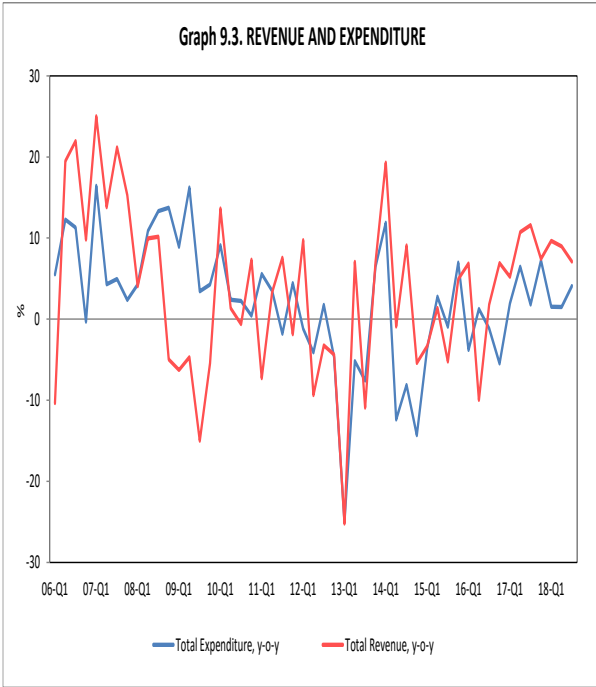
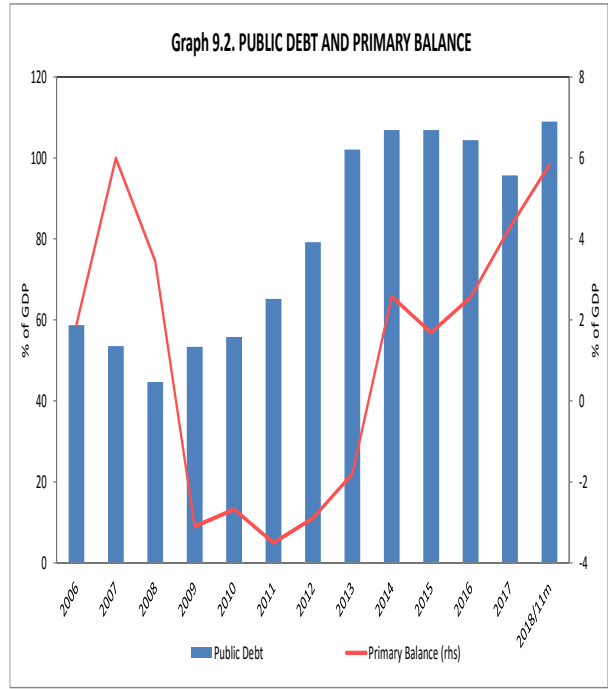
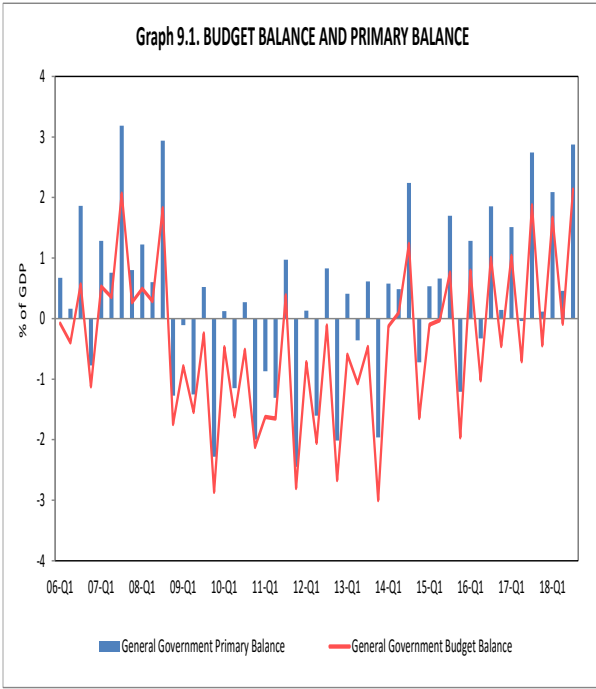
Sources: ECB, CBC, Bloomberg

8. FINANCIAL SECTOR – CONT.



Source: ECB

9. PUBLIC SECTOR



Sources: Ministry of Finance, Cystat