

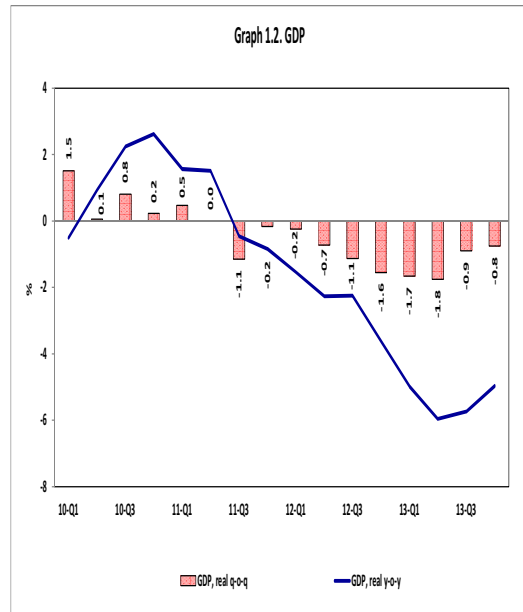
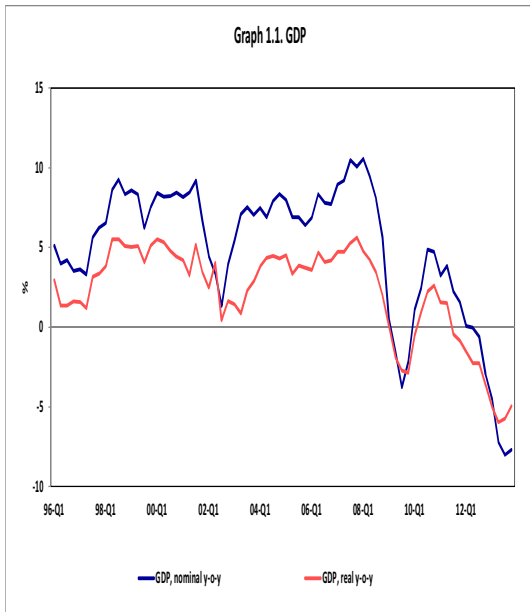
MACROECONOMIC MONITOR OF CYPRUS

Updated on 21 March 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).
- The economic sentiment indicator by CypERC presents a less negative picture, as it increased by 1.4 points in February 2014 compared to January 2014, although still remaining at negative levels (see graph 1.3). Expectations in some sectors showed an improvement albeit from low levels.
- Exports of goods decreased by 8.6% in January 2014 compared to January 2013.
- In January-February 2014 tourist arrivals increased by 1.5% compared to the same period in 2013 (see graph 6.3). A decrease of 4.2% was recorded in arrivals from the United Kingdom and 13% decrease in arrivals from Greece, while an increase of 11.1% was recorded in arrivals from Russia.
- 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 Force Survey (LFS) unemployment, in monthly seasonally adjusted figures, increased significantly from 14.4% in January 2013 to 16.8% in January 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.
- 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 -1.3% in February 2014 compared to -1.6% in January 2014 and for 2014 so far it stands at -1.4% (see graph 5.1). Core inflation decreased at a rate of -0.4% in February 2014 (see graph 5.2). All subcategories of HICP presented a decrease except for restaurants and hotels, communication, transport, clothing and footwear and alcoholic beverages and tobacco which presented an increase.

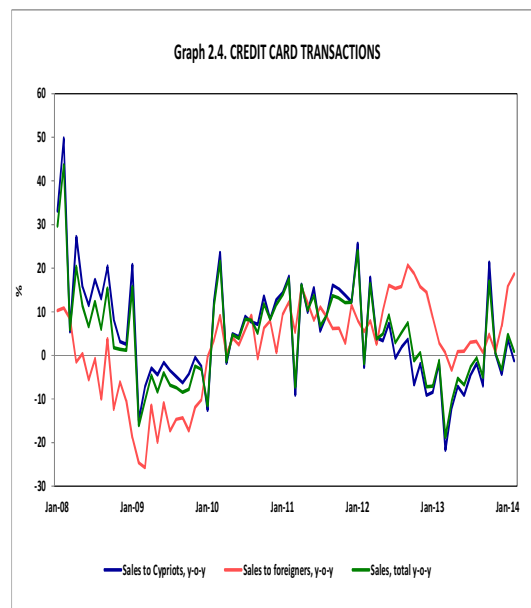
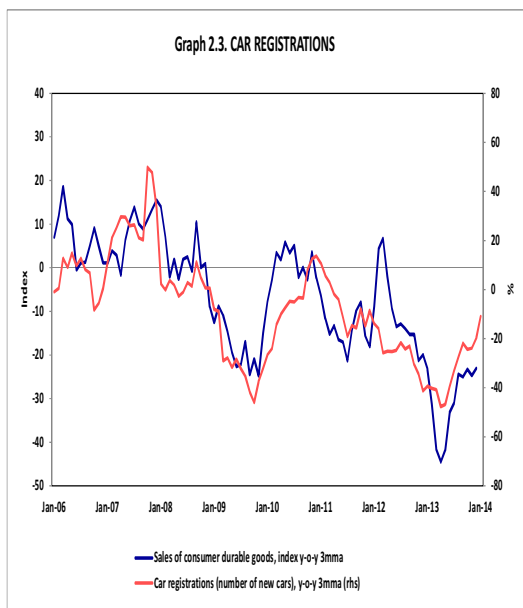
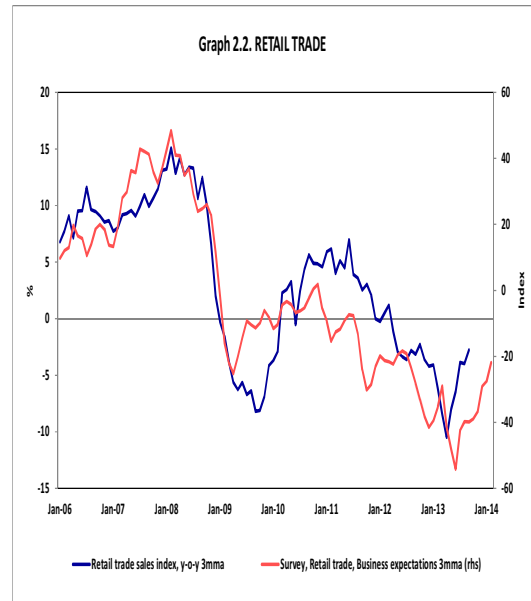
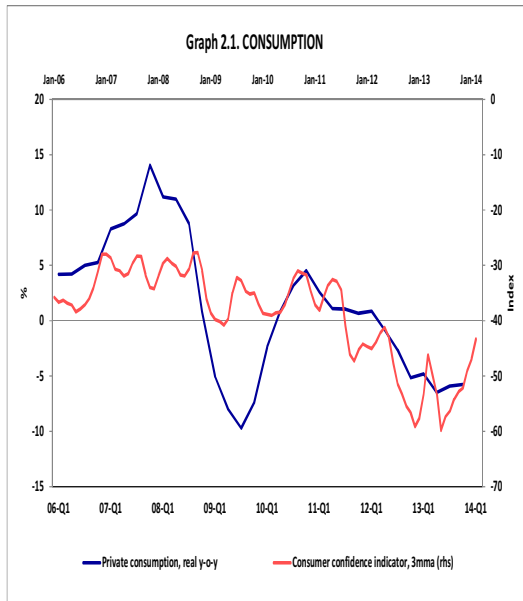
- The current account balance in the first nine months of 2013 was in surplus of €34,2 mn compared with a deficit of €765 mn in the first nine months of 2012 (see graph 6.4). This development was mainly due to the improvement of the goods account.
- The income account recorded a deficit of €162,9 mn in the first nine months of 2013 compared with a higher deficit of €223,7 mn in the first nine months 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 September 2013, reaching €15.753 mn compared with €17.126 mn in June 2013, thus remaining in a net liability position (Cyprus' liabilities exceed the respective assets). This development was due to the improvement recorded in direct investment and to a lesser extent, in portfolio investment, in spite of the deterioration recorded in other investments.
- In January 2014, the budget balance (on a cash basis) recorded a surplus of €144,6 mn (0.92% of GDP) compared to a surplus of €61,4 mn (0.37% of GDP) in January 2013. It is premature to draw any conclusions due to a series of imponderable factors.
- Monetary Financial Institutions (MFI) loans to domestic residents (private sector), declined with an annual rate of 6.9% in January 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 14.7% in January 2014, reflecting the negative climate of confidence (see graph 8.1). During the last three months though there is a deceleration in the fall.
- 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 January 2014, deposit interest rates for maturity up to 1 year exhibited a small increase, whereas the rate for deposits up to 3 months decreased. The lending interest rates to households for house purchase exhibited a marginal decrease and the rate for other loans up to €1 mn for businesses exhibited a small decrease. The rate for bank overdrafts to non-financial corporations exhibited a small increase. 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 4th quarter of 2013 on an annual basis. Cumulative from the 1st 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 16.9% lower and property transfers were 1.5% higher in January-February 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 5.3% in January 2014 (see graph 7.2).
- The Cyprus Government bond spread compared to the German Government bond, decreased further in mid-March 2014 compared to February 2014 (see graph 8.6, yields refer to the bonds maturing in 2020).

1. OUTPUT



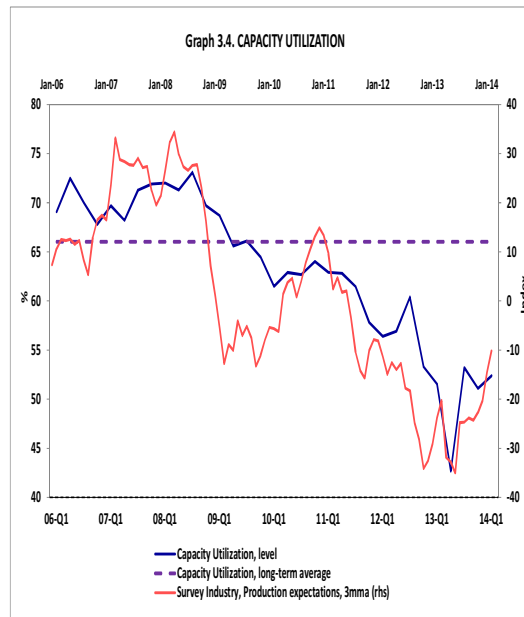
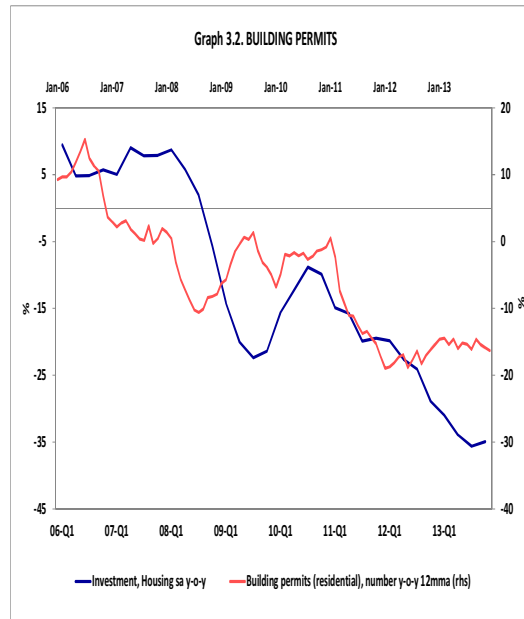
Sources: Eurostat, DG ECFIN, Cystat

2. CONSUMPTION



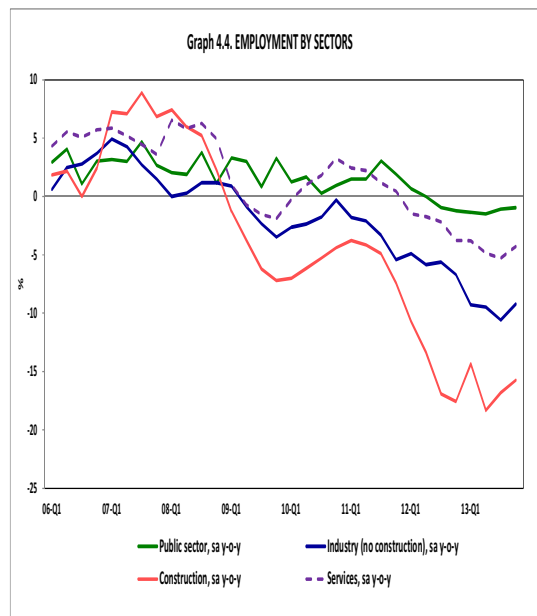
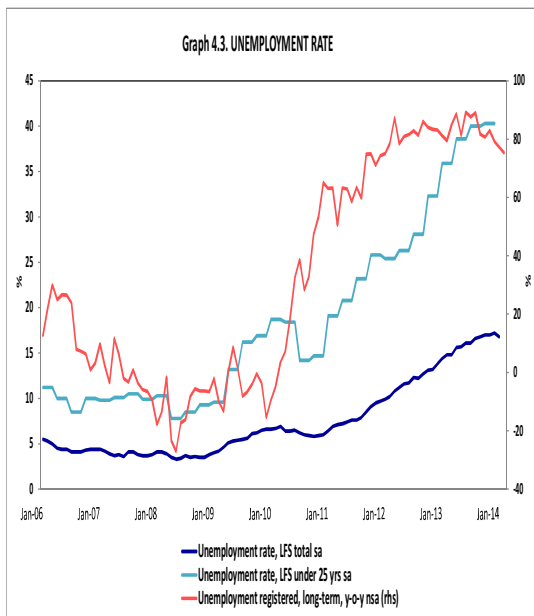
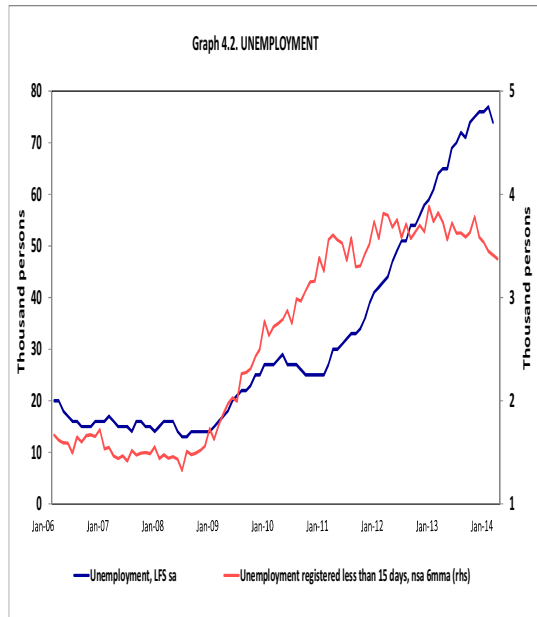
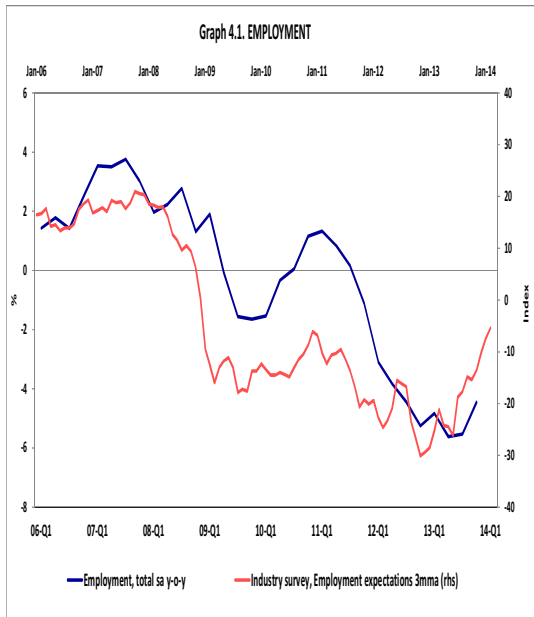
Sources: Eurostat, DG ECFIN, Cystat, JCC Payment Systems Ltd

3. INVESTMENT



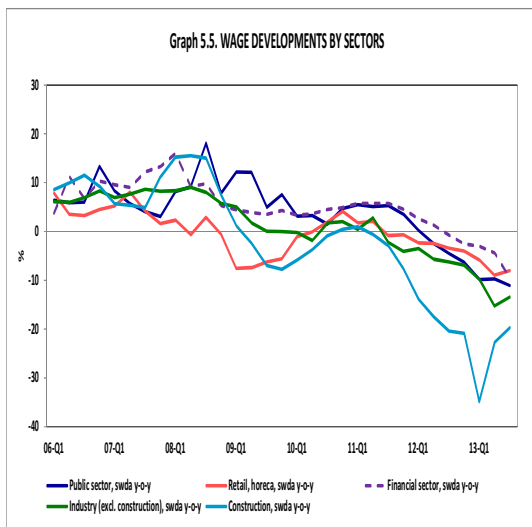
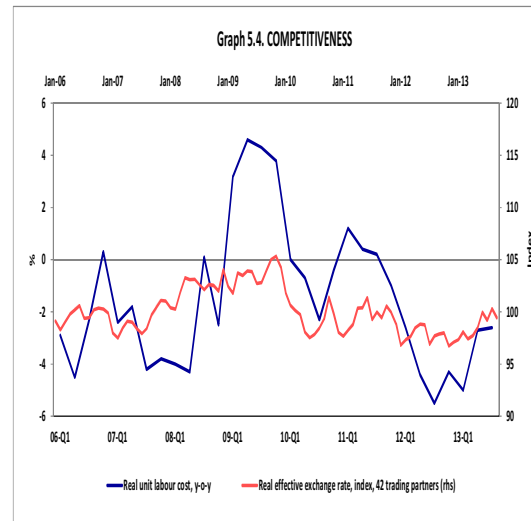
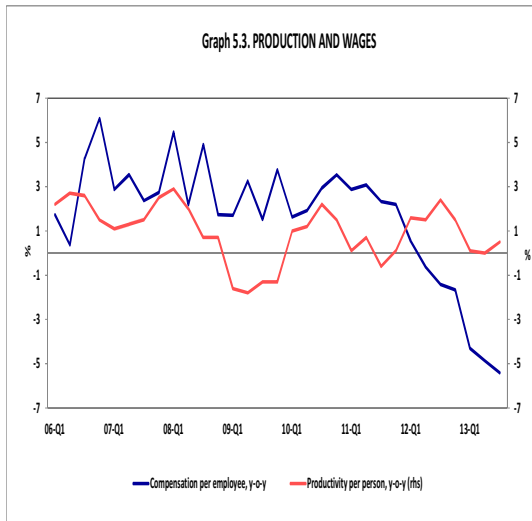
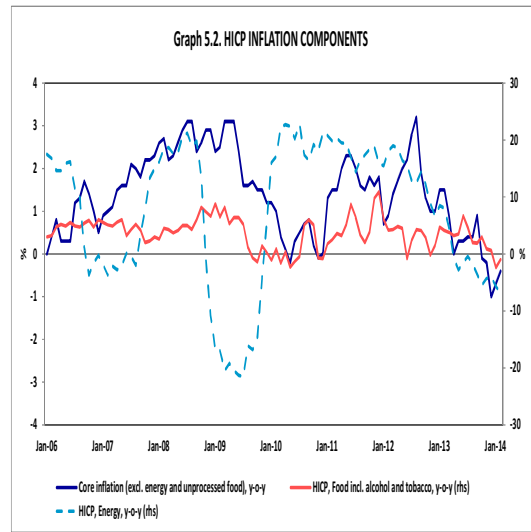
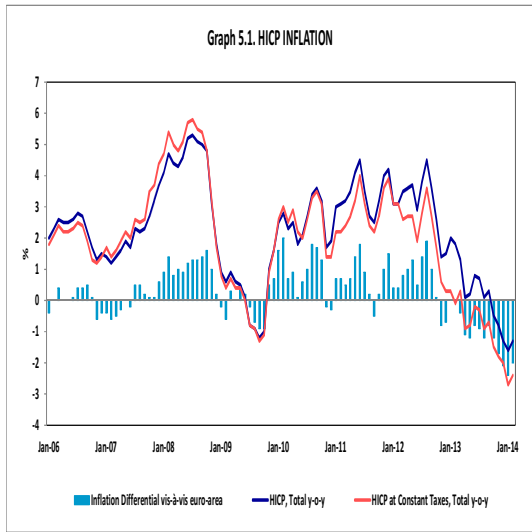
Sources: Eurostat, DG ECFIN, Cystat

4. LABOUR MARKET



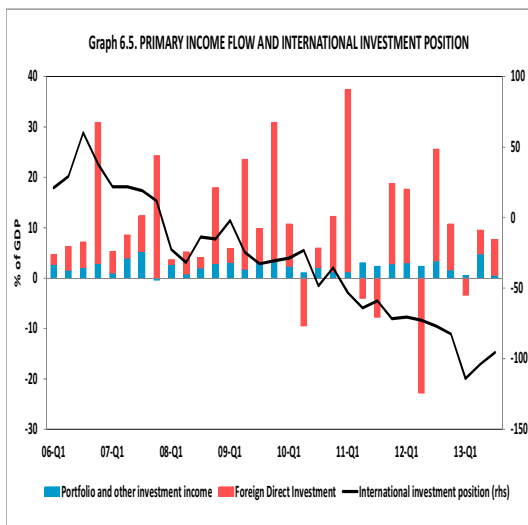
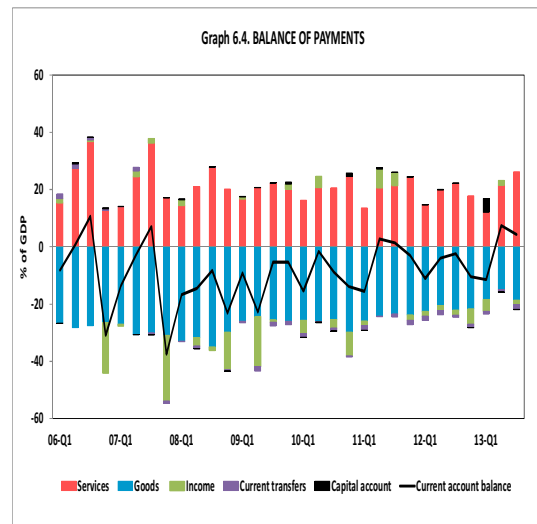
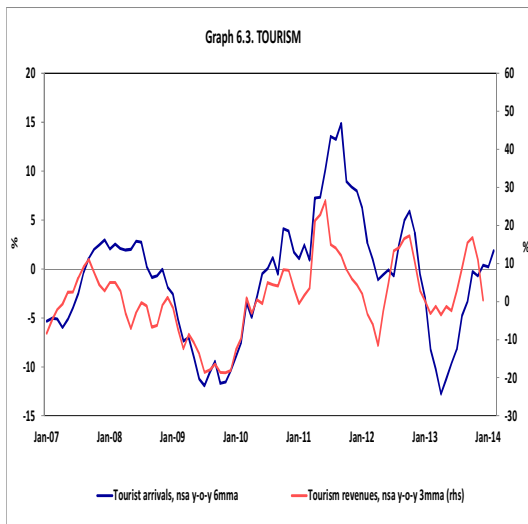
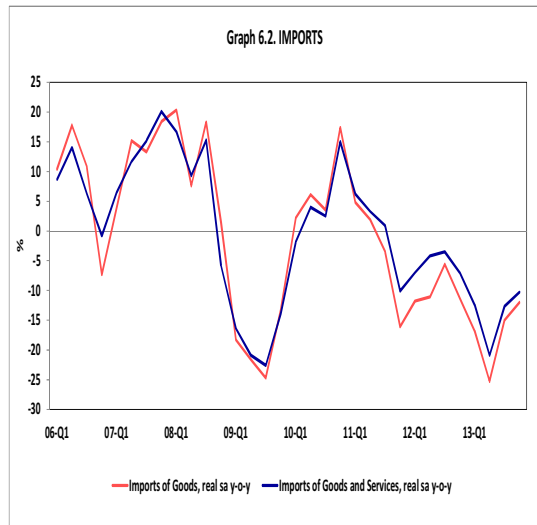
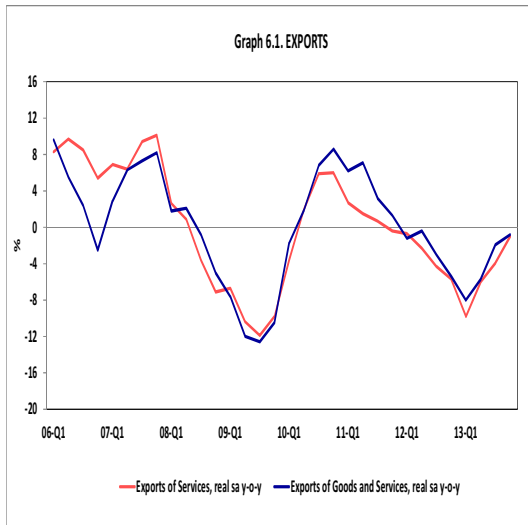
Sources: Eurostat, DG ECFIN, Cystat

5. INFLATION, WAGES



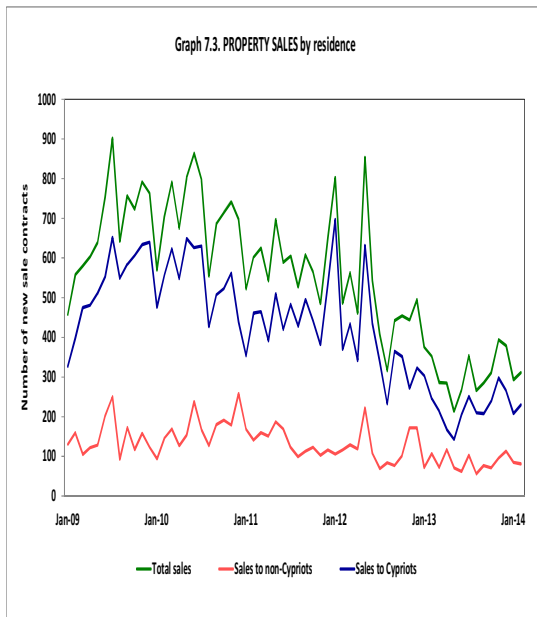
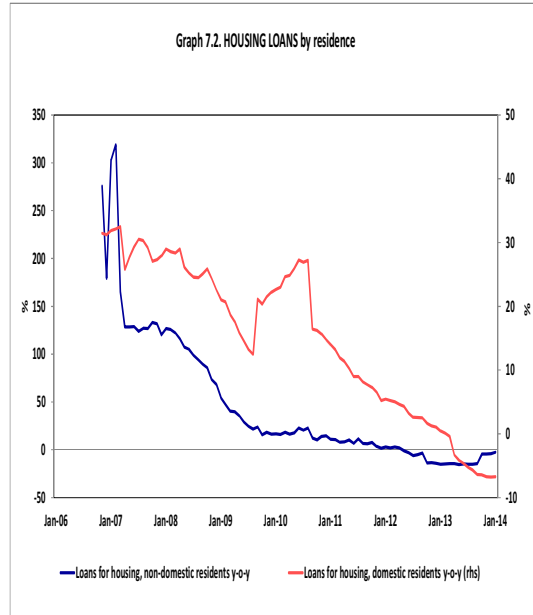
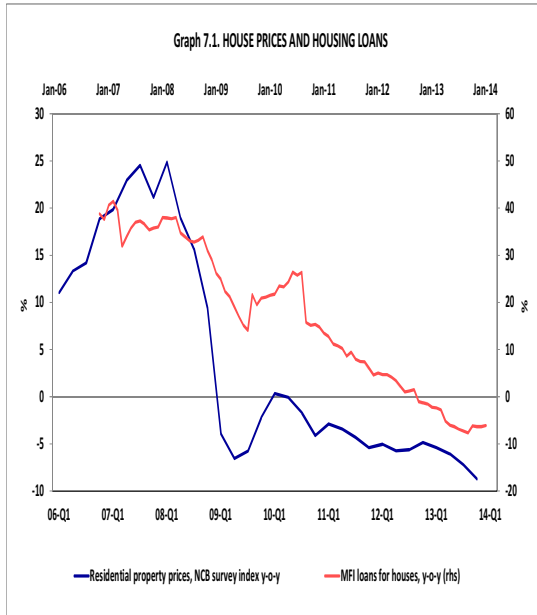
Source: Eurostat

6. EXTERNAL SECTOR



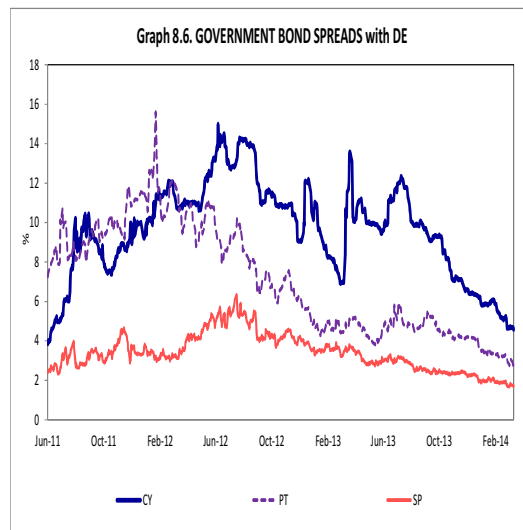
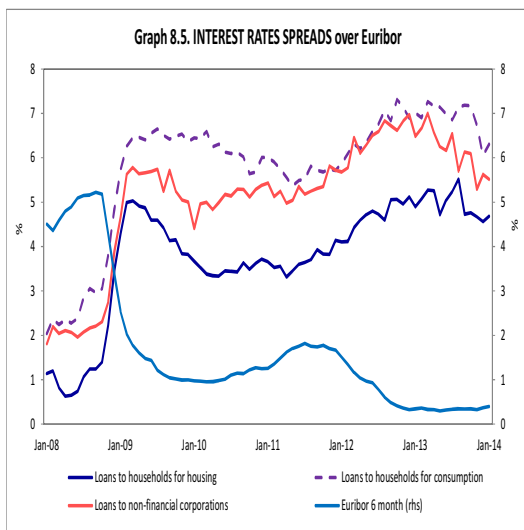
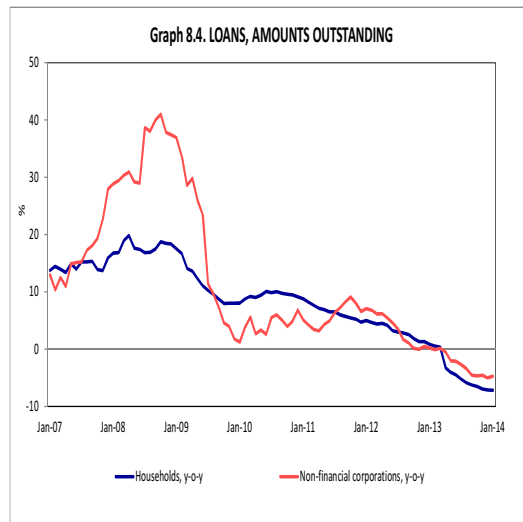
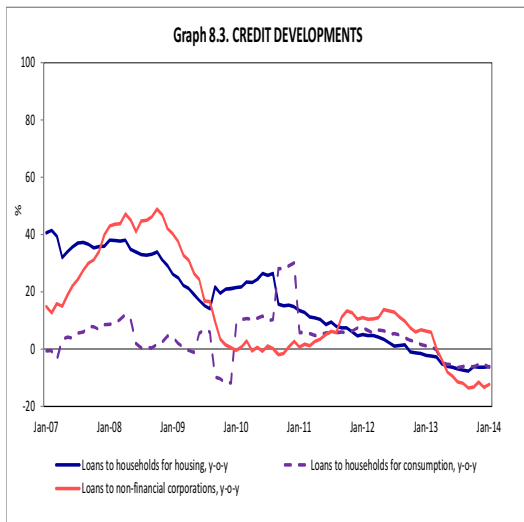
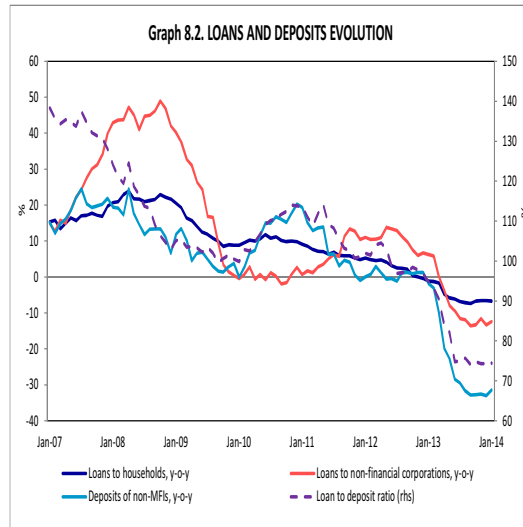
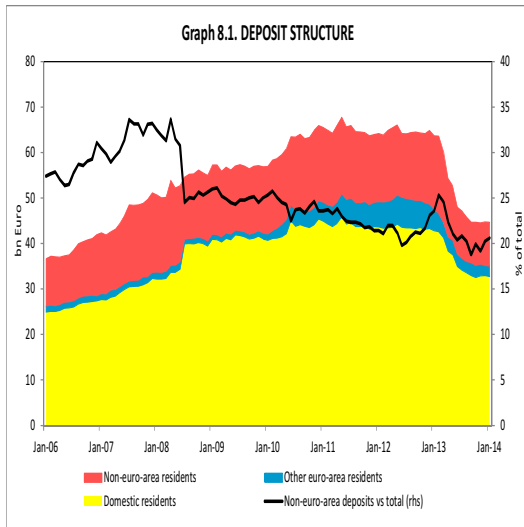
Sources: Eurostat, Cystat, ECB, CBC

7. HOUSING



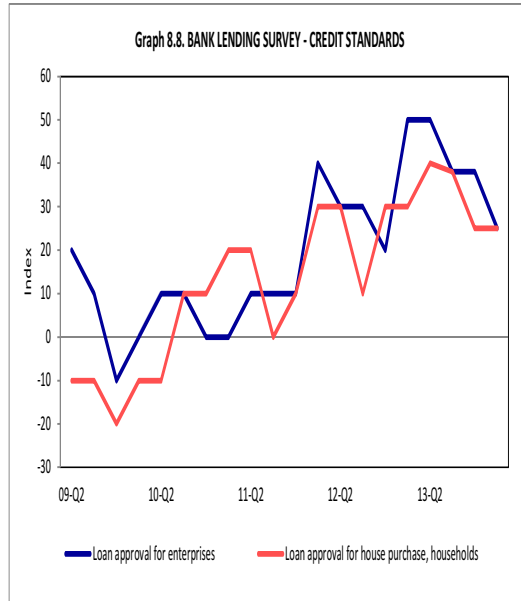
Sources: ECB, CBC, Dep. of Lands and Surveys

8. FINANCIAL SECTOR



Sources: ECB, CBC, Bloomberg

8. FINANCIAL SECTOR – cont.



Source: ECB