

Cyprus Economy Developments August 2018 Treasury and Correspondent Banking Department

Major recent developments in Cyprus

Cyprus Macroeconomic Developments

- Cyprus' Real GDP growth rate (seasonally adjusted) is positive and is estimated at 3.9% in the second quarter of 2018. It recorded a positive rate of growth of 4.0% in the first quarter of 2018. Growth is expected to reach 4.0% in 2018 and 4.2% in 2019 (IMF's June projections).
- Unemployment decreased to 8.2% in June 2018. It is expected to average at around 9.5% in 2018 and 8.0% in 2019 (IMF's June projections).
- Inflation (HICP) increased by 1.4% in July 2018 compared to July 2017. For the period January– July 2018, HICP recorded an increase of 0.2% compared to the correspondent period of the previous year. HICP is expected to be around 0.2% in 2018 and 1.0% in 2019 (IMF's June projections).
- Arrivals of tourists have recorded an increase of 9.6%, for the period January – July 2018, compared to the corresponding period of 2017.
- For January – May 2018, revenue from tourism is estimated at €677.2 million compared to €649.2 million in the corresponding period of 2017, recording an increase of 4.3%.
- In January – July 2018, property sales increased by 23.4% (5,366 property sales) compared to the corresponding period of 2017 (4,349 property sales). The highest number of property sales is recorded in Limassol (1,975 property sales). The highest percentage increase of property sales is recorded in Famagusta by 56.0%.
- The Residential Property Price Index (RPPI) of the Central Bank of Cyprus maintains a positive trend for the seventh consecutive quarter, recording a 0.6% increase in the 1st quarter of 2018 compared to the 4th quarter of 2017. On an annual basis, RPPI increased by 1.8% in the 1st quarter of 2018 (75.0 units) compared to the 1st quarter of 2017 (73.7 units).
- The Turnover Volume Index of Retail Trade for January – June 2018 is estimated to have recorded an increase of 7.6% compared to January – June 2017.
- In January – July 2018, the total registrations of motor vehicles increased by 17.3% to 30,373, from 25,896 in the corresponding period of 2017. Registration of new cars increased by 1.2% reaching 11,604 registered new cars, whilst the registration of used cars increased by 30.1% reaching 18,769 registered used cars.

Cyprus Fiscal Developments

Developments in public finances continue to exceed expectations.

- **General government budget balance (GGBB)**, also known as Fiscal Balance, stands at €514.7 million surplus (c. 2.6% of GDP) from January – July 2018 compared to a surplus of €217.2 million (1.1% of GDP) in January – July 2017.
- **General government primary balance (GGPB)**, also known as Primary Balance, during January – July 2018, GGPB stood at €828.1 million surplus (c. 4.2% of GDP) compared to a surplus of €547.5 million (2.9% of GDP) for January – July 2017.

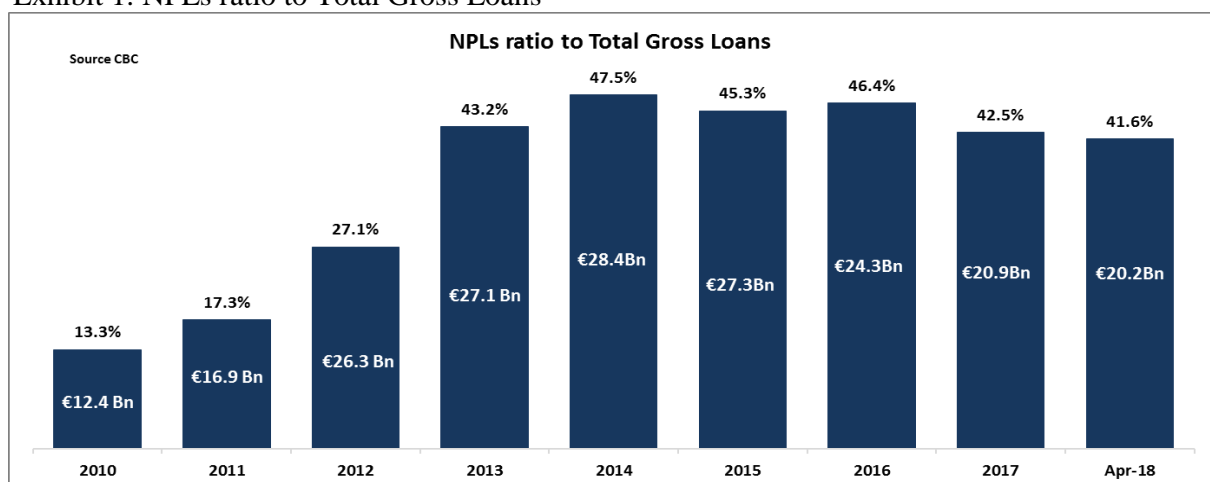
The General Government Debt reached €20.8 billion in June 2018 recording an increase over the end of the 2017 debt stock of €18.7 billion due to the bond issuance as part of the Cyprus Cooperative Bank-Hellenic Bank transaction. The debt to GDP ratio increased from 97.5% in 2017 to 108.5% as at the end of June 2018.

- Cyprus is rated “BB+” by S&P with positive outlook, “Ba2” by Moody’s with a stable outlook, “BB+” by Fitch with a positive outlook and “BB” by DBRS with a positive outlook.
- Latest Treasury Bills auction of 13-week duration with settlement date the 31st of August 2018 had an average yield of -0.24% and a bid to cover ratio of 1:2.0.

Banking Sector

- Deposits in the banking system amounted to €50.9 billion in July 2018 compared to €49.4 billion as at the end of 2017. The increase of deposits is mainly explained by the deposit of an amount of €2.5 billion by the Cyprus Government, with the Cyprus Cooperative Bank in April 2018, and an additional deposit of an amount of €0.8 billion in July 2018.
- Loans continue the downward trend. The outstanding amount of loans has decreased to €46.2 billion in July 2018 from €51.4 billion in December 2017.
- Restructurings were €11.5 billion at 31/03/2018 (€11.9 billion on 31/12/2017 and €13.5 billion on 31/12/2016). Data show that 68.0% of undertaken fixed-term loan restructurings abide by the new repayment schedule agreed as part of the restructuring.
- The outstanding amount of Cyprus banks on ECB’s Open Market Operations, amount to €0.83 billion in July 2018, down from its peak of €13.6 billion in September 2012.
- The NPLs (Exhibit 1) amounted to €20.2 billion as at April 2018 compared to €20.9 billion in December 2017 and €24.3 billion in December 2016. The Cyprus banking NPLs ratio has decreased from 42.5% as at end of 2017 to 41.6% as at April 2018.

Exhibit 1: NPLs ratio to Total Gross Loans



- Total New Lending for the period January – June 2018 compared to the period of January – June 2017 remained unchanged. Housing loans increased by 48.0%, consumption loans increased by 8.0%, whilst Corporation loans decreased by 13.0%. Total new lending for the period January – June 2018 amounts to €1,488.0 million compared to €1,483.0 million of the corresponding period of 2017. Detailed figures are illustrated in Table 1.

Table 1: New Loans (excluding renegotiation)

New Loans (excluding Renegotiation) Amounts in € millions	2009	2010	2011	2012	2013	2014	2015	2016	2017	Jan - Jun 2017	Jan - Jun 2018	%Δ Jan - Jun 2018/17
	Consumption Loans	1,273	764	693	547	267	89	78	112	169	80	86
Housing Loans	2,098	3,017	1,907	1,518	1,399	480	268	543	723	301	444	48%
Corporations Loans	4,953	4,398	3,734	3,253	3,122	1,414	1,158	1,479	2,143	1,102	958	-13%
Total	8,324	8,179	6,334	5,318	4,788	1,983	1,504	2,134	3,035	1,483	1,488	0%

Moody's upgraded Cyprus' credit ratings

Moody's Investors Services has upgraded by one notch the government of Cyprus long term issuer rating to Ba2 from Ba3, and the outlook has been changed to stable from positive. The upgrade puts Cyprus two notches below investment grade. According to Moody's, the upgrade of Cyprus 'ratings to Ba2 from Ba3 is driven by a number of factors, such as the ongoing recovery of Cyprus 'banking system, in the context of which the liquidation of Cyprus Cooperative Bank Ltd (CCB) via the sale of its healthy assets and liabilities has materially reduced systemic risks emanating from the banking sector. Also from the positive fundamental trend with respect to the government's balance sheet, based on robust nominal growth and a primary surplus, irrespective of the one-off related to the recent CCB transaction. The stable outlook on Cyprus' Ba2 ratings balances the country's strong fiscal dynamics against pressures for higher public expenditure. It also reflects uncertainty around the extent to which new legal tools will enable a material decline in the banking system's non-performing loans (NPLs) ratio.

Country-specific recommendations (CSRs) for economic policies under the 2018 European Semester (ECB Publication, August 2018)

The EU governance framework provides guidance to individual EU Member States on how to address structural reform needs and macroeconomic imbalances in the following 12-18 months. According to the latest ECB's publication, Cyprus (along with Italy) is identified as a member state with excessive imbalances (Appendix 1, Chart on 2018 CSR on euro area countries).

The chart shows the number of 2018 CSRs for euro area countries broken down into broad policy areas. 'Fiscal-structural' comprises mainly public administration, age-related public spending and taxation. 'Framework conditions' comprises mainly judicial systems, insolvency frameworks, housing, financial sector, and research and innovation. 'Labour market' comprises mainly wages and wage-setting, employment protection, education and active labour market policies. 'Product market' comprises mainly sector-specific regulations and barriers to market entry.

Bank of Cyprus Holdings' Announcement, 28 August 2018

Bank of Cyprus Holdings Public Limited Company has reached an agreement for the sale of a portfolio of loans with a gross book value of €2.8 billion (of which €2.7 billion relate to non-performing loans) secured by real estate collateral.

The Portfolio has a contractual balance of €5.7 billion. The net book value of the assets being sold as at 30 June 2018 amounted to €1.5 billion before the impact of the Transaction on the 2Q 2018 income statement. At completion, the Bank will receive gross cash consideration of c. €1.4 billion. The Portfolio comprises 14,024 loans to corporate and SME borrowers, secured over 9,065 properties.

The completion of the transaction remains subject to a number of conditions precedent, including mainly regulatory and other approvals, and the ECB agreeing to a Significant Risk Transfer benefit from the Transaction.

Table 2: Major Macroeconomic Indicators: 2017 Actual Figures, 2018/19/20 Projections

	2017 (Actuals)	2018 (Projections)*	2019 (Projections)*	2020 (Projections)*
<i>Real GDP</i>	3.9%	4.0%	4.2%	3.4%
<i>Consumer Prices</i>	0.7%	0.2%	1.0%	2.2%
<i>Unemployment</i>	11.1%	9.5%	8.0%	7.0%
<i>Debt to GDP**</i>	97.5%	106.1%	97.8%	89.9%
<i>General Government Balance</i>	1.9%	2.1%	2.1%	1.7%
<i>General Government Primary Balance</i>	4.5%	4.5%	4.5%	4.1%

* IMF's June 2018 Projections

** Prior to the expected issuance of €1.0 billion for CCB

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Appendix 1: Graphical presentation of the key Cyprus Economy figures.

