

Republic of Cyprus



Investor Presentation

July 2019

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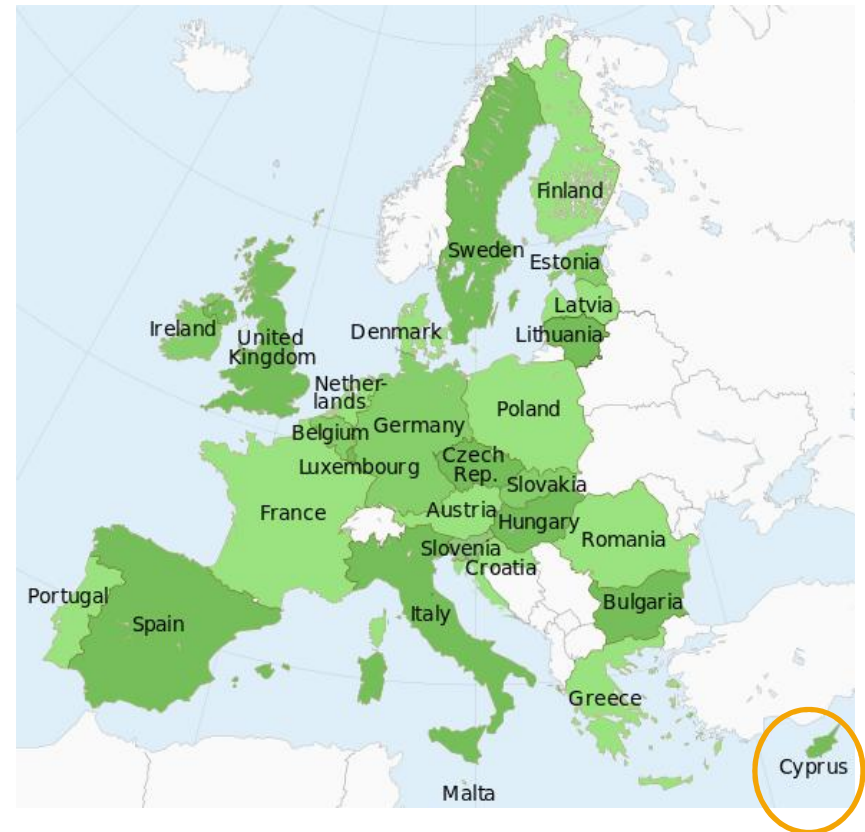
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The Republic of Cyprus

Key facts

- **Political system:** Presidential Democracy
- **Legislature:** House of Representatives
- **Population:** 956.800 (est. 2017)
- **Geographical size:** 9.251 km²
- **Currency:** Euro
- **GDP per capita in PPS¹:** 87% of EU-28 (2018)
- **Human Development Index:** 32nd out of 189 (HDR², 2017)
- **Main economic sectors:**
 - Services (84% of GVA³ in 2018): business and financial services, tourism, shipping, real estate, retail trade
 - Industry (14% of GVA in 2018): manufacturing of pharmaceutical and food products, construction
- **International memberships:** EU, Eurozone, Council of Europe, United Nations, IMF, World Bank, Commonwealth, World Trade Organisation et al.



Source: Cyprus Statistical Service, Eurostat, United Nations

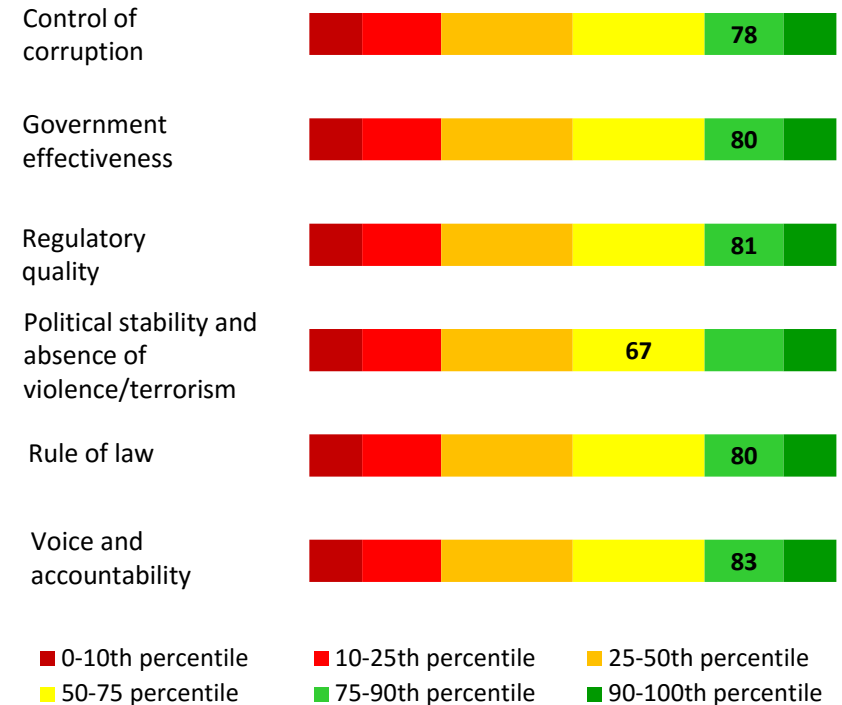
Notes: 1. Purchasing Power Standards ; 2. Human Development Report ; 3. Gross Value Added



Strong institutional framework and effectiveness

- Cyprus is in upper range of Worldwide Governance Indicators of the World Bank.
- The Republic of Cyprus has a presidential system of government with divisions of authority in the executive, legislative and judicial branches. The constitution vests executive power in a president who is elected for five years. Legislative power is exercised by the House of Representatives and judicial power lies with the courts.
- Next scheduled elections: Parliamentary (2021), Local (2021), Presidential (2023).
- Government effectiveness shown by track record of correction of imbalances with swift improvement of public finances in the years 2006-2008 and 2013-2015.
- Cyprus' legal system is modelled on the English legal system and European Law; also practises Common Law.

Worldwide Governance Indicators for Cyprus (2017)



Source: The World Bank



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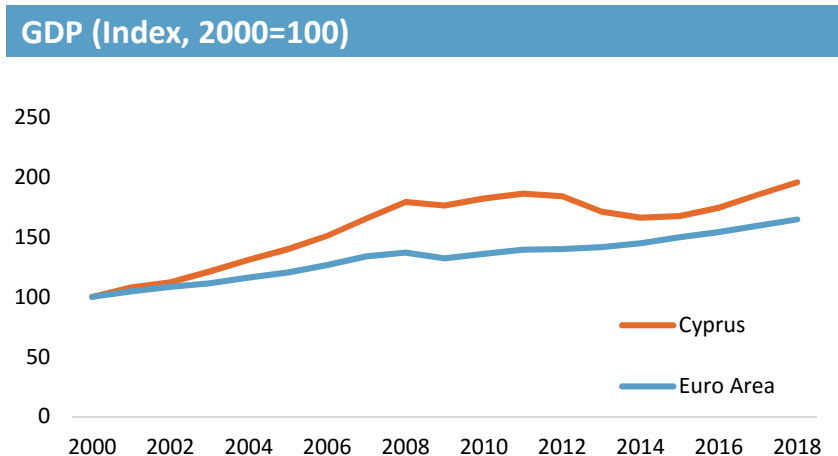
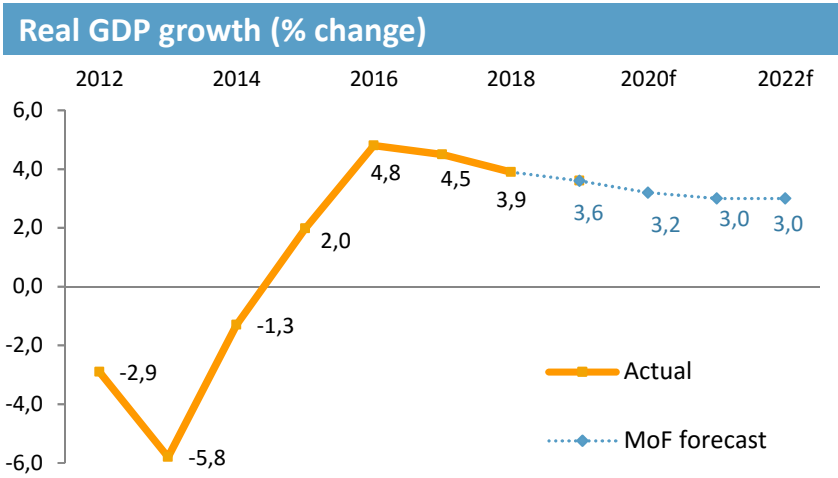
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Solid near-term growth outlook

- Growth momentum of recent years continued over 2018 at a rate of 3,9% and Q1-2019 of 3,4%. Economic growth remains strong despite deceleration attributed to a less favourable external environment.
- Growth is broad-based and derives from higher demand in the sectors of tourism, construction, business services and retail trade. The positive developments are partly attributed to the gains in price competitiveness recorded in recent years. The only sector recording negative growth rate is financial services due to its deleveraging.
- On the expenditure side, consumption has been the main driver attributed to higher employment level and disposable incomes. Additionally, mainly foreign-financed private investment has boosted growth with high value added projects in the tourism, energy and education sectors.



Source: Cyprus Statistical Service, Ministry of Finance

Note: "f" denotes forecasts by the Ministry of Finance, as of April 2019. All forecasts are based on assumptions and there can be no assurance they will be realised.



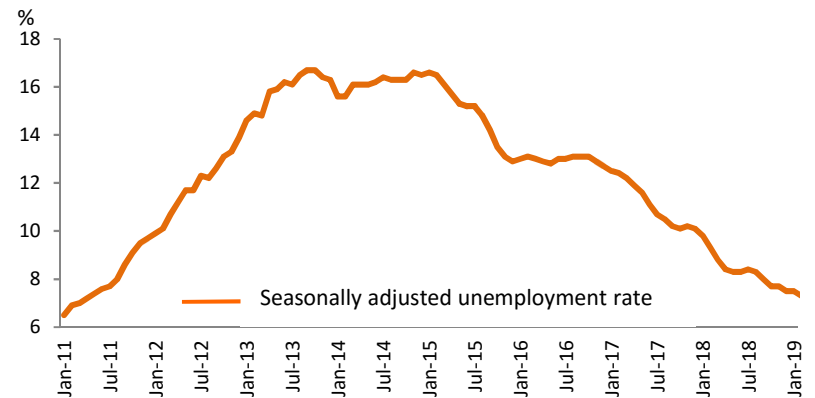
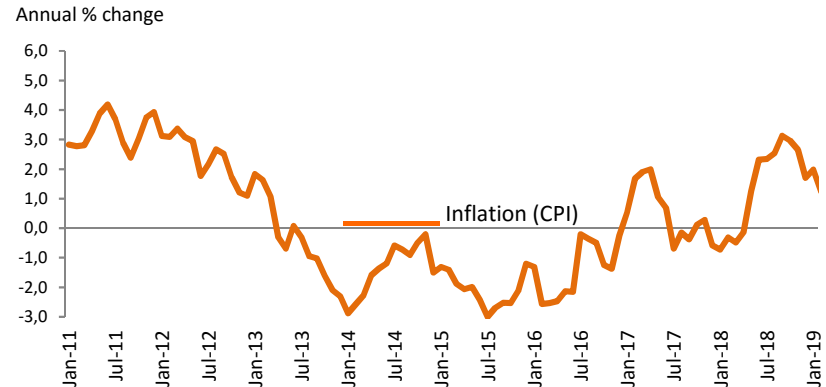
Moderate inflation and rapid reduction in unemployment

Low inflationary pressures

- Subdued inflationary pressures despite growth owing to exogenous factors. CPI inflation at 1% in the first half of 2019 with core inflation excluding energy and seasonal food at 0,3%. Respective figures in 2018 were 1,4% and 0,4%.
- Fast correction during crisis years reflecting the wage flexibility of the labour market which led to an internal devaluation and improvement in price competitiveness.

Rapid decline in unemployment

- Labour Force Survey unemployment in monthly seasonally adjusted terms decreased to 6,5% in May 2019 compared to 8,3 % in May 2018.
- Flexibility of labour market and strong economic activity contributing to normalization of labour conditions.
- Encouraging signs of de-escalation in youth unemployment while long-term unemployment is correcting faster than total.



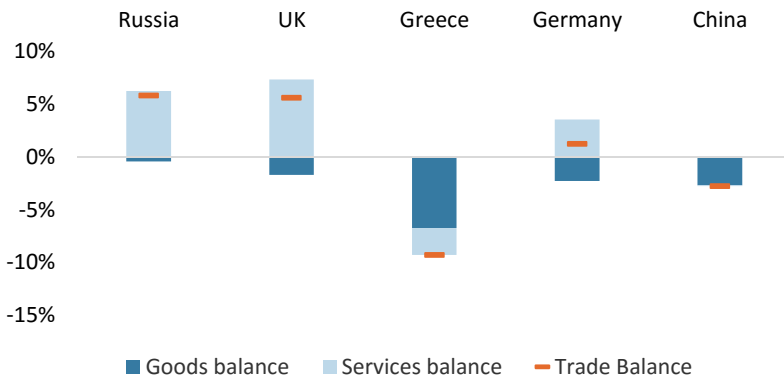
Source: Cyprus Statistical Service, Eurostat



Moderate current account deficits

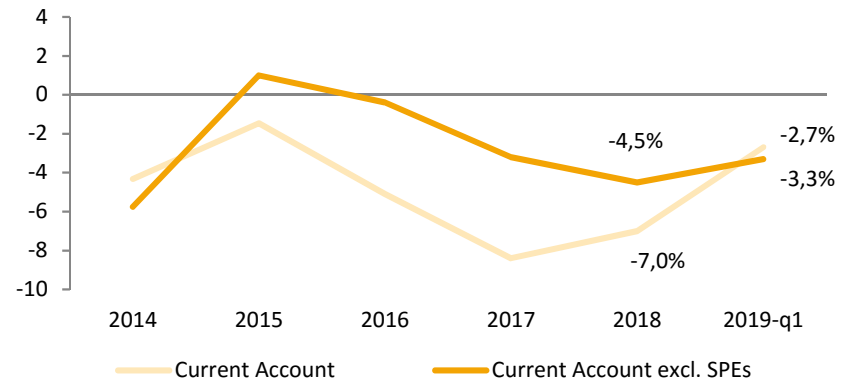
- Cyprus presents small to moderate current account deficits, within sustainable levels
- Companies statistically registered as Special Purpose Entities (SPEs) in Cyprus, have strong balance sheets relative to the size of the economy but minor real economic activity in the domestic economy. Exclusion of SPEs provides a more accurate picture of the external position.

Main trade partners (% of GDP) ¹

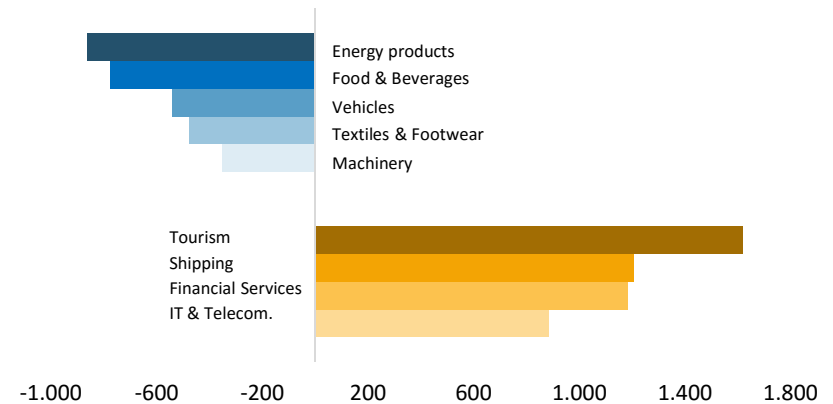


Source: Central Bank of Cyprus, Cyprus Statistical Service, Eurostat
 Notes: ⁽¹⁾ Based on 2017 figures

Current account balance (% of GDP)



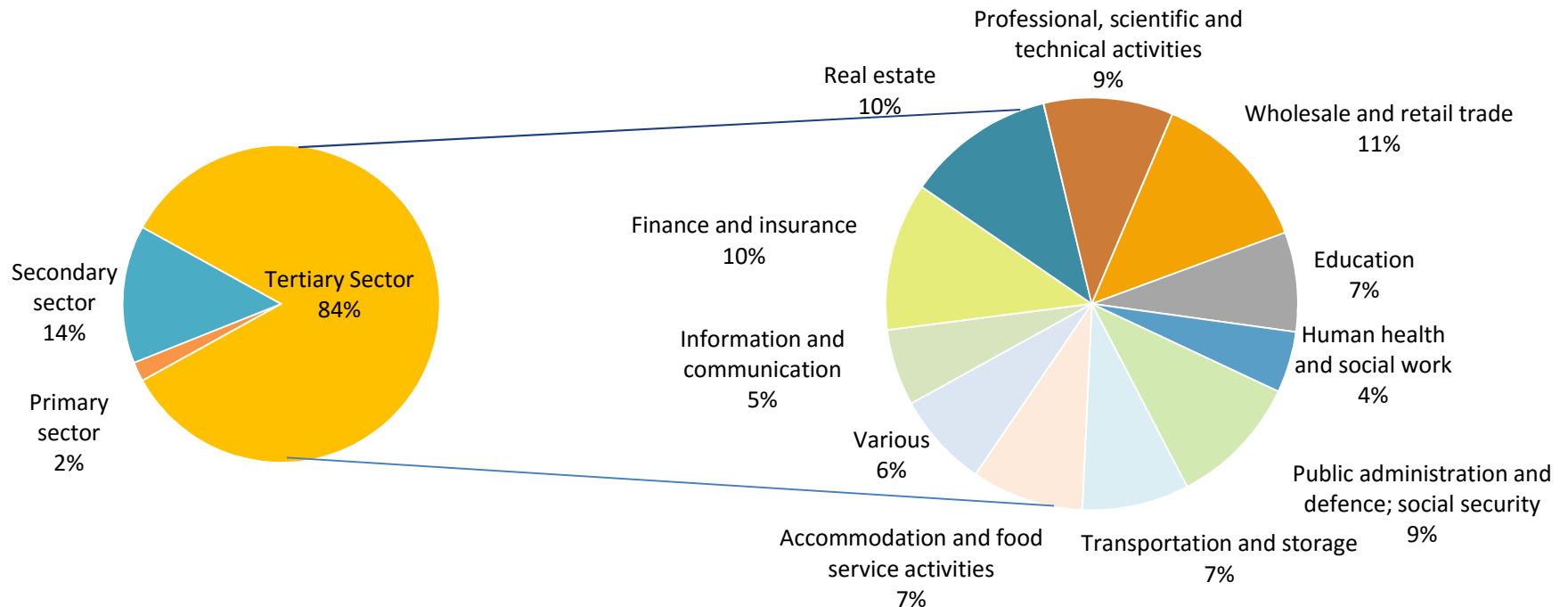
Trade balance, EUR mn



A diversifying service-based economy

Whilst financial-business services, tourism and shipping services have been traditionally the main sectors of Cyprus, the economic activity has recently diversified in IT& Telecoms and pharmaceuticals manufacturing

Structure of Economy in 2018 (Current prices, % of GVA)



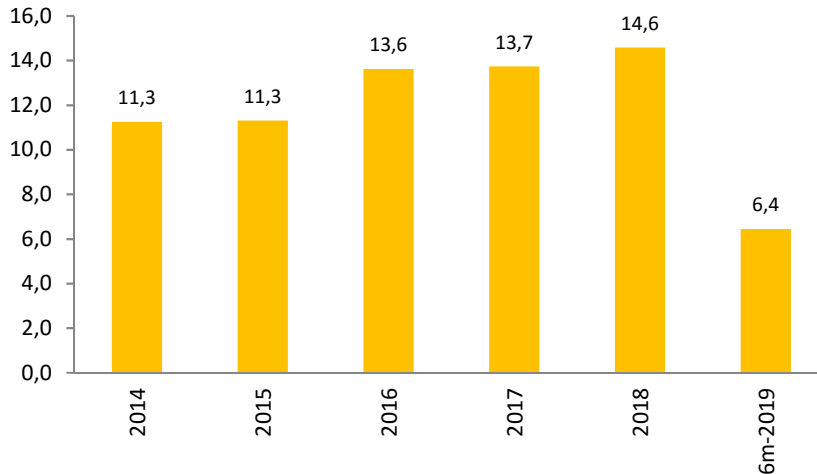
Source: Cyprus Statistical Service



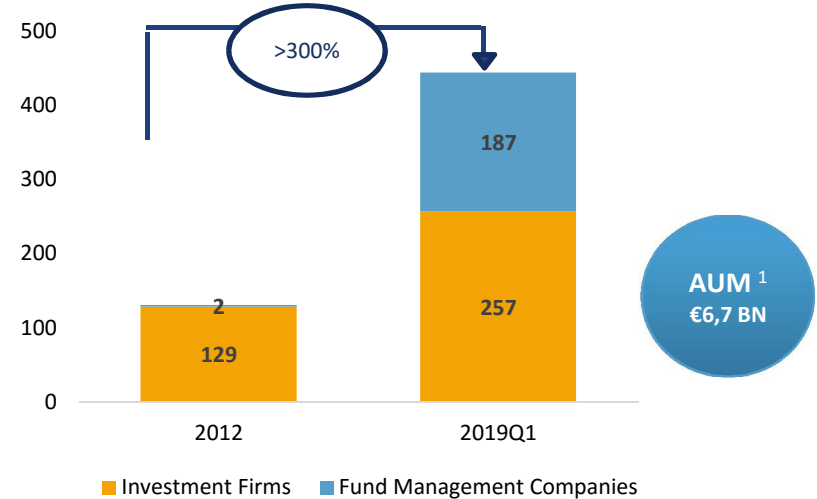
Significant international business activity

Competitive advantages in business and financial services

Registration of new companies, thousand



Investment Firms and Fund Management



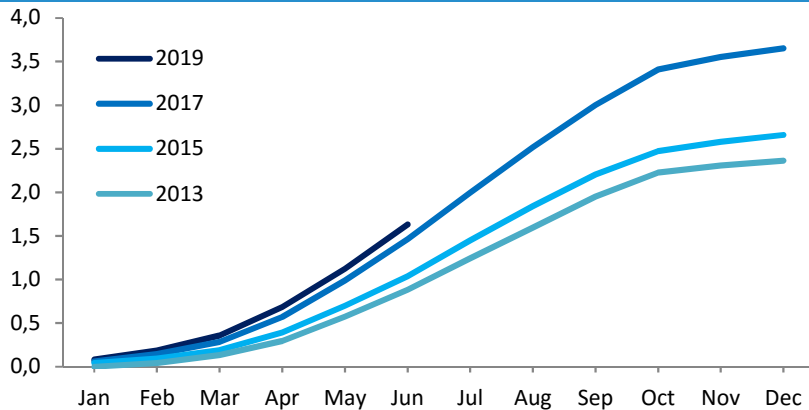
- Cyprus is a regional Business and Financial Services Centre with strong regulation and supervision and a reliance on a well balanced portfolio of services.
- Cyprus maintains a modern, consistent and simple tax system with a broad tax base, limited exceptions or credits, and low tax rates and a significant network of Agreements for Avoidance of Double Taxation (65 as of today). Cyprus is a Common Law country and has a well-developed professional services industry with more than 20 years presence in the international financial markets and over 500 organisations supporting international business.

Source: Department of Registrar of Companies and Official Receiver, Cyprus Securities and Exchange Commission. Note 1: Assets Under Management

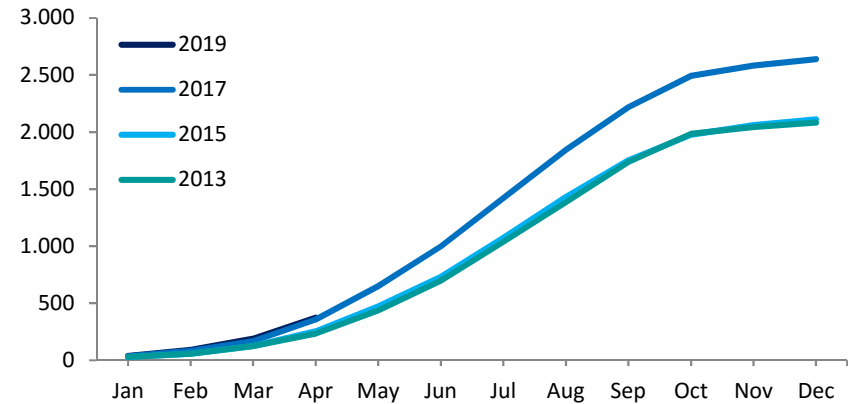


Tourism: a long-standing contributor in economy

Tourist arrivals, million



Revenues from tourism, EUR million



- Arrivals and revenues in the first months of 2019 at similar levels as the respective period of 2018.
- Arrivals in 2018 reached an all-time record of 4 million persons. Efforts to enhance the tourism sector including through prolonged seasonality period and better flight connectivity contributed to the increase in inbound tourism.
- The origin of tourists has diversified over time with tourists from the UK representing 34% of arrivals in 2018, down from 56% of arrivals in 2005. The second largest origin market in 2018 was Russia with 20% of arrivals.
- Revenues have increased at a lower rate than the increase in arrivals due to travel characteristics such as length of stay and forms of travel eg. all-inclusive packages.

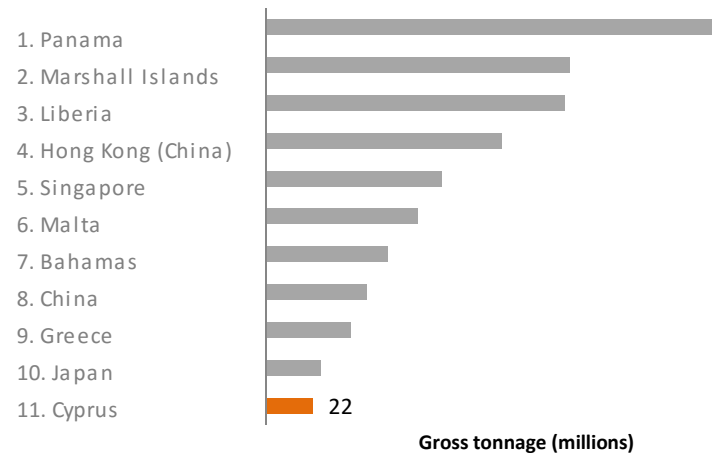
Source: Cyprus Statistical Service



An internationally renowned shipping centre

- Cyprus has a strong maritime tradition and has combined strong geographical, institutional and commercial advantages to become:
 - ❖ A leading Ship Registry (IHS Maritime & Trade, World Fleet Statistics 2017)
 - ❖ One of the largest third party ship management centres worldwide
 - ❖ Home to a total of around 60 ship management companies operating from Cyprus, including leading names in the global shipping industry.
- Cyprus was the first “Open Registry” with an EU-approved Tonnage Tax regime, which covers the three main maritime transport activities: ship owning, ship management (crew and technical management), and chartering.
- The size of the ship management sector in terms of turnover represented 5% of GDP in 2018.

World merchant fleet size by flag, 2017



Source: Deputy Ministry for Shipping, Central Bank of Cyprus, IHS

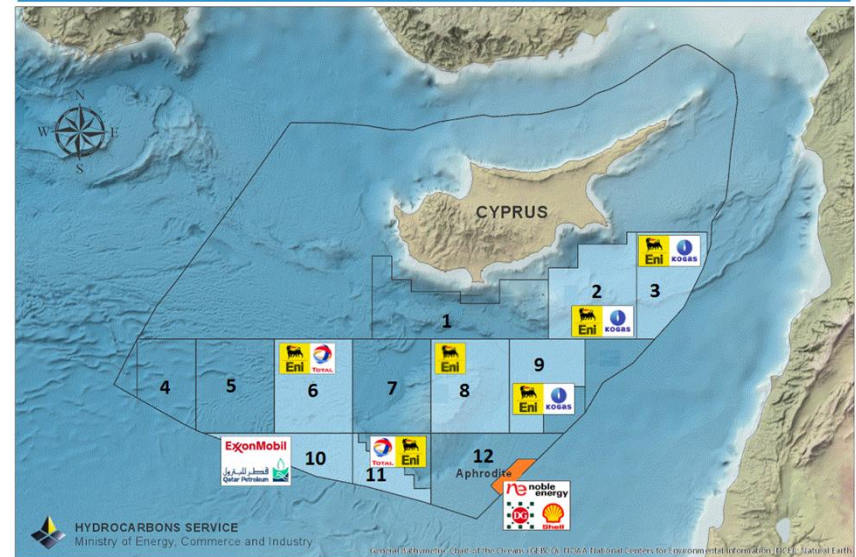


Natural Gas Exploration and Exploitation

Prospects for Cyprus as an energy producer and exporter

- Noble Energy International announced **the first natural gas discovery (“Aphrodite”)** in Block 12 in January 2012, which was declared commercial in 2015. Current estimated natural gas resources are in the order of **4,5 trillion cubic feet** (best estimate). The regional pipelines option seems to be the optimal monetization alternative, under the current economic and commercial conditions.
- The “Aphrodite” field project opens up **new investment opportunities, including a subsea pipeline connecting Cyprus and Egypt**. An Intergovernmental Agreement between Cyprus and Egypt has been signed.
- The Noble Energy International / BG Cyprus / Delek Drilling consortium is working on the development of the “Aphrodite” gas field.
- Other discoveries are: **“Glaucus-1”** in Block 10 by ExxonMobil/QP for which preliminary estimates are of **5 trillion to 8 trillion cubic feet**; “Onesiphoros West 1” in Block 11 by TOTAL/ENI (technical discovery), and “Calypso-1” in Block 6 by ENI/TOTAL under evaluation.

Offshore exploration licenses of Republic of Cyprus



- In 2017 exploration licences were awarded to ENI / TOTAL for Block 6; ENI for Block 8 ; and ExxonMobil / Qatar Petroleum for Block 10. Other active exploration licences are held by ENI/KOGAS for Blocks 2, 3 and 9 and by TOTAL / ENI for Block 11.



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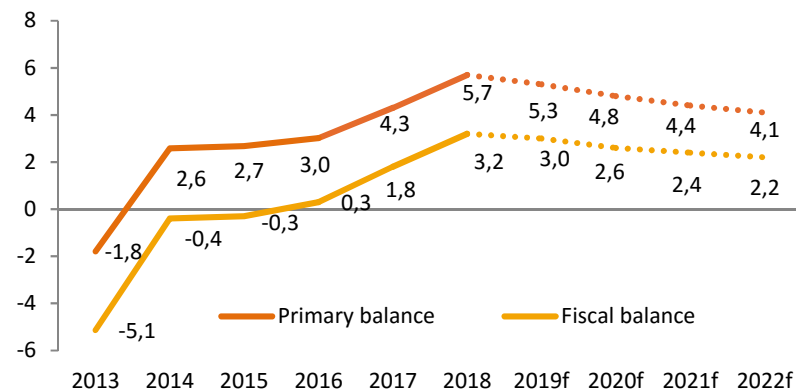
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Public finances in a solid surplus position

- The government policy is for a growth-friendly fiscal stance safeguarding the maintenance of robust primary surpluses supporting a sustained reduction of public debt. The budget reflects a continuation in the employment policies adopted by the government and places emphasis on reallocation of expenditure towards growth-enhancing activities.
- Since 2016 the fiscal position is positive peaking at 3,2% surplus in 2018. In the next years both government revenue and government expenditure are expected to increase primarily due to the introduction of the national health system. The budget surplus is expected to fall marginally mostly due to increased expenditure associated with the gradual abolition of wage cuts.
- The budget is designed to achieve the medium term objective of a balanced fiscal position in structural terms.

Evolution of main fiscal indicators, % of GDP



Source: Ministry of Finance

Note: The budget outcomes of 2014-15 and 2018 exclude government contributions for the Cyprus Cooperative Bank

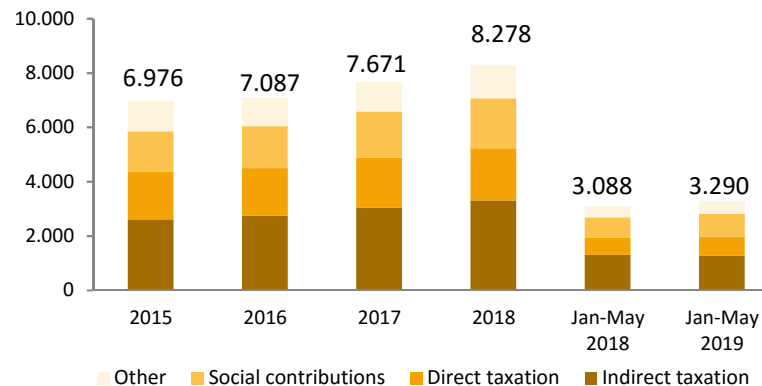
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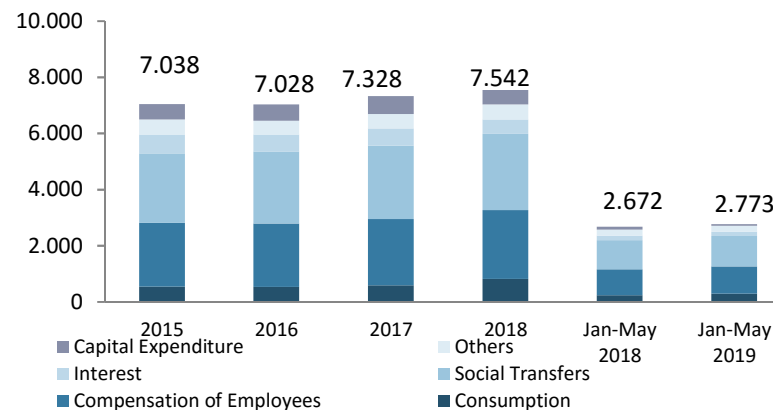
Strong fiscal performance continues during early 2019

- During Jan-Apr 2019 the fiscal position continued to be in surplus at 2,5% of GDP compared to 2,0% of GDP of the corresponding period of the previous year.
- Government budget was in surplus in 2018 at 3,2% of GDP compared to 1,8% the year before.
- The revenue side increased by 7,7% vis-à-vis the corresponding period of 2017. This improvement can be attributed to higher income tax receipts reflecting primarily indirect tax revenue and secondarily, tax revenue on income and wealth.
- The expenditure side increased at a rate of 2,3% vis-à-vis 2017. An increase was recorded in compensation of employees, attributed to higher employment in education, health and security sectors. Intermediate consumption increased mostly due to expenditure relating to water supply and pharmaceuticals.

Budget revenue breakdown, EUR million



Budget expenditure breakdown, EUR million



Source: Cyprus Statistical Service, Ministry of Finance

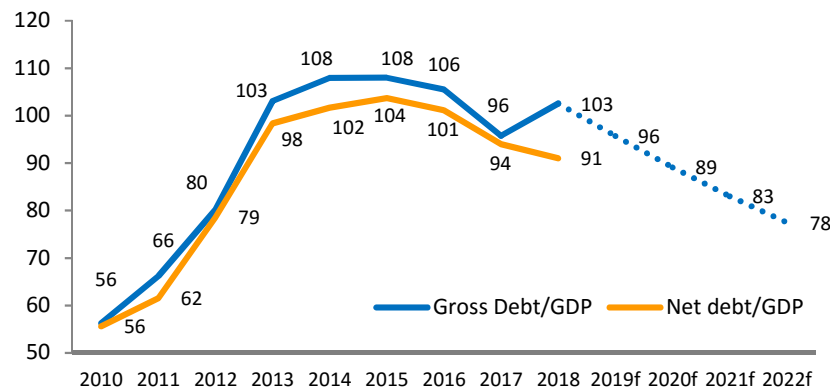
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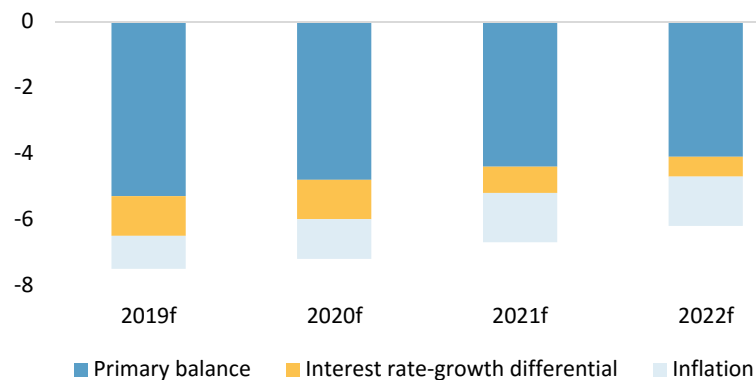
Positive public debt dynamics

- Public debt peaked over 2015-2016. After a one-off increase in 2018 due to the placement of government bonds as part of the partial sale of Cyprus Cooperative Bank, the decline is expected to resume and progress steadily to 78% by 2022.
- Debt dynamics are favourable due to growth, positive fiscal balance and low interest burden.
- The debt sustainability analysis, introducing various shocks to the macroeconomic parameters, indicates that the debt ratio continues to exhibit a declining path albeit at a slower pace.
- The current policy followed is for liquid assets to cover gross financing needs of the following 9-month period on a rolling basis.

Evolution of gross and net general government debt, %



Debt dynamics, % of GDP



Source: Cyprus Statistical Service, Ministry of Finance

Note: "f" denotes forecasts by the Ministry of Finance as of April 2019. All forecasts are based on assumptions and there can be no assurance they will be realised.



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A consolidated, capitalised and liquid banking system

The banking system has refocused its operations and renewed its corporate governance. The regulatory framework has been reformed and modernised. Decisive actions have been undertaken for the tackling of NPEs .

- Banking sector shrinks by half to 4x the GDP and reaches EU average
- International investors obtain majority holding of Hellenic Bank and Bank of Cyprus
- Capital controls lifted
- Successful stress test results
- ECB assumes supervision of systemic banks

2013-2014

- Legislation on Foreclosures, Insolvency and Sale of Loans enter into force
- Emergency Liquidity Assistance repaid
- Deposits on upward path
- Decline in interest rates
- Provision of new credit increases
- Non performing exposures mark first reduction

2015-2016

- Bank of Cyprus listed in London Stock Exchange and returns to bond capital markets
- Hellenic Bank and Bank of Cyprus outsource management of NPEs and real estate portfolios to independent servicing companies
- Sales of non-performing exposures
- Partial sale of the Cyprus Cooperative Bank to Hellenic Bank; state owned AMC for residual entity
- Banking sector at 3x the GDP
- Enhancement of laws on foreclosure, insolvency and sale of loans; Introduction of Securitisation law
- Introduction of scheme for NPE burden sharing among state, banks and borrowers

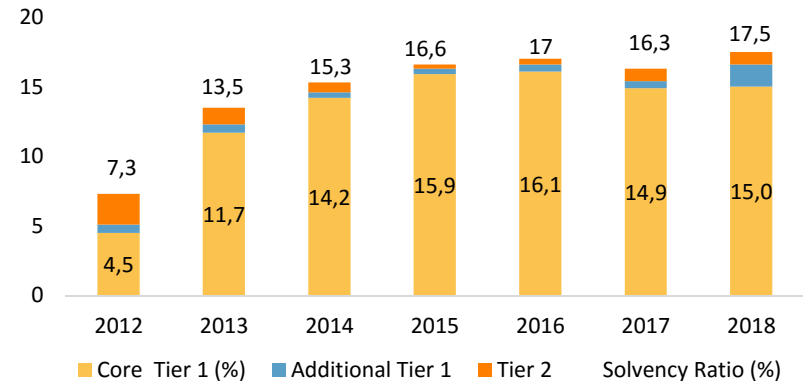
2017-2019



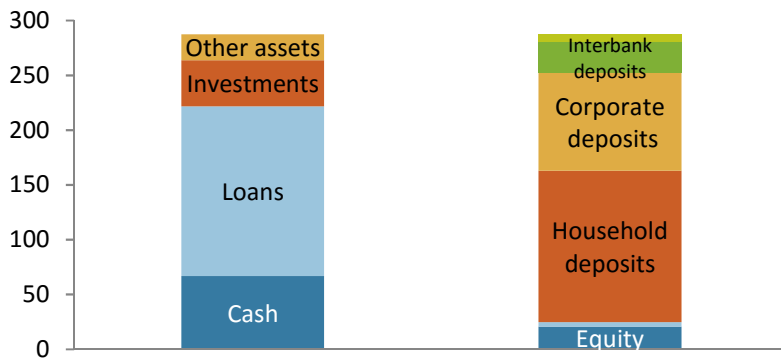
Solid capital base

- International investors hold majority of shareholding and board composition in systemic banks.
- Since 2013 the banks' capital position has been consistently strengthened, due to increase in common equity and deleveraging, resulting in key ratios of systemic banks to be above the thresholds specified by the supervisor.

Aggregate banking sector capital position, %

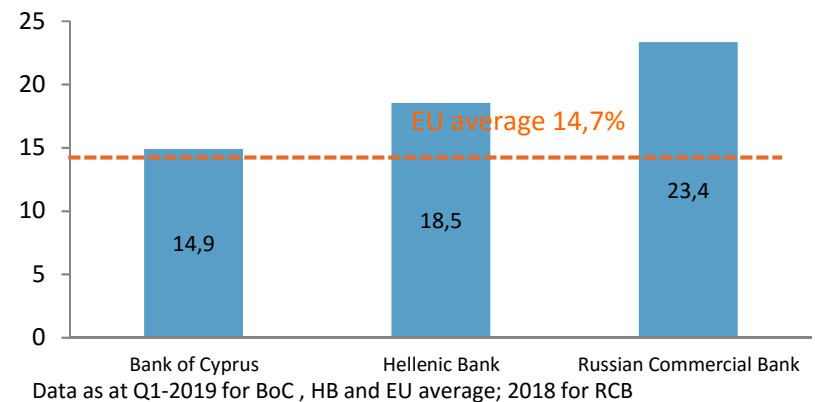


Banking system balance sheet (% GDP), Q4-2018



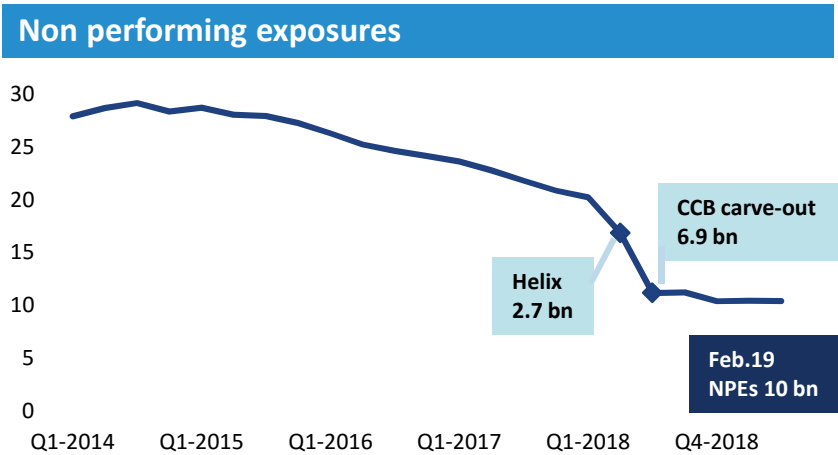
Source: EBA, Central Bank of Cyprus, systemic banks publications.

Systemic Banks CET1 capital ratio, %

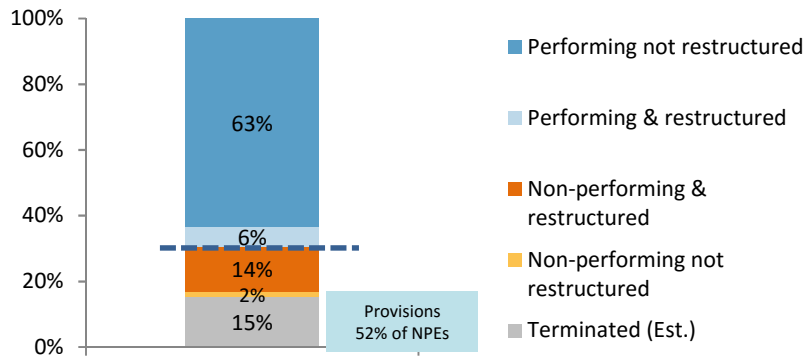


Sharp reduction in NPEs during 2018

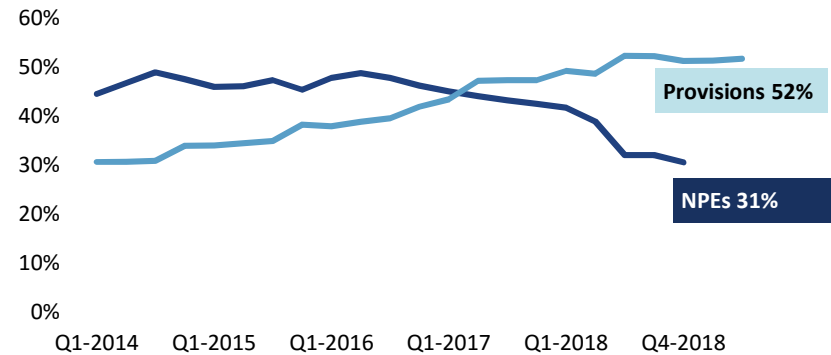
- Reduction by 50% in NPES over 2018 due to sale by Bank of Cyprus (Project “Helix”) and the Cooperative Central Bank carve-out.
- Remaining reduction attributed to (i) cash repayments, (ii) successful restructurings reclassified as performing facilities, (iii) write-offs as well as (iv) settlement of debt through swaps of immovable property with the ultimate aim the property sale.



Gross loans breakdown, Feb. 2019



Gross loans breakdown, Feb. 2019



Source: Central Bank of Cyprus, Ministry of Finance



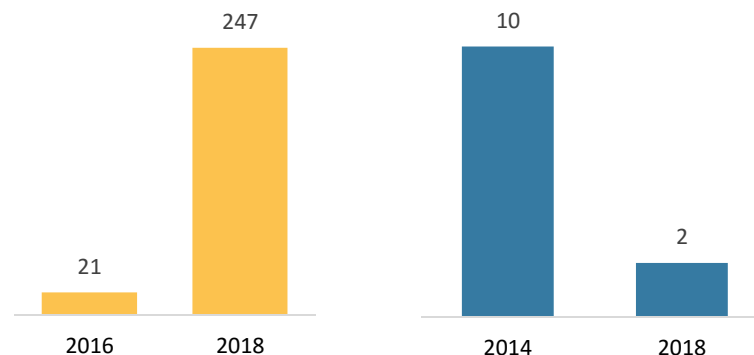
Non performing exposure management

- The banks' governance, and the regulatory and supervisory framework have been reformed to introduce incentives for borrowers and lenders:
 - Enhancement of banks' capacity: Centralized arrears management systems and dedicated recovery units have been implemented throughout the banking sector, whereas the largest banks have proceeded with outsourcing of NPE management;
 - Legislative measures: Legislation has been enhanced to facilitate a more streamlined and less time consuming asset recovery process: property foreclosure, insolvency, sale of loans, swift transfer of property title deeds and loan securitisation.
- Under the ESTIA scheme, which tackles NPEs collateralised by primary residence, the state will provide fiscal support to non-performing borrowers that meet certain eligibility criteria. The scheme will become operational during September 2019.
- Property prices mark a first increase albeit from a low base.

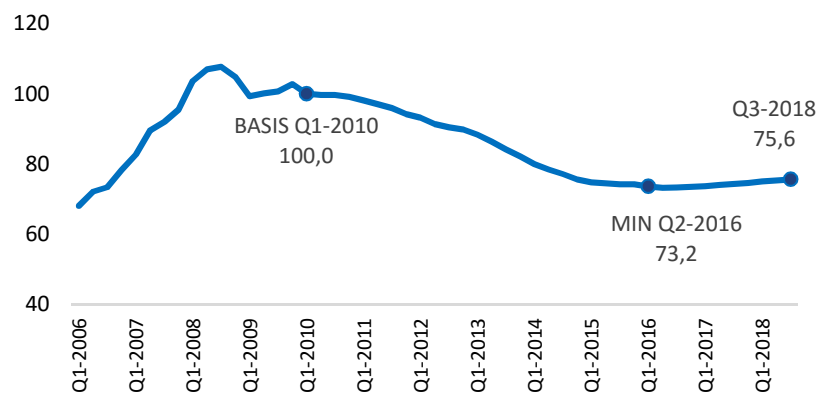
Source: IMF, Ministry of Finance, Central Bank of Cyprus

Auction sales, no. of properties

Years to foreclose (est.)



Residential Property Price Index

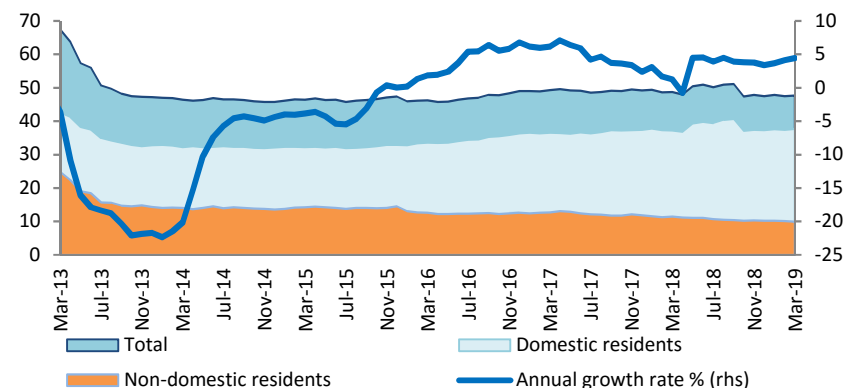


Liquidity and funding position continues to improve

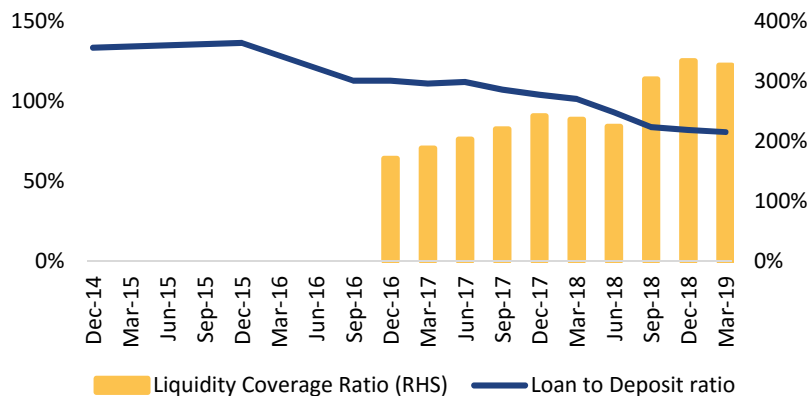
Low-cost deposit-funded banking sector

- Deposit increases in the domestic depositor base reflecting strengthened confidence and a stronger domestic economy. The increase in deposits relates mostly to higher deposits by companies while households record a more modest increase.
- The Liquidity Coverage Ratio more than double the EU-average while the two largest banks report comfortable Net Stable Funding Ratios.

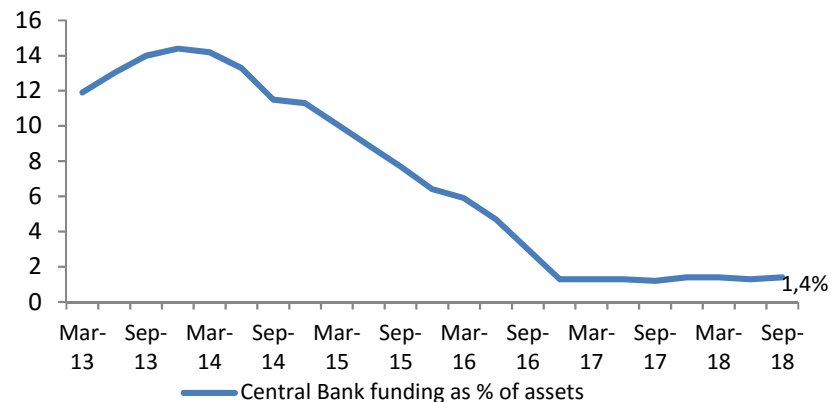
Evolution in deposits, EUR bn



Liquidity



Eurosystem funding, % of assets



Source: Central Bank of Cyprus, EBA ; Note: LCR data not available prior to Dec. 2016



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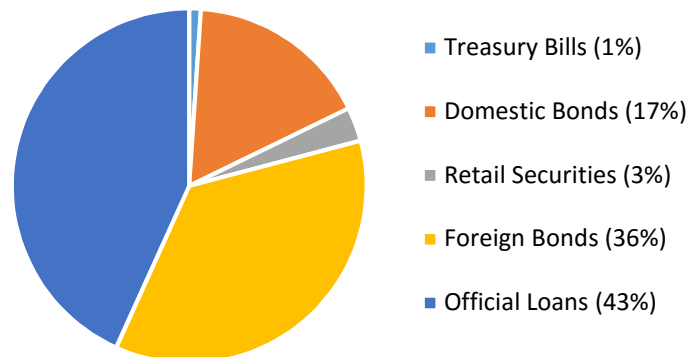
Public debt overview

Public debt structure, May 2019 ^(p)

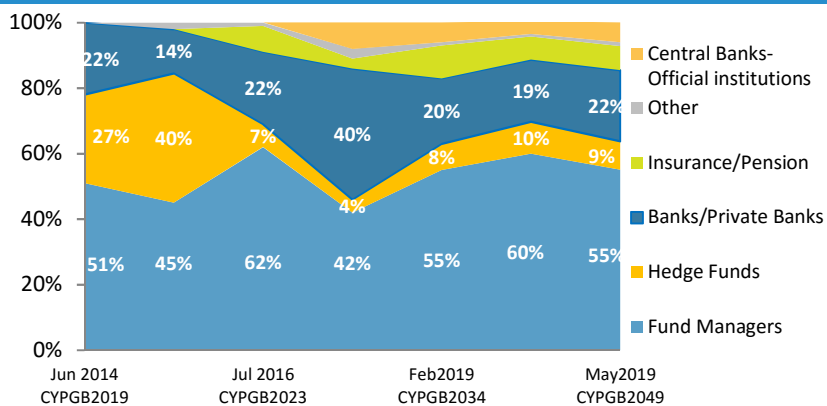
General Government Debt	€23,1 bn
General Government Debt/GDP	106% ^f
Of which liquid assets/GDP	14%

• Short term debt	1%
• Resident holders (estimate at issuance)	21%
• Domestic currency	97%
• Fixed interest rate	66%
• Private sector holdings (at issuance)	57%

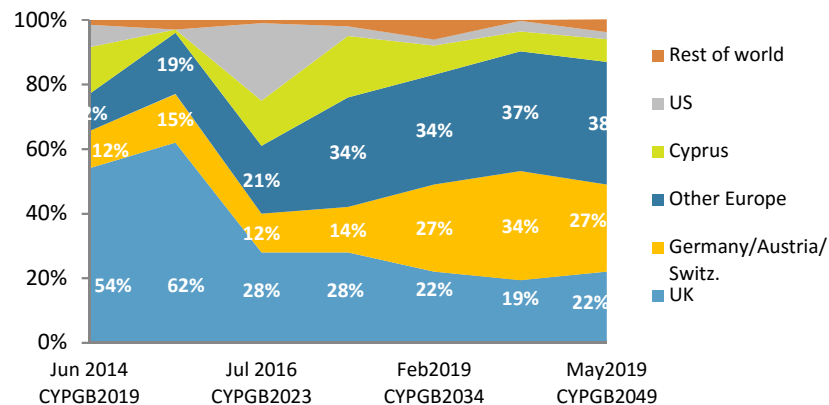
Public debt by instrument, May 2019 ^(p)



Evolution of investor base by type



Evolution of investor base by geography



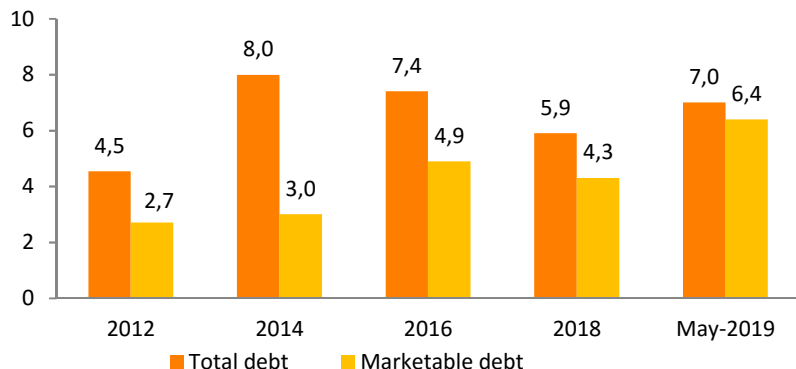
Source: Public Debt Management Office

Note: "f" denotes forecast by the Ministry of Finance as of April 2019 ; "p" denotes provisional figures

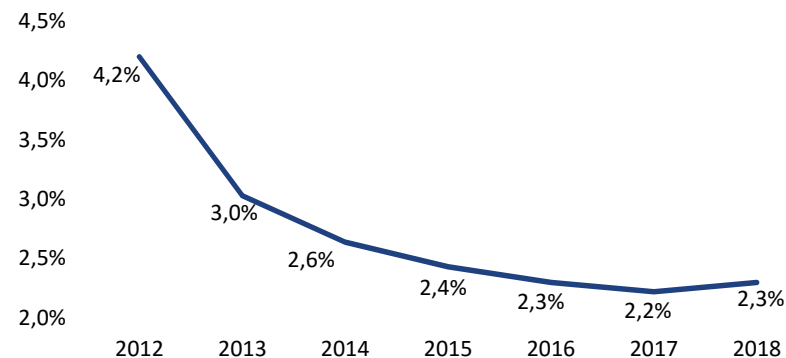


Debt portfolio cost-risk indicators improving

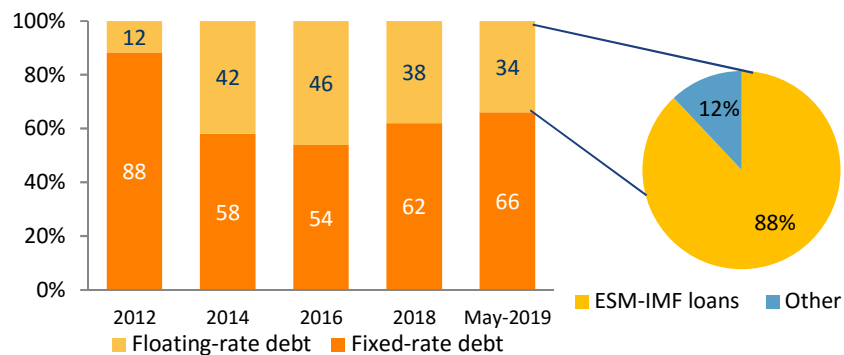
Weighted average maturity of debt, years



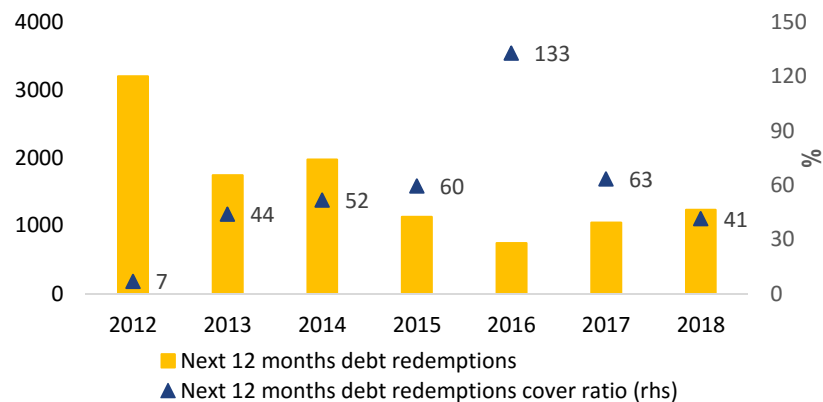
Cost of public debt, %



Interest rate distribution of debt, %



Evolution of government liquidity buffer, EUR mn



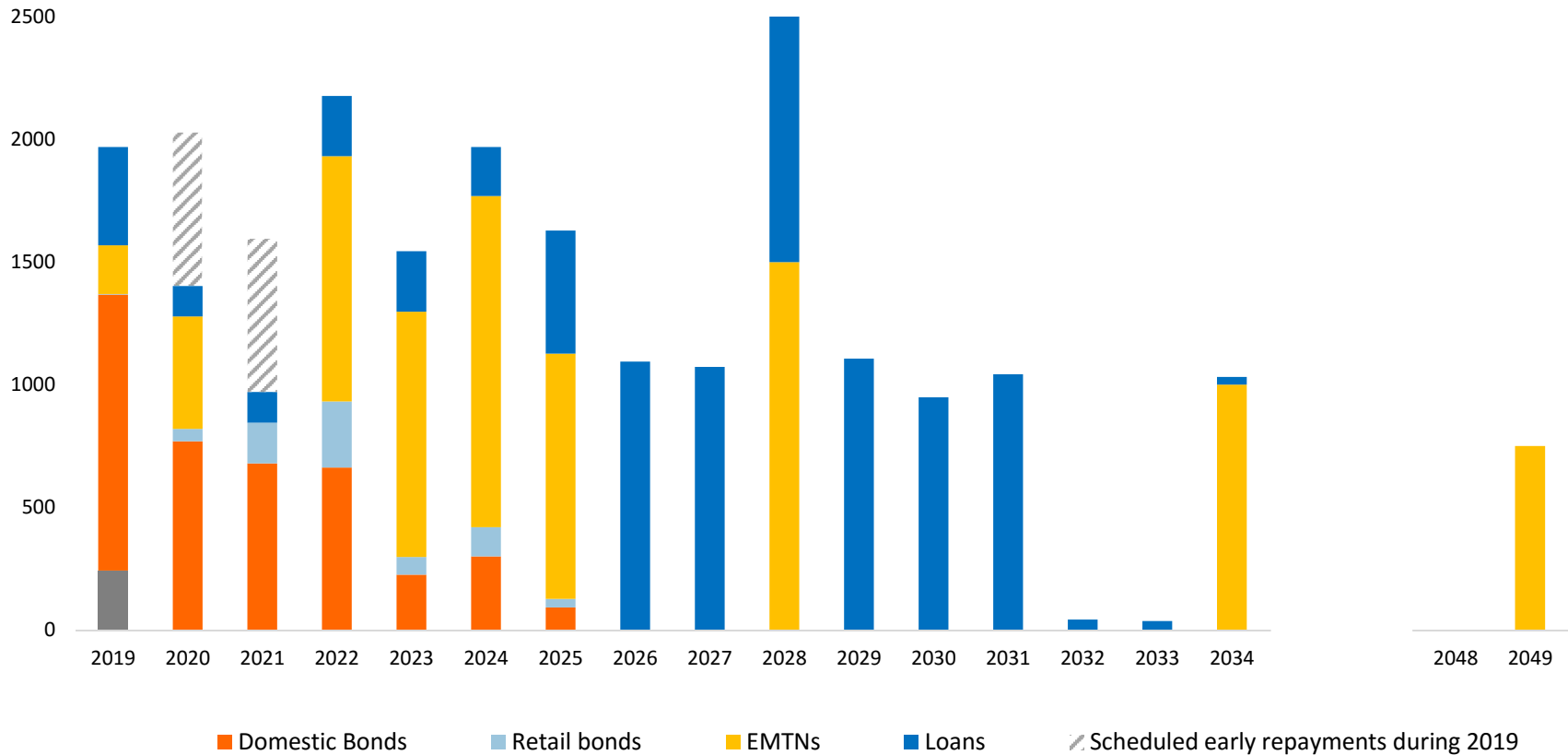
Source: Public Debt Management Office ; Note: "e" denotes estimates by the Ministry of Finance



Public debt maturity structure

Active management of debt aims to smooth out maturities further

Debt maturity profile May 2019, EUR mn



Source: Public Debt Management Office



Liquidity covers the budgeted financing needs up to Q3-2020

Annual Funding Plan 2019	
	EUR bn
Financing needs	2,9
Debt Redemptions 2019	
Treasury Bills	0,3
Domestic Bonds	1,1
EMTNs	0,2
Loans	0,7
Prepayments 2020-2021	1,3
Fiscal needs, cash basis	-0,7
Financing Sources	2,9
Treasury Bills	0,2
EMTN	2,3
Loans	0,3
Retail bond	0,1

- Main financing actions for 2019 have been completed through issuance of three international benchmark bonds with 5-year, 15-year and 30-year maturities.
- Complementary financing through Treasury Bills, retail bonds and loans.
- Yields at the local Treasury Bills market have been in negative territory throughout 2017-2019.
- Liquidity at year end to cover the financing needs of the first 9 months of 2020.

Source: Public Debt Management Office



Public Debt Management Strategy

Cornerstones in Public Debt Management Strategy 2016-20

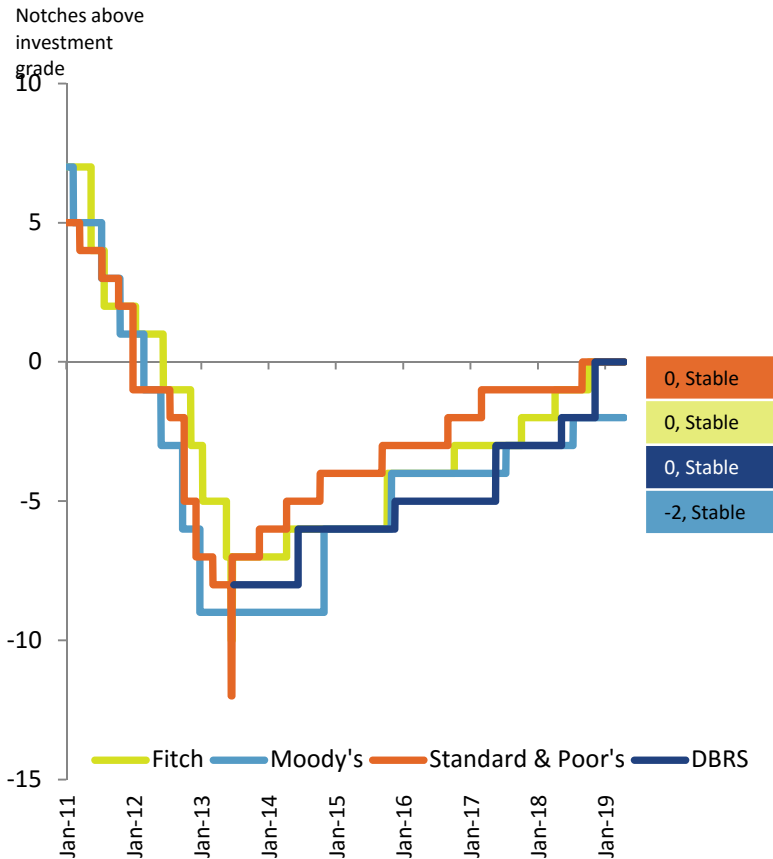
Target	Progress
Smoothing of debt maturity profile and increase of marketable debt maturity	On course: Average maturity of marketable and total debt extended
Maintaining liquid funds for at least the next 9-month period	On course
Risk mitigation via reduced exposure to foreign currency and interest rate risks	On course: new issuance completed in EUR, fixed rate format only
Building of international bond yield curve	On course: at least one benchmark issuance per annum achieved; Yield curve extended up to 30-year tenor
Enhancement of investor relations and expansion of investor base	On course: higher diversification and larger orderbooks recorded in primary issuances

- Strategically, the international bonds will continue to be the main financing instrument to achieve the medium-term objectives such as the extension of international bond yield curve and increase in debt maturity. The domestic market will continue to serve as a complimentary financing source.
- The current Debt Management Strategy covers the period 2016-2020 focusing on longer-term, fixed-rate, euro denominated issuances to assume low new risk into portfolio. Progress to date is evident in all targets.
- Issuance of at least one benchmark bond per year and liability management transactions have contributed to the attainment of strategic targets.



Restoration of investment grade status

Credit rating history and current status



Ratings' summary ¹

Rating strengths

- High income per capita, strong institutions and governance
- Fiscal policy space
- Highly skilled labour force

Concerns

- High levels of public and private debt
- Banking sector asset weakness

Progress

- Material reduction in the stock of NPEs
- Strong fiscal policy management
- Robust and resilient growth
- Government financing buffer

Note: 1. Non-exclusive list, as indicated in publicly available opinions of the Credit Rating Agencies reports. Please see full reports for more detail.



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- I. INTRODUCING CYPRUS
- II. STRONGER MACROECONOMY
- III. SOUND PUBLIC FINANCES
- IV. REFORMED BANKING SECTOR
- V. ACTIVE PUBLIC DEBT MANAGEMENT STRATEGY
- VI. LOOKING AHEAD**



Looking Ahead

Main indicators	2018	2019 <i>f</i> ⁽¹⁾	2020 <i>f</i>	2021 <i>f</i>	2022 <i>f</i>
Real GDP (% change)	3,9%	3,6%	3,2%	3,0%	3,0%
Unemployment rate	8,4%	7,0%	6,0%	5,5%	5,0%
Public debt (% of GDP)	103%	96%	89%	83%	78%
Fiscal Balance (% of GDP)	3,2% ⁽²⁾	3,0%	2,6%	2,4%	2,2%

Source: Ministry of Finance

(1) “f” denotes forecasts by the Ministry of Finance as of April 2019. Forecasts are based on assumptions and there can be no assurance that any such forecasts will be realised. Forecasts are subject to revisions from time to time.

(2) Excluding impact from the sale of Cyprus Cooperative Bank



Key credit highlights

Prudent fiscal policy

Robust and sustainable economic growth

Consolidated banking sector

Improved debt risk indicators

Strong institutions and legal system

Upside risks in services and energy sector

Government prefunding

Political stability

Economic resilience



Contacts

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Other sources of information

- Ministry of Finance www.mof.gov.cy
- Ministry of Foreign Affairs www.mfa.gov.cy
- Ministry of Energy, Commerce, Industry and Tourism www.mcit.gov.cy
- Central Bank of Cyprus www.centralbank.cy
- Cyprus Statistical Service www.mof.gov.cy/cystat
- Cyprus Investment Promotion Agency www.investcyprus.org.cy

