



## **Cyprus National Reform Programme 2013**

# **Europe 2020 Strategy for: Smart, Sustainable and Inclusive Growth**



**PLANNING BUREAU**

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## **1. INTRODUCTION**

### **1.1 Outline of the National Reform Programme**

Cyprus submits its National Reform Programme (NRP) on Europe 2020 for smart, sustainable and inclusive growth, as well as the fiscal tables (Annex I), in the context of the third European Semester, in a period when the country is entering into a Macro-economic adjustment Programme (the Programme) and is confronted with a major financial and economic challenge.

The NRP 2013 format has been adjusted to match the requirements for Member States under a Macro-economic Programme; it presents the progress in achieving the quantitative national targets for EU2020, as well as the most important measures promoted to achieve them. In this context, relevant measures adopted recently and announced by the President of the Republic, aiming to boost growth and face the high unemployment challenge, have also been included under the relevant national target. Finally, the progress with respect to the Euro Plus Pact commitments, as well as the measures taken to comply with the country-specific recommendations are briefly presented as well.

The NRP 2013 has been prepared in collaboration with all pertinent Ministries and has been approved by the Council of Ministers on 24 May 2013.

### **1.2 Economic Background**

On 16 March and 25 March 2013, the Eurogroup reached a political agreement with the Cypriot authorities on the key elements of a programme, which included the restructuring and substantial downsizing of the banking sector, combined with extensive bail-in of uninsured depositors, as well as the reinforcement of efforts on fiscal consolidation, structural reforms and privatisation. Following a financial turmoil, a bank holiday of 10 working days was imposed, during which the sector was downsized substantially through resolution and restructuring of the two main banks, separation of the Greek operations of Cypriot banks and a set of wide-ranging temporary capital controls and administrative measures, which are still in force to a great extent.

The programme is envisaged to build the foundation for sustainable growth over the long run. Nevertheless, in the short run, the economic outlook remains challenging. Real GDP is projected to contract by 12,5% cumulatively in 2013-14. Short-run economic activity will be negatively affected by the immediate restructuring of the banking sector, which will impact on net credit growth and by additional fiscal consolidation measures. The temporary restrictions required to safeguard financial stability will hamper international capital flows and reduce business volumes in both domestic and internationally oriented companies. The bail-in of uninsured depositors will cause a loss of wealth, which will reduce private consumption and business investment. This, compounded by the impact of fiscal consolidation already undertaken and new measures agreed, will result in a sharp fall in domestic demand.

Such new measures agreed and expected to be implemented as of 2013 by the Cypriot authorities include reforms of the pension system, to address the high projected increase in pension spending and to ensure the long-term financial viability of the pension system through 2060, the introduction of measures to control healthcare expenditures, complete and implement the national healthcare system, while ensuring its financial sustainability and providing universal coverage, the improvement of the fairness of the tax burden by levying the recurrent property tax on current market prices, proceeding with the reform of the wage indexation system (COLA), proposing a comprehensive reform plan to improve the effectiveness and efficiency of tax collection and administration and improve the efficiency of public spending and the budgetary process by means of an effective Medium-Term Budgetary Framework.

The agreed Programme with the Troika is an ambitious one, aiming at adopting fiscal measures totaling 7,25% of GDP during 2012-2016. It is emphasised that the implementation of various actions of the Programme has already started. Fiscal measures of 5,5% of GDP have already been legislated by almost total unanimity of the Parliament, covering the period up to 2016. It is acknowledged that there will be significant short-term negative impact on growth from the implementation of the Programme with positive growth only to be expected in the medium term.

Cyprus is transitioning to a new era, having a lot to gain from the utilisation of gas for its own energy needs, but even more to benefit from exploiting the gas through the manufacturing sector. Benefits from natural gas are three dimensional. Firstly, there will be investments in infrastructure in the coming 2-3 years, including the liquefying of natural gas (LNG). For the period 2013-2020, almost one-tenth of the estimated expenditures on mineral exploration and exploitation activities are expected to have a positive contribution to Cyprus economy. It can be expected that this contribution to the Cyprus economy will be reflected in a positive impact on growth rates of real GDP. On average, the impact is estimated at 1,5% for the whole period 2013-2020, with most of this influence expected in the last 4 years (2013-2016: +0,7%, 2017-2020: +2,3%). Secondly, it is projected that in the coming 3-4 years, Cyprus will have the capability of extracting natural gas for home consumption, which will lead among others to a reduction in electricity prices bringing multiple benefits to Cyprus economy. Lastly, longer term benefits will come from revenues from the exports of natural gas.

It is acknowledged that the Cyprus economy must first face some turbulent matters before it returns to a sustainable path. Despite the challenging times ahead for the Cypriot people, the medium and long-term outlook does have a more promising note due to the recent natural gas discovery.

### **1.3 Progress in achieving the National Targets**

Given the dire economic situation, most national targets have deteriorated, especially employment and the risk of poverty, but also the R&D and the early school leavers targets. The employment rate dropped considerably in 2012 to 70,2% deviating from the national target, while unemployment reached the record high level of 14,7%, (January 2013) with more than 44.000 being unemployed and consequently increasing the people at the risk of poverty. The climate indicators seem to be ahead of the set intermediary milestones, whereas the tertiary graduates target has been exceeded. The

last available data are listed in Table 1 below, with a detailed analysis been given in Section 2).

Table 1: Recent developments in National Targets

EU 2020 Targets	National target	Last available data/ year	Trend
Employment	75-77%	70,2% (2012)	Deteriorated
Social inclusion/poverty	19,3%	23,7% (2011)	Deteriorated
Early school leavers	10%	11,4% (2012)	Slightly worsened
Tertiary education	46%	49,9% (2012)	Improved
Research & Development	0,50%	0,49% (2011)	Slightly worsened
CO <sub>2</sub> emission ( non ETS )	-5%	-2,7% (2011)	Ahead of interim milestones
Renewable Energy	13%	6,8% (2011)	Ahead of interim milestones
Energy efficiency	14,3%	4,3% (2011)	Ahead of interim milestones

#### 1.4 Main measures to boost growth and achieve the national targets

**Recent measures announced by the Government:** In order to stimulate growth and help face the really adverse impacts of the Programme, the Government announced in April 2013 a number of measures that can be implemented immediately. In an effort to address the high level of unemployment the Government has recently announced three new schemes aiming to create jobs for about 8000 people, including the youth, with an estimated budget of €30 mln, to be funded primarily through the re-allocation of funds from the ESF. Also, tax reliefs will be offered to enterprises for new recruits, the issuance of all permits for new projects of the private sector will be completed within a maximum of three months, so as to create new jobs, SMEs will be helped to continue their operations by decreasing the cost of electricity by 9,5% and decreasing the lending rates, while government property will be offered to new farmers, for self-employment in the agricultural sector. In order to improve private and public sector competitiveness in Cyprus, measures promoted include the operation of the One Stop Shop, the simplification of procedures for setting up a company, the setting up of the Cyprus National Guarantee Fund for Small and Medium Enterprises, the re-activation of the JEREMIE initiative, continuation of the schemes for the promotion of innovation, for women and youth entrepreneurship, implementation of projects to improve the tourism product and the offering of subsidies to prolong the tourism season by two months.

The new Government puts great emphasis on improving the efficiency of the public sector and thus a Commissioner has been appointed, with the specific task to oversee the modernisation of the public sector, the simplification of procedures, the introduction of staff mobility within services, the faster introduction of e-government, the evaluation system of public employees and the increase of accountability and transparency.

Efforts also focus on addressing the social consequences of the current crisis and to support the most vulnerable, by prolonging the loan–repayment period, protecting debtors that cannot pay by ensuring property ownership, increase the number of

students at the public universities to accommodate students that cannot afford to continue their studies abroad and take measures to counter the exploitation of the social system by immigrants.

**Measures already in the pipeline** are also promoted, in an effort to improve the workforce skills, reduce drop out rates and stimulate business innovation. Some such measures include the operation of Post Secondary Institutes of Vocational Education and Training, in an effort to increase employment in technical jobs, and a scheme that promotes the development of innovative products and services by SMEs, creating also high value added jobs. Currently a Smart Specialisation Strategy for Research and Innovation is being prepared and will primarily be based on the analysis of the local economy and the social structure and innovation. For the promotion of innovation and high valued added jobs, the Digital Strategy is also implemented; an Action Plan for 2013-2015 was approved by the Council of Ministers in November 2012 with a corresponding timetable and allocated budget in place. Main efforts during 2012 focused on further achieving the broadband targets, modernising public administration and the provision of electronic services, promoting eEducation in schools, promoting digital literacy, implementing new subsidy schemes for SMEs to develop ICT products or services and for using ICT for their internal procedures and for eBusiness.

The introduction of natural gas to the national energy system will be a major contributor to the energy efficiency target. Other measures to this end include grant schemes for energy saving and domestic generation for Renewable Energy Sources (RES) in all sectors, measures focusing on road transport and the implementation of new EU policies such as the new Energy Efficiency Directive.

Measures for increasing the contribution of RES to the gross final energy consumption by 2020 are on-going. Currently, efforts focus on a pilot project announced by the Cyprus Energy Regulatory Authority (CERA) in 2012 for examining the effects of Net-metering. In addition, the Electricity Authority of Cyprus (EAC) has tendered out for the implementation of an Advanced Metering Infrastructure in Cyprus. This contract will be awarded before the end of 2013.

It is of course recognised that many more measures are required to boost growth, for which additional funds will be needed. To this end, a relevant request has been already addressed to the Commission, the Council and the European Parliament, including the request to increase the co-financing rate by Structural Funds. A needs assessment is also in process to finalise the most appropriate measures to be implemented, in order to help face the serious side effects of the Programme and put the economy back to the path of growth.

## **2. NATIONAL TARGETS**

This section reports on the developments of Cyprus national targets on employment, poverty, education, R&D and climate, as expected of a Member State under a Macroeconomic Programme. In addition, under each target, the main policy measures that aim to contribute towards the achievement of the targets, improve competitiveness and help re-ignite economic activity are mentioned.

In the last year, because of the financial and economic crisis and a long period of uncertainty, before the final agreement for Cyprus' programme, there was a sharp worsening of employment rate (70,2%) and unemployment figures (14,8%) in January 2013 , reflecting the significant worsening of economic activity. The share of people at risk of poverty or social exclusion (AROPE) has increased, however the most recent data concern the year 2011 (23,7%). It is expected that in 2012 the situation will deteriorate further, with both unemployment and poverty getting worse. The share of 30-34 years old having completed tertiary or equivalent education improved in 2012 (49,9%) while the early leavers from education and training rate, slightly worsened (11,4%) since 2011. The percentage of Cyprus GDP invested in R&D was reduced in 2011 (0,49% provisional figure). With respect to the RES target, Cyprus has already achieved its first (4,92% for 2011-2012) and second (5,93% for 2013-2014) indicative trajectory since the share of RES in the gross final energy consumption was 6,8% in 2011. The energy efficiency reduction of energy consumption was 4,3% which is well above the projected reduction (0,9%) for 2011. Cyprus's national targets are enumerated in the last column in the table below and progress can be seen by comparing it to the adjacent columns with the most recent available data.

Table 2: EU Headline Targets and National Targets

EU HEADLINE TARGETS & NATIONAL TARGETS	EU HEADLINE TARGETS	NATIONAL LEVEL 2008	NATIONAL LEVEL 2009	NATIONAL LEVEL 2010	NATIONAL LEVEL 2011	NATIONAL LEVEL 2012	NATIONAL TARGETS
Employment rate for women and men aged 20-64	75%	76,5%	75,7%	75,4%	73,4%	70,2%	75-77%
Promoting social inclusion in particular through the reduction of poverty	Lift at least 20 mln people out of the risk of poverty and social inclusion	23,3% or 181.000 people at risk of poverty	23,5% or 188.000 people at risk of poverty	23,5% or 192.000 people at risk of poverty (Eurostat)	23,7% or 199.000 people at risk of poverty (Eurostat)	n.a	19,3% Lift 27.000 people out of the risk of poverty
Early school leavers	10%	13,7%	11,9%	12,6%	11,3%	11,4%	10%
Share of 30-34 years old having completed tertiary or equivalent education	40%	47,1%	44,7%	45,1%	45,8%	49,9%	46%
3% of the EU's GDP should be invested in R&D	3%	0,42%	0,49%	0,50%	0,49% (provisional figure)	n.a	0,50%
CO <sub>2</sub> emission reduction targets	-20% (compared to 1990)	N.A	N.A	N.A	2,7%	n.a	-5% (compared to 2005)
Renewable energy	20%	4,5%	4,8%	5,8	6,8		13%
Energy efficiency reduction of energy consumption in Mtoe	20% equaling 368 Mtoe	N.A	N.A	3,6%	4,3%	n.a	14,3%

More information on each national target is given below.

### 2.1 Employment National target:

75%-77% of the population aged 20–64 should be employed by 2020

*Dropped to 70,2% in 2012 compared to 73,4% in 2011*

According to the Labour Force Survey, the unemployment rate between 2011 (yearly average) and 2012 (yearly average) increased from 7,9% to 11,8% as opposed to the unemployment rate of only 3,7% in 2008. Based on the EUROSTAT latest forecast

statistics, in January 2013 the unemployment rate stood at 14,7% while the Euro area unemployment rate was at 11,9%.

The overall employment rate for the age group 20-64 years old decreased from 73,4% in 2011 to 70,2% in 2012. In 2008 the employment rate was at a high level reaching 76,5%. According to the distribution of employment by sector during 2012, the biggest percentage of employed persons was concentrated in services with 76,9%, whereas industry followed with 20,2% and lastly agriculture with only 2,9%.

During 2009, the first year of the recession, more male than female workers lost their jobs, a phenomenon attributed to the economic downturn, which affected primarily male-dominated occupations, namely, construction, real estate and tourism. For 2012, the unemployment rate for male workers stood at 12,5% and for female workers at 11,1%, while the respective employment rates were 76,1% and 64,8% (age group of 20-64 years).

Youth unemployment followed the European trend and increased significantly, from 9% in 2008 to 27,8% in 2012 (for the age group 15-24 years). The respective employment rate for this age group went down from 33,8% in 2010 to 28,1% in 2012.

Prior to the recession, in the second quarter of 2009, Cyprus had been enjoying a sustained growth with a GDP growth averaging 4% against 2% in the euro area. As a result of the crisis and the adverse external environment, domestic demand was reduced, leading to the slowdown of economic activity and subsequently to the loss of jobs. The aggregate demand was further reduced because of the budgetary reconciliation measures which followed.

The economic downturn surfaced the structural problems of the economy, namely the limited diversification, the engagement in low added value activities and the lack of investment in innovation and new technologies leading subsequently to low productivity, the economy being highly sensitive to cost and vulnerable to external shocks and employing low skilled workforce.

Additionally, the exposure of Cyprus banks to Greece had increased the cost of capital and reduced its availability, making it reasonably difficult for SMEs to finance their development or expansion activities.

The global character of the economic crisis and the fact that some countries were hit more severely than others caused large migration flows between member states, including Cyprus as well. Cyprus experienced a disproportional inflow of EU workers (mainly low skilled or unskilled) who were attracted by the good employment situation and the sound economy of Cyprus. This resulted in unfair competition between domestic and external workers, uncertainty, phenomena of exploitation of workers and substitution of domestic workers by foreigners. Despite the enhancement of inspection mechanisms, undeclared and illegal work is still at high levels as a consequence of the crisis.

It is worth mentioning that in 2011, one in every five persons of the labour force was non-Cypriot. Similarly, 29% of the unemployed persons were also non Cypriots. Even during 2012, with the country's economy experiencing such downturn, from the analysis of the labour market statistics it appears that such inflows of EU workers continued, even though at a lesser extent.



In an effort to address the high level of unemployment the government is promoting several schemes aiming to create more jobs. Some of these measures are presented below:

- **Scheme for Job Placement and Training of Tertiary Education Graduates:** This scheme is a consolidated programme focused on highly qualified young people. While the target for 2012 was to have 670 participants, the actual participants reached 709 persons. In 2012, the HRDA completed an evaluation study regarding the impact on the participants of the Scheme to whom a subsidy was granted during the period 2009-2011, that revealed that 90% of scheme participants were employed. In 2013, a second evaluation study will be carried out. The budget for 2012 amounted to €5,7 mln with actual expenditure for 2012 reaching the amount of €6.227.934.
- **Grant Scheme to support youth employment:** This is a new scheme consisting of subsidies to businesses for hiring young unemployed (up to 29 years) for 12 months (+6). Businesses that have already been subsidised from the scheme of the Ministry of Commerce, Industry and Tourism for Youth, Women and Innovative business start ups (414 businesses up to now) will be subsidised for hiring unemployed people (criteria: tertiary unemployed people, up to 29 years old that have been registered unemployed for more than 6 months). 80% of their salary will be subsidised with max. €15.000/per annum. The project fund has been approved, starting in March 2013. The budget for the scheme is €3 mln to be co-funded by the ESF (75%).
- **Scheme providing incentives to employers for the employment of the long-term unemployed and the young:** This scheme targets young people up to 29 years old who have been registered as unemployed for at least 3 months, and persons registered as unemployed for at least 7 months. Since May 2012 approximately 250 persons have participated in the scheme. (Youth under 29 years old: 145 persons, long term: 108 persons). The timetable for the implementation of the scheme is May 2012-2015 with a budget of €8 mln. Actual expenditure for 2012 was €140.000.
- **Project offering guidance and/or placements in companies to the young unemployed to gain work experience:** This new scheme is aiming to enhance the job search capacity of the newly registered young unemployed through their participation in short induction courses and improve the employability of the young unemployed through their placement for 16 weeks in companies for acquiring work experience. The funding has been approved. The scheme is expected to start in June 2013 and finish by September 2015. The target is to have 1.940 young people benefiting from this project, 840 people in guidance and 1.100 in placement programmes. The budget of the scheme is €4,2 mln co-funded by the ESF (75%).
- **Subsidy scheme for attracting people in the labour market through flexible forms of employment:** The scheme provides incentives to employers to hire unemployed or economically inactive individuals who have difficulty to enter and remain in the labour market without the option of some form of flexible arrangement. Through the scheme, participating businesses are subsidised with 65% of the labour cost of the persons employed (salary + employer's social insurance contributions). The subsidy is granted for the first 12 months of the

employment provided that the employment period is at least 14 months. The employees are also subsidised for the travelling cost to and from their work place. The responsible authority for the implementation of the scheme is the Cyprus Productivity Centre. The Scheme was launched in May 2010 and by December 2012 more than 500 applications were received from companies and more than 1.600 applications from individuals seeking employment, while 300 employment contracts were signed. The budget of the scheme is €4,5 mln and is being co-funded by the ESF. Actual expenditure for 2012 reached €1,4 mln.

- **Schemes for the enhancement of women and youth entrepreneurship:** The schemes aim to the financial support of women and young people who wish to engage in the sectors of manufacturing or in specific activities in commerce, services and tourism. Total budget for the programming period 2007-2013 is €18 mln. By the end of 2012, €3,6 mln have been granted to 205 eligible applicants. The remaining funds will be allocated among 240 applicants whose applications have already been approved and are implementing their investment proposals and also to the eligible applicants of the 3<sup>rd</sup> call of the scheme. In addition, 890 new job positions are expected to be created upon completion of all approved projects.

In the package of the new measures announced by the Government last April, the following are also included:

- **Encouraging self-employment in the primary sector:** Land owned by the government will be granted to young farmers, based on professional, financial and social criteria with the farmers paying a token rent. The Ministry of Agriculture, Natural Resources and Environment will provide the necessary training, counseling services and any other relevant support to the beneficiaries.
- **Maintain employment in public sector:** 800 seasonal hourly paid employees will be reemployed in the public sector in 2013 to meet seasonal needs. Similarly, needs in the educational system will be covered by the reemployment of teachers on a contract basis according to the estimations of the Ministry of Education and Culture for the school period 2013-2014.
- Three new measures to stimulate employment of an estimated budget of €30,8 mln to be derived mainly by re-allocating funds from the ESF:
  1. **Flexible Forms of Employment Subsidy Scheme:**  
Budget: €6,8 mln. Target: Employment of 1000 unemployed persons.  
The Scheme aims at combating unemployment, through attracting unemployed persons who wish to work on a flexible form of employment basis and at the same time it gives businesses a means to address the difficulties brought on by the financial crisis for the creation of new jobs
  2. **Subsidised Employment Scheme for the Hotel, Food and Tourism Industry**  
Budget: €20 mln. Target: Employment of 6000 unemployed persons.  
The Scheme aims at combating unemployment as well as further enhancing the quality of services provided by the Industry, inter alia, through the recruitment of qualified staff.

### 3. Scheme for Job Placement of Young Unemployed Tertiary Education Graduates for the acquisition of work experience in enterprises / organisations

Budget: €4 mln. Target: Employment of 1000 unemployed young graduates.

This programme aims at offering young graduates the opportunity to gain working experience. The participants will be offered a weekly training allowance of €125.

**2.2 Poverty National target: Reduce the number of people-at-risk-of-poverty and social exclusion by 27.000 people or decrease the percentage of people-at-risk-of-poverty and social exclusion from 23,3% in 2008 to 19,3% by 2020.**

*Increased to 23,7% (199.000 people) in 2011 compared to 23,5% (192.000 people) in 2010*

The share of people-at-risk-of-poverty or social exclusion (ARPE<sup>1</sup>) increased in 2011 from 2010 by 0,2 percentage points (from 23,5% in 2010 to 23,7% in 2011). With regard to the sub-indicators comprising the ARPE, the at-risk-of-poverty rate (i.e. monetary poverty, AROP) has dropped from 15% in 2010 to 14,5% in 2011, while the severe material deprivation<sup>2</sup> has increased to 10,8% in 2011 from 10,1% in 2010 and the share of people living in very low work intensity households<sup>3</sup> (quasi-jobless households) in 2011 was 4,6% (statistically insignificant change from 2010).

Although the poverty threshold (i.e. the 60% of the median equivalised income) has increased, the at risk of poverty rate (AROP) decreased in 2011, which is considered an improvement (lower percentage compared to the percentage before the economic crisis<sup>4</sup>). A considerable decrease is found at the at-risk-of-poverty rate for the elderly (from 40,5% in 2010 to 37,2% in 2011). Child poverty also decreased (from 12,3% in 2010 to 11,9% in 2011). Regarding severe material deprivation, the most vulnerable group is children, with rates rising up to 13,7% in 2011 in comparison to 10,9% in 2010.

In response to the economic crisis and in accordance with the current Troika negotiations following the request by the Republic of Cyprus for a financial bailout, Cyprus undertook several reforms which have had an impact on social policies. The aim of the Cyprus government in taking these reforms was to minimise the social consequences of the financial crisis and subsequent recession and also to provide additional services in order to better support the most vulnerable.

As such and towards preventing and combating poverty and social exclusion the priorities are to:

<sup>1</sup>This rate refers to the union of the 3 indicators: at-risk-of-poverty (AROP) and/or people living in conditions of severe material deprivation and/or people living in low work intensity households.

<sup>2</sup>Severely materially deprived persons have living conditions severely constrained by a lack of resources, they experience at least 4 out of 9 following deprivations items: cannot afford i) to pay rent or utility bills, ii) keep home adequately warm, iii) face unexpected expenses, iv) eat meat, fish or a protein equivalent every second day v) a week holiday away from home, vi) a car, vii) a washing machine, viii) a colour TV, or ix) a telephone. It refers to 2010 income reference year.

<sup>3</sup>People living in households with very low work intensity are people aged 0-59 living in households where the adults work less than 20% of their total work potential during the past year. It refers to 2010 income reference year.

<sup>4</sup>However, we must bear in mind that the income reference year for 2011 data is 2010.

- Maintain or/and lower child poverty and social exclusion. This priority is addressed mainly through (i) measures to get parents back to work through training and employment schemes and improve their income situation, and (ii) provide accessible and affordable child care services and other services.
- Activate and support inactive and unemployed persons dependent on public benefits and promote/continue projects for the employment of persons with disabilities and the inclusion of migrants.
- Decrease old people's poverty (see reference on CSR 5) and improve their well-being (long-term care).

Measures under these priorities include:

- **Measures to get parents back to work through training and employment schemes and improve their income situation:** Many active labour market policies are co-funded by the ESF through the Cyprus Operational Programme “**Employment, Human Capital and Social Cohesion**” 2007-2013. The Operational Programme focuses on increasing the adaptability of the private and public sector, attracting and retaining more people to the labour market and strengthening social inclusion. Its total budget reaches €149.711.443 and is allocated under three priority axes. The first priority axis, “Development of Human Capital and Adaptability” amounts to €5.815.324, the second, “Expansion of the Labour Market and Social Cohesion” has a budget of €9.898.813 and the third priority axis “Technical Assistance of Implementation”, has a budget of €3.997.306. The total amount spent under the Operational Programme for 2012 was €24,9 mln. For 2013, the total estimated amount to be spent will reach €34,5 mln allocated as follows: Priority Axis 1 €9,7 mln, Priority Axis 2 €13,6 mln and Priority Axis 3 €1,2 mln. The projects continued to operate in 2012 and 2013.
- **Provide accessible and affordable child care services and other services:**
  - In order to prevent and minimise the risk of children's poverty and support female employment, the government continued the **subsidisation of social care services within the framework of family and employment reconciliation**. The measure, which was officially launched in February 2012, includes the reimbursement of part of the cost of care services for children, older people and persons with disabilities. Women who find a job may apply for a subsidy for the cost of care services for their family dependants for a period of up to 18 months. The benefit is €260 (maximum amount) monthly, for childcare, and €200 (maximum amount) monthly for the care of older persons or persons with disabilities. In 2012, 49 women were approved to receive subsidisation. A total of €49.157,10 was spent in 2012 and the Budget for 2013 is €0,5 mln.
  - Furthermore, the **subsidisation schemes for child care programmes** operated by local authorities and NGOs continued throughout 2012 and will also be continued in 2013. The aim of these schemes is to enhance the expansion of available child care services at a lower cost and within their 2013 priorities the Schemes include the subsidisation of programmes for the most vulnerable/deprived persons.
- **Project for the Work and Social Activation of People in Vulnerable Groups through the Development of Social Skills and Other Actions:** The aim of these training programmes is to up-skill Social Services Officers in activation techniques and adopt an activation culture towards inactive people that are frequently trapped

in the social benefit system and require special individualised approach in order to be motivated to take up training or/and a job. Following this training, Social Services Officers intensively work with beneficiaries and divert them to training classes for improving their self-confidence and upgrading their communication skills. These training courses to beneficiaries of Welfare Services commenced in February 2013 and are expected to be completed in May 2015. Furthermore, for people furthest from the labour market who are facing a higher risk of exclusion, a special scheme is operated within this Project which supports 9 local authorities in co-operation with NGO's in implementing "Street work" programmes.

Cyprus currently investigates the development of new projects through the establishment of **social economy actions** in order to promote the employment of vulnerable people.

- **Reform of the Public Assistance:** To ensure efficient use of public funds within the welfare system, while at the same time ensuring an appropriate balance between welfare benefits and incentives to take up work, the Social Welfare Services are in the process of carrying out a reform of the welfare system (Public Assistance Law) to be implemented and applied the soonest possible. The planned reform of public assistance should ensure that social assistance serves as a safety net to ensure a minimum income for those unable to support a basic standard of living, while at the same time providing incentives to take up work, ensuring consistency with the reform of the welfare system.
- **Integration of Migrants:** The National Action Plan 2010-2012 for the Integration of Third Country Nationals legally residing in Cyprus, has been completed and will be evaluated in order to adopt a renewed National Action Plan covering the upcoming two years 2013-2014. The 2010-2012 National Action Plan covers eight Priority Pillars, including Information, Employment, Education, Health, Housing, Culture, Participation and Assessment and have been partly funded by the Solidarity Funds of the EU (Integration Fund), by the European Social Fund and also by national funding.

In the new measures recently announced by the Government in April, the following promote rationalization of public assistance and strengthening of social cohesion:

- **Eliminating the right to social or unemployment benefit** to those that reject twice a job offered by the Public Employment Service.
- **Modification of the subsidy schemes to asylum seekers and other foreigners** so as to minimize the abuse of the system.
- **Abolition of any subsidy to foreigners in cases they refuse to work** in sectors and periods where employment is permitted.
- **Protection of problematic debtors: Measures for extending the loans' repayment period are promoted** thus, reducing the installments without any extra cost to the debtors. Debtors facing problems are asked to contact their financial institutions within 60 days to work out a settlement. The Central Bank of Cyprus has issued a relevant circular letter and further, legislation is being promoted for the protection of households' owners. According to the legislation, the bank can buy the property at loan's remaining value and at the same time rent the property to the owner for a specific time of period, so that the owner retains its home.

### 2.3 Education National target:

- Reduce the dropout rate to 10% by 2020 from 11,9% in 2009  
*Reached 11,4% in 2012 compared to 11,3% in 2011*
- Increase the share of the population aged 30-34 having completed tertiary education to at least 46% by 2020 from 44,7% in 2009  
*Reached 49,9% in 2012 compared to 45,8% in 2011*

#### A. Reduce the rate of early school leavers to 10%

The rate of early leavers from education and training remained almost at the same level in 2012 reaching 11,4% compared to 11,3% in 2011 and from the set target of 10% by 2020. Conditions of low economic activity and of poverty can lead to low education achievement and subsequently to the lack of employment opportunities. Early identification of learning difficulties, promotion of integration programmes for migrants as well as promotion of programmes for vocational education are among the priority actions carried forward aiming to offer equal opportunities in education and combat social injustices.

For reducing the rate of school dropouts to 10% by 2020, measures facilitating the integration of students at risk in the school system have been introduced with a total budget of €1,6 mln co-funded by ESF. The actions include programmes for targeting early school leaving, young delinquency and antisocial behavior. For students with migrant background, a special induction program has been especially designed and it is currently implemented. Under this measure the following actions are included:

- Proposal for the development of new curriculum for Upper Secondary and Secondary Technical and Vocational Education and Training.
- Encourage school enrolment and school success through schemes such as the “Zones of Educational Priority”, services such as Psychological support and Career Counselling, special induction programs for migrants.
- “Support hours” such as student tutoring and mentoring programs.
- Setting up a Task Force for the early identification of behaviour problems to accomplish the goal of reducing school failure and dropout rates.
- Migrant Students’ assessments for early identification of literacy problems through early diagnosis.
- Establishing an Observatory for Violence in Schools to address the problem of violent and antisocial behaviour in a holistic approach.

For the designing and implementation of the aforesaid actions the method of open coordination was introduced inviting Stakeholders to actively engage themselves in the process. The Stakeholders involved Political Parties, Teacher Unions, Parents Associations, Associations of Students, and the Government, represented by the Ministry of Education and Culture and the Planning Bureau.

#### B. Increase participation in Higher education to 46%

Cyprus continues to be above the set target of 46% of higher education graduates, reaching 49,9% in 2012. However, due to the adverse economic situation and the decrease of income in most households, it is expected that less people will be able to afford tertiary level studies.

Hence, the University of Cyprus has decided to increase the number of students it will accept in September by 100 and also give the opportunity to 200 students that will not be able to afford to continue their studies abroad, to transfer to Cyprus. In much the same way, the Cyprus University of Technology will increase enrollment by 35 and 30, respectively. Also, in 2012 the main scheme for granting education subsidies has been changed to include income criteria, aiming at addressing the needs of the most vulnerable groups. There are also ongoing measures that continue to be implemented:-

In order to improve participation in Higher Education the following measures are promoted:

- **Strengthening the links between technical vocational education, training and the labour market:**

Establishment of Post Secondary Institutes for Technical and Vocational Education and Training, which could offer to learners, at affordable cost, programmes at an intermediate level, between upper secondary and tertiary education, complementary to the programmes offered by the private colleges. It has also been decided to increase the number of students enrolled in the Post Secondary Institutes of VET as of school year 2013-14. The budget for the establishment of the PSITVE is €4,500,000 (co-financed at 85% by the ESF) and it will be fully implemented by 2015.

- Strengthening the contacts between VET, the social partners and the enterprises.
- Promoting a culture of research and innovation.
- Strengthening the efforts towards better and systematic collection of data, which includes VET related skills anticipation.
- Upgrading vocational guidance services.

- **Expansion and modernisation of the higher education system:**

- Increase the number of students attending programs of studies related to science and technology.
- Improve the cooperation between High Education Institutions (HEIs), business, local industry and the labour market.
- Enhance the cooperation between the Ministry of Education and Culture and other competent ministries regarding the link of Higher Education to the labour market.

- **Promoting transnational mobility:**

- Establishment of a National Qualification Framework which will include recognition of prior learning procedures.
- Implementing EU tools such as the European Qualifications Framework (EQF) or linking to this the National Qualifications Framework (NQF) and the European Credit Transfer System for Vocational Education.
- Increasing participation in EU programs such as the Lifelong Learning Programme that have a strong element of geographical mobility. Encouraging all Technical and Vocational Schools and adults to actively participate in Leonardo da Vinci mobility action for initial and continued training and placements in enterprises abroad (currently only 50% of the technical schools are participating).

Important milestones: Implementation of the EQF, NQF and the ECTS by 2016.

**2.4 R&D National Target: Increase R&D expenditure to 0,50% of GDP by 2020**  
*Dropped to 0,49% in 2011 (provisional figure) from 0,50% in 2010.*

In 2011, according to provisional figures, R&D expenditures as a percentage of GDP accounted for 0,49% compared to 0,5% in 2010. The national target for R&D expenditures as a percentage of GDP has been set to reach 0,50% by the year 2020, from 0,42% in 2008, taking seriously into consideration the particularities of Cyprus in terms of both the size of the research community, as well as the structure of the productive web (lack of big manufacturing firms) and the very small size of the Cypriot enterprises.

Cyprus is doing better in the innovation part, so there is an increased effort to develop the innovation ecosystem, cultivate innovative culture and establish Business Innovation Centers (BIC by EBN certification) to widen the possibilities of cooperation and the sectors where innovative activities take place. Private enterprises and private research centers had an increased participation in R&D projects during the last years as it is demonstrated from the results of the 7<sup>th</sup> Framework program. The number of applications for the last call of the program “Promoting Innovative Entrepreneurship – Develop and introduce products and services to the market” has been very satisfactory and there is a significant interest for a new call.

In addition, the Innovation Strategy is currently under review and a series of public consultations are taking place in order to help finalise the Strategy. The proposals for the creation of new support schemes currently reveal the need to address the key challenges that Cyprus faces while at the same time open cooperation opportunities with the other European Member States. The aim is to give the opportunity to all the enterprises, research institutes and public organizations to benefit from special schemes that will be promoted with financing from the structural funds. The schemes will address not only product/service innovation but also processes and organisational innovation. Emphasis will be given to social innovation so as to address the new economic crisis.

For the next programming period 2014 -2020 there are several proposals to increase the cooperation of Universities, research centers and private industries. One of the proposals is to develop infrastructure to house an Innovation Center near universities, where research centers and private companies along with labs, workshops and fast prototype facilities will coexist, cooperate and utilize synergies. The infrastructure will also be supported by soft services from Incubators and other Innovation support service providers.

Furthermore, a Smart Specialisation Strategy for Research and Innovation (RIS3) is currently under preparation and will be based, primarily, on the analysis of the local economy, the social structure and on innovation, in order to evaluate both existing qualifications and prospects for future growth. The analysis will cover three key dimensions:

- Research / Technological infrastructure
- Linkages with the rest of the world as well as the position of Cyprus in the European and in the global economy,
- The dynamics of the business environment



## 2.5 Climate and Energy National target:

- Achieve an increase of 14,3% (463 ktoe) in energy savings in the projected primary energy consumption of the year 2020  
*Reached 4,3% in 2011 compared to 1,8% in 2010*
- Reduce greenhouse gas emissions by 5% by 2020 compared to 2005.  
*Decreased by 2,7% in 2011 compared to 2005 levels*
- Increase of the contribution of Renewable Energy Sources (RES) to 13% of the total energy consumption by the year 2020  
*Reached 6,8% in 2011 compared to 5,8% in 2010*

### A. Energy Efficiency

Within the framework of the 2nd National Energy Efficiency Action Plan (2nd NEEAP), Cyprus has set a national indicative target for saving 14,3% primary energy in 2020. To achieve this target, an action plan has been adopted analyzing future steps and additional measures. Major contributor to achieving the target will be the introduction of natural gas to the national energy system (will contribute to 59% of the target) as well as the operation of Grant schemes for energy saving and domestic generation for RES, in all sectors (by 6%). Moreover, attempts for improvement of the energy efficiency of the Cypriot energy system must be focused on road transport, which is the sector that consumes by far the greatest part of non- electricity energy and will contribute by 12% to the target achievement. A good share of that 14,3% target will be met by the implementation of new EU policies, such as the new Energy Efficiency Directive, (will contribute to 13%) the recast directive for the energy performance of the buildings etc.

The reduction in primary energy consumption for the years 2010 and 2011 was higher than the reduction projected in the national energy efficiency scenario. More specifically, in 2010 the actual reduction was 1,8% and in 2011 was 4,3%, while the projected reductions were only 0,2% and 0,9% respectively. The assessment has also showed that the national energy intensity index for the years 2010 and 2011 is declining, indicating the effectiveness of the measures established in the two previous years and the improvement of the energy efficiency of the national economy. It should also be noted that, even though the reductions in primary energy consumption for the years 2010 and 2011 were higher than those projected, the achievement of the national 2020 target, is highly depended on the introduction of natural gas in the national energy system from 2015.

Conforming to article 3, article 24 and annex XIV part 1 of the Directive 2012/27/EE, Cyprus has already prepared the first report on the progress achieved towards national energy efficiency targets. The report will be communicated to the Commission before 30 April 2013.

- Hydrocarbon Exploration: Exploration for oil and gas offshore the Republic of Cyprus is in an ongoing phase. The Council of Ministers is responsible for granting licences for prospecting, exploration and exploitation of hydrocarbons. Applications for exploration and exploitation licences are accepted during licensing rounds. At present, an Exploration License for Block No 12 has been granted on 24 of October 2008. On 28 of December 2011 a natural gas discovery was announced indicating an estimated gross resource range of 5 to 8 trillion cubic feet (Tcf), with a gross mean of

7 Tcf. The Cyprus Block 12 field covers approximately 40 square miles and will require additional appraisal drilling prior to development.

On 11 February 2012, the Republic of Cyprus announced the second licensing round offshore Cyprus concerning the authorisation for hydrocarbon exploration in Blocks 1-11 and 13 of the Republics' Exclusive Economic Zone. On January 2013 licenses were granted for blocks 2, 3 and 9 and on February 2013 licenses were granted for blocks 10 and 11.

For Block 12 the "Appraisal Well" operations are anticipated to commence within the second half of 2013 and is estimated to reach its completion in the beginning of 2015. The Block 12 Development Plant consists of the Verification (exploratory) well drilling, the Reservoir appraisal and assessment, studies on the installation of offshore and onshore equipment, the completion of production of drilling and well, the installation of subsea system, the host commissioning of deep water and the installation of export pipe.

Studies are underway regarding the pipeline routing from the gas field to Cyprus' shore. The gas supply from Block 12 via pipeline is anticipated in 2017-2018. The political decision for the establishment of an onshore LNG plant has been taken and there is available land for the construction of up to 3 trains (5MT/year each). The plant will handle additional gas flows from other upstream fields (EEZ of the Republic of Cyprus and the neighboring countries). It is expected to be the largest investment in the island's history with an indicative timetable for its completion set in 2019.

With the recent natural gas discovery and the continuing hydrocarbon exploration activities offshore Cyprus, Cyprus' energy sector profile is set to change radically. Current developments include ongoing exploration activities, an interim solution for gas supply, a long-term solution for gas supply from indigenous sources and an LNG Plant for gas exports to EU and International Markets. In parallel, the installation of a gas export pipeline and a subsea power cable are under evaluation.

Other options for gas monetization could include Gas-to-Liquids (GTL) technology and a petrochemicals industry.

In addition, the Cyprus Natural Gas Company (DEFA) is planning the development of the internal pipeline network for the transmission of natural gas to the Power Stations at Vasilikos, Moni and Dekhelia. The project consists of two phases: (a) delivery of gas to EAC's Power Plants (at Vasiliko, Moni and Dekhelia) and (b) gas delivery to the Industrial sector (Power and thermal generation), Commercial sector (Thermal generation), Tourism industry (Thermal generation), Residential sector (far future) and Transportation.

## B. Renewable Energy

In accordance with the requirements of the European Directive 2009/28/EC for the promotion of the use of energy from renewable sources, Cyprus has the legally binding target to increase the contribution of renewable energy sources to 13% of the gross final energy consumption by 2020. Cyprus has already over-achieved its first and second indicative trajectory, which according to the provisions of the RES Directive, was

4,92% for the years 2011-2012, and 5,93% for the years 2013-2014, since the share of RES in the gross final energy consumption was 6,8%, in 2011.

In the action plan it is estimated that in order to achieve the target of 13% of RES to the gross final energy consumption by 2020, the contribution of RES must increase to 16% for electricity, 23,5% for heating/cooling and 4,9% for transport. More specifically, it is estimated that 300MW of wind parks, 192MW of photovoltaic systems, 17MW of biomass/biogas utilisation plants and 75MW of Concentrated Solar Thermal Plants must be installed so as to achieve 16% of RES contribution to the electricity production by the year 2020. The present status of RES (end of January 2013) in the electricity sector is encouraging since 146,7MW of wind parks 19,5MW of photovoltaic systems (autonomous and grid connected), and 9,4MW of biomass utilisation units have already been installed. Another 10 MW of biomass utilisation and 18,3MW of wind parks are under construction, while 50MW of photovoltaic systems and 10MW of wind parks are under evaluation.

- Net metering: Net-Metering is a policy that applies to distributed generator systems (more likely small domestic Photovoltaic Systems, or small combined heat and power systems) to be compensated when their systems generate more electricity than the generator/consumer is using in its premises. A pilot project was announced by the end of 2012 by CERA (Cyprus Energy Regulatory Authority), for 125 new Households installations for PV Systems up to 7KW, in order to assess the effects to the electricity marginal price and the effects to the Grid. In addition, there is a study going on for implementing the net metering to the self-producers for large scale systems.

In addition to the above, Electricity Authority of Cyprus (EAC) had tendered out for implementation of an Advanced Metering Infrastructure (AMI) in Cyprus. The system will be covering at least 3000 electricity meters and a few water meters. It is expected that a contract will be awarded before the end of 2013. The specifications that cover this first phase implementation are in line with the most update proposals of the EC and cover completely the functionalities that are included in the EC recommendations.

Following the implementation of the above project a full cost and benefit analysis will be submitted with recommendations for the roll out that will cover the whole of Cyprus, for achieving two way communication covering the needs for the water authorities as well.

Measures announced last April:

- **50% subsidisation of the cost of installing photovoltaic systems** by households will be offered based on financial and social criteria. It is estimated that 2000 households will benefit from this measure within 2013.
- Acceleration and immediate implementation of installation projects of photovoltaic parks with a total capacity of 50 MW. Also, the procedures for the issuing of licenses are accelerated, so that the 24 companies selected through tendering process can move forward in the realization of the projects. With the full implementation of projects generating electricity from solar energy, the following will be achieved: (i) fuel savings of around €51 mln annually, (ii) savings of €2 mln annually by reducing

the emission of pollutants, (iii) 650 or more jobs, and (iv) a contribution to the achievement of the obligation of Cyprus to increase the percentage of renewable sources to 13% by 2020.

### C. Reduction of GHG emissions

The goal for Cyprus is a reduction of the non-ETS emissions of 5% by 2020 compared to 2005. According to the latest greenhouse in 2011 the non-ETS emissions were reduced by 2,7%, while the total emissions in 2011 were reduced by 8,2% compared to 2005. Road transport remains the largest contributor to the non-ETS emissions (43%). The reason for the reduction of emissions is predominately the financial situation of the country. For the same reason, it is expected that the emissions of 2012 will be reduced even further. Information on the progress of implementation of measures to reach the goal allocated to Cyprus and any changes to the measures previously presented will be available later this year, when the greenhouse gases emissions' projections will be available.

No legislation is yet available for Cyprus to reach the 2020 effort sharing goal. While most other MS of the EU already had in place legislation defining the system for the reduction of emissions to be achieved, due to the UNFCCC and Kyoto targets, Cyprus is only not facing targets at EU and international level.

- **A modern and efficient public transport scheme:** the Government introduced in 2007 a Public Transport Enhancement Programme with the aim of increasing the use of public transport to at least 10% by 2020 and reduce the gas emissions. Public Transport services were of very low quality, covering only 2% of total daily trips, resulting in extensive use of private cars (85% of trips), a high cost to the economy and accentuating the problem with CO<sub>2</sub> emissions. Thus in July 2010 six new bus companies, one for each of the five districts and one for the intercity routes, commenced public transport service operations offering an upgraded service with longer hours, more frequent and shorter itineraries, as well as new bus routes, on the basis of public service contracts signed between them and the Government. The new companies are contracted to operate all urban and rural routes in their corresponding district. They also have the obligation to finance the renewal of their bus fleet within a specified time period. An overall increase of 24% in the use of public buses was recorded after the first year of operation of the new upgraded service. The intercity service recorded an increase of 39%.

#### **2.6 Competitiveness National Targets:**

- The promotion of Cyprus as an attractive regional centre for the provision of high value added services, including in the financial, legal, health, shipping and education sectors
- Strengthening the productivity of the economy so that the total labour productivity reaches the EU27 average
- Reduction of the administrative burden on national legislation by 20% by 2012
- Restructuring of the economy towards innovation

Strengthening the competitiveness of the economy is a basic prerequisite for economic growth and for the promotion of Cyprus into a regional service centre. Even though Cyprus has the second best most highly qualified labour force among EU27, with 34,5%

having tertiary education, the economy faces chronic competitiveness problems relating to the specialisation in low-skilled, low-technology sectors, making extensive use of low skilled labour, mainly from third countries, whereas many young university graduates remain unemployed/underemployed. Therefore, one of the main policy priorities, is the restructuring of the economy towards innovation by giving incentives and by shifting the emphasis towards high-skilled, high value-added activities, mainly in the services sector, including tourism, health and education. Cultivating an entrepreneurial and innovative culture is crucial towards the achievement of this challenge and thus, relevant Schemes such as the one for grants to strengthen the competitiveness of SMEs and for the Digital Entrepreneurship are promoted.

The performance of the Public Sector is a decisive factor to effectively face key challenges that arise as a result of technological developments, changing perceptions, increasing expectations of citizens and businesses and the need to be more cost-efficient, in the midst of the economic crisis. The modernisation of the public service is of high importance for the government, thus a Commissioner for the modernisation of the Public Service was appointed in order to promote the change in this area.

A number of measures are promoted to increase the competitiveness of both the private and the public sector and tackle the bottlenecks.

### **Improving the Competitiveness of the private sector and restructuring the economy**

- **Tourism Sector:** Tourism has traditionally been a major source of income and a driver of economic growth in Cyprus, as it is an important export sector and of great importance to domestic value added and employment. The improvement in tourist arrivals and incomes that started in 2011, continued more moderately in 2012, while the prospects for the continuation of that upward trend in 2013 are excellent. In particular, in 2012, there was an increase of 3,0% in tourist arrivals and 10,2% in revenue growth compared to 2011, while in 2011 there was a an increase of 10,1% in tourist arrivals and 12,9% in revenues in comparison with 2010. Given the significance of the sector to the economy, especially at the current juncture of great contraction of the financial sector, significant effort is put at enriching the tourist product and increasing competitiveness. Concerning particularly the issue of competitiveness, the competent Ministry (Ministry of Commerce, Industry and Tourism, MCIT) has entered into intensive talks with all relevant stakeholders in order to agree on ways to reduce the cost of the Cypriot holiday package in a comprehensive way. In this context, it is also important to mention that the Ministry of Commerce Industry and Tourism is promptly promoting the establishment of casinos in Cyprus. Also, taking into consideration the current economic situation, the Cyprus Tourism Organisation (CTO) is now proceeding with the revision and upgrading the Tourism Strategy 2011-2015, with the aim to improve the tourism sector business model, in particular, with a view to lengthening the tourist season, increasing occupancy rates of hotels and promoting resident tourism during winter time, developing a multi-dimensional and high quality tourism. Some of the most important envisaged actions in the sector are the following:

Actions/measures to further increase the competitiveness of the sector and reduce seasonality are the following:

- a) Enrichment of the “Sun and Sea” product with a variety of special interest products (the marine tourism, conference and incentives tourism, sport tourism, cycling, golf, weddings and honeymoon trips, hiking, religious and cultural tourism, health tourism, rural tourism, learning, cruising, gastronomic and wine tourism), aiming at enhancing the overall tourist experience, giving alternative options for activities and improving tourists’ satisfaction.
  - b) Special interest market segments/products: Due to the broad degree, good infrastructure, great quality and high level of professionalism of the offer of certain specific interest products, Cyprus succeeded in attracting special interest markets, other than the traditional “Sun and Sea” segment, that can definitely contribute positively in overcoming Cyprus tourism seasonality problems.
  - c) The strategically planned development of a balanced and a complete package of tourist special products aim to help Cyprus to move towards tourism sustainability.
  - d) Cooperate with Tour Operators to specifically allow for the addition of flights during the shoulder months, by cooperating with airlines to have them add new routes from main or regional airports and by carrying out own promotional and advertising activities in all markets of interest.
  - e) Alternative forms of tourism: CTO’s measures to encourage alternative forms of tourism (i.e. thematic tourism) include efforts to attract new investment towards the construction of big infrastructural projects (casinos, golf courts and marinas), by promoting Cyprus as a respective thematic destination, the exploitation of EU-co funding opportunities, the cooperation with local authorities and other government and private sector bodies (PPP’s) in a number of areas such as product development, organisation and promotion.
  - f) Condo hotel facilitation: It has been the subject of systematic deliberations between private and public stakeholders involved. CTO has prepared an extensive concept document involving all aspects of the project which could form the basis for enacting the necessary amendments of relevant laws and regulations, the removal of current legal impediments and the introduction of the scheme. The paper will be discussed with all stakeholders in order to formulate the final proposal which will then be submitted to the Council of Minister for decision.
- **Attracting Increased Foreign Investment:** Following the political agreement on the Programme, the Government has asked the Cyprus Investment and Promotion Agency (CIPA) to intensify its efforts in order to contribute to the promotion of Cyprus as an international investment and business centre. The Agency gives emphasis on placing Cyprus on the international business radar screen as a competitive regional hub in a wide range of sectors, thereby facilitating foreign investments in these sectors. To encourage foreign investment, it has been decided to grant a permanent residence permit to applicants who invest the total amount of €300,000 for the purchase of more than one house or other building, provided that the purchase will be made by the same vendor. To facilitate the process, simplification of the legislative framework is promoted to adopt a fast process of granting long stay permission.
  - **National Guarantee Fund for SMEs:** The setting of the Cyprus National Guarantee Fund for Small and Medium Enterprises (“CYNGF for SMEs”) is an initiative developed jointly by the European Investment Fund (EIF), the European Investment Bank (EIB) and the Ministry of Finance.

- **JEREMIE Initiative:** In order to improve SMEs access to finance, a total budget of €20 mln from the EU Structural Funds (ERDF) was allocated for the implementation of the JEREMIE initiative in Cyprus and two products were designed, the “Funded Risk Sharing Product” (FRSP) and the “First Loss Portfolio Guarantee Product” (FLPG), with the aim to offer new loans to SMEs with lower interest rates, longer loan repayment and grace periods and potentially lower collateral requirements. Up to 31 January 2013, 240 loans were approved under the first product, for a total committed principal amount of more than €18 mln, out of which €17,8 mln have been disbursed to eligible SMEs. In addition, up to 31 December 2012, 61 loans were approved under the second product and €2,8 mln were disbursed to eligible SMEs.

As the second product did not prove as attractive, an amount of €7,5 mln has been diverted to the first but, given the recent deteriorating conditions in the banking sector of Cyprus and the temporary restrictions currently in place on capital movement, the Bank of Cyprus, as the selected financial intermediary for JEREMIE products in Cyprus requested for a delay in the due diligence process that needs to be undertaken, in order for a new contractual agreement to be reached between the bank and the European Investment Bank.

- **Scheme for grants to strengthen the competitiveness of SMEs in the manufacturing sector:** The scheme aims at the financial support of the companies in the manufacturing sector in order to upgrade their technology and to promote innovation. The total budget is €26,7 mln for the programming period 2007-2013 (co-financed by Structural Funds (85%) and the Republic of Cyprus (15%). By the end of 2012, €15,3 mln have been granted to 271 eligible applicants. The remaining funds will be allocated among applicants whose applications have already been approved or are currently under evaluation. In addition, 335 new job positions have been created and 25 new manufacturing entities have been established.

Measures announced last April:

- Efforts to **reduce loan rates:** A relevant circular letter was issued and put in effect as of 1<sup>st</sup> of May imposing additional special equity in new and renewed deposits bearing interest beyond Euribor +3%, aiming at covering the risk that arise from high deposit rates and shifting the benefits from the reduction of deposit rates to loan rates.
- Legislation is being promoted for the protection of business’ owners. According to the legislation, the bank can buy the property at loan’s value and at the same time rent the property to the business’ owner for a specific time of period, and thus the business’ owner continues its operations.
- Businesses will benefit from a further 9,5% **reduction of electricity prices** and the scheme for **reducing electricity energy consumption** (see more information in Section 2.5).
- In order to help companies that are interested in participating in public tenders but face liquidity problems, it is decided to replace the security with a commitment not to withdraw the offer. Additionally, the level of security paid for faithful performance of the work is also reduced.

- The Government has decided that the level of rent charged at industrial areas will remain the same for the next 5 years.
- Reduction of the time needed to issue a **building permission**, so that it doesn't exceed one month for small development projects and three months for big development projects.

### **Improving the Efficiency of the Public sector**

- **Better Regulation:** Cyprus has set 20% as its national target for the reduction of AB in the national legislation by 2012, as it derives from its commitment to the European Commission. For achieving this target, measures aimed at modernisation and simplification of procedures in 8 sectors were implemented thus decreasing the administrative burden by 18% and 20% up to this June for the enterprises, which corresponds to about 1% of our national GDP.
- **Electronic Public Procurement System (e-PS):** The Government in its effort to create a helpful and user-friendly website regarding the public procurement developed the e-procurement system (e-PS). e-PS is a secure and interoperable web-based application of the Republic of Cyprus, which constitutes a total solution for the implementation of electronic procedures in conducting public procurement competitions. **Sustainable public procurement** is also promoted through the revision of the National Action Plan for Green Public Procurement. Its main aim is to include environmental considerations in the public procurements so as to boost the consumption of green products and services.
- **Point of Single Contact (PSC):** Within the scope of harmonization with the Services Directive, the Ministry of Commerce, Industry, and Tourism has established the Point of Single Contact in order to facilitate the establishment of businesses in the services sector and the cross border provision of services within internal market. During 2012, the PSC Cyprus Portal received approximately 80.000 visits and 45.000 unique visitors. Notably, the number of visits to the PSC Cyprus Portal has shown an increase in the range of 155% in 2012 compared to 2011; while the respective increase in unique visitors to PSC Cyprus Portal was in the range of 130%. Additional measures also included under the digital agenda below.

Measures announced last April:

- **Appointment of a Commissioner for the Public Service Reform**, in an effort to modernise and upgrade the Public Service, so that it can cope with modern demands and bring government services closer to the citizen. The Commissioner will develop within three months an action plan with specific recommendations for the reform of the public sector, with terms of reference which include among others:
  - a) Simplification of the structures and procedures followed
  - b) Strengthening, combination or elimination of services
  - c) Modernisation of the evaluation system of civil servants
  - d) Use of modern technological tools and introduction of eGovernment
  - e) Enhancing the skills of the human resource for fulfilling the objectives of the Public sector
  - f) Synergy of the Public and Private Sector



- g) Improving citizen service
- h) Reduction of Operating Expenses of the Public Service
- i) Adoption of codes of conduct on transparency
- j) Implementation of a time schedule for the whole Action Plan that should not exceed December 2013.

### 2.7 Digital Society National Targets:

- By 2013, all households and businesses will have access to the Internet with at least 2Mbps.
- By 2013, 70% of the enterprises will have access to the Internet with at least 20Mbps.
- By 2020 all households and businesses will have access to the Internet with at least 30 Mbps.

*Achieved 100% coverage of at least 2Mbps of all urban and rural areas since 2012.*

The Council of Ministers approved the Digital Strategy on February 8<sup>th</sup>, 2012, as committed. The Digital Strategy is a comprehensive plan for the period 2012-2020 and adopts a holistic approach for the development of information society in Cyprus. It focuses on six strategic objectives, (i) Connect Cyprus, (ii) Modernize public administration and provide public electronic services, (iii) Inclusion of all into digital Cyprus, (iv) Education and learning, (v) Digital entrepreneurship, (vi) ICT for the environment.

According to the Digital Strategy for Cyprus two annual reports are prepared:

- (i) **The annual Action Plan at the beginning of the year:** This report includes the actions of the Digital Strategy to be implemented in the next three years accompanied with a corresponding timetable, budget and competent authority for each action. The action plan is submitted to the Council of Minister for approval and it is published on the digital Cyprus web site [www.digitalcyprus.gov.cy](http://www.digitalcyprus.gov.cy). The Action Plan for 2013-2015 has been approved by the Council of Ministers on November 2012. We are currently preparing the Action Plan for 2014-2016.
- (ii) **The annual Progress Report by the end of each year:** This report summarizes the progress of the actions of the Digital Strategy for Cyprus, including the evaluation of the progress of the broadband targets. The purpose of this report is to identify the areas at which more effort is required and, where appropriate, necessary indicate corrective measures. The progress report is submitted to the Council of Ministers for its information and is published on the digital Cyprus web site [www.digitalcyprus.gov.cy](http://www.digitalcyprus.gov.cy). The draft Progress Report for 2012 has been prepared and will be presented to the Advisory Committee. The progress report will be submitted to the Minister for approval at early April and thereafter the Minister will inform the Council of Ministers. The target date for its publication is May 2013.

According to the draft Progress Report for 2012 the progress on the main Objectives of the Digital Strategy is:

**(i) Connect Cyprus:** Cyprus has achieved 100% coverage of at least 2Mbps of all urban and rural areas since 2012. The focus now is to achieve the broadband targets of 2020 (namely: by 2020, all households and businesses shall have access to the Internet with at least 30 Mbps and by 2020, 50% or more of the households shall have access to the Internet with at least 100 Mbps). Therefore a National Broadband Plan has been prepared, which is embedded on the Digital Strategy and includes:

- a) The existing broadband networks (wireless and wired)
- b) The plans of the operators to achieve the broadband targets of 2020
- c) The efforts of the Government to promote consultations between relevant players in order to agree a common framework for the deployment of a single FTTH network in urban and sub-urban areas where all players will have equal access and there will be no competitive advantage to the owner. This network, which can be called “utility network”, will extend from the customer’s premises to the concentration points. The plan is to use as much of the existing infrastructure as possible
- d) The Government efforts for financial support for the development of a New Generation Access Network from Structural Funds in the New Programming Period
- e) The regulatory framework that is in place and helps the development of high-speed internet infrastructure. This includes the adoption of the revised EU framework for electronic communications
- f) The spectrum policy, where the procedure for the authorization of the available spectrum in the frequency bands 800 MHz, 900 MHz, 1800 MHz, 2100 MHz and 2.6 GHz has been initiated and will be completed by the end of 2013. These frequencies will be used for the deployment of national broadband wireless networks (3G and 4G networks) that will provide a variety of new services with higher data rates to the public. Also, there is an ongoing parallel procedure for the amendment of the authorizations of the current mobile operators in order to be allowed to use new technologies in the 900MHz, 1800MHz and 2100MHz bands. It is foreseen that special obligations will be imposed to existing and to possible new operators including coverage and data rate obligations that will contribute towards the achievement of national broadband targets
- g) The mapping of the existing broadband infrastructure
- h) The Network and information security policy that has been approved by the Council of Ministers in February 2013 and the operation of the Cyprus Government CERT in 2013.

**(ii) Modernise public administration and provide public electronic services:**

The need for a general reorganization and modernisation of the public sector and local authorities, with the widespread use of ICT (achieve a paperless government and promote the development of all public services electronically) is still valid. Although significant progress has been made in the delivery of electronic public services mainly for companies and for the citizens there is still a lot to be done:

- a) Public sector: The study for the Next Generation Network (NGN) for the public sector will be completed at the beginning of 2013; the roll out of the web-enabled version of the Office Automation System (eOAS) in all government departments continues and it will be completed by the end of 2014; the revised Information Systems Strategy will be prepared by the end of 2013; the development of the Government Secure Gateway will be completed by 2014; the Central Government Data Warehouse will be completed by 2015; the Help Desk

System is on a pilot phase since the beginning of 2013; the e-filing system for online registration of companies is under development; the expansion of the Point of Single Contact (PSC) will be completed by the end of 2014; online payments to the Government are already offered for many public services; incentives to citizens to use the available e-government services are given; the consolidation of the several datacenters of the government into 3-4 major datacenters will begin with the Ministry of Labour and Social Insurance being the first priority; and the establishment of more Citizen Service Centers (CSCs) all over the country continues

- b) Local authorities: The study for the development of a centralised information management system that will be used to serve all municipalities will be completed by the end of 2013.
- c) eHealth: The implementation of the Integrated Health Care Information System in all public hospitals and health centers will continue with the installation of the system in all other hospitals and is expected to be completed by the end of 2017. The drug management system will be installed in all public hospitals and health centers until the end of 2013 and one programme under the Ambient Assisted Living (AAL) will be completed in 2013.
- d) eID: The eID to every citizen which will include personal identity data, biometric data and store advanced certificate for the creation of qualified signatures and other data will be completed by the end of 2013. The implementation of the legal framework for electronic signatures (esignatures) will be completed by the beginning of 2013. DITS will become Government Certification Service Provider by the end of 2013.

**(iii) Digital Entrepreneurship:** A new subsidy program has been introduced for SMEs to develop innovative ICT products or services until 2013 and a new subsidy program for financial support of companies to use ICT for their internal procedures and for the provision of customer services (eBusiness) is under study. Also incentives are given to businesses to use public electronic services.

### 3. EURO PLUS PACT

In March 2011, euro area Member States and six non Euro area Member States agreed on the “Euro Plus Pact” which required these countries to make voluntary commitments in the areas of competitiveness, employment, sustainable public finances and financial stability, going beyond what had been agreed at EU level. Member States national commitments are integrated in the NRP and SP and assessed within the framework of the European semester. The results of this assessment are taken into account in the recommendations. Progress with respect to the national commitments of Cyprus, is presented below.

#### A. Fostering competitiveness

1. **Containment of public sector wage bill:** In the context of the Memorandum of Understanding, a number of measures have been implemented in this area, analysed in Section 4 below, under CSR 1.

2. **Strengthen the competitiveness of SMEs in the manufacturing sector:** the scheme aims at the financial support of the companies in the manufacturing sector in order to upgrade their technology and to promote innovation with a total budget of €26,7 mln for the programming period 2007-2013 (co-financed by Structural Funds (85%) and the Republic of Cyprus (15%)). More information is provided in Section 2.6 (Poverty national target).

3. **Enhancing digital economy:** The Digital Strategy was approved by the Council of Ministers on 8 February 2012 and is gradually being implemented. More analysis is provided in Section 2.7 (Digital Society national target).

4. **Measures for energy efficiency and promotion of RES:** information is given in Section 2.5 (Climate and Energy national target).

#### B. Fostering employment

1. **Exploit job creation possibilities by improving the competitiveness of enterprises.** Information is provided in Section 4, under CSR 5.

2. **Labour market reforms to reduce undeclared work:** Despite the enhancement of inspection mechanisms, undeclared and illegal work is still at high levels as a consequence of the crisis. More analysis on this issue can be found in Section 2.1.

3. **Strengthening the links between technical vocational education, training and the labour market:** The PSITVE were established by September 2012. More analysis on this measure can be found in Section 2.3.

#### C. Contributing further to the sustainability of public finances

Detailed information on related measures is provided in Section 4, under CSRs 1&3.

#### **D. Reinforcing financial stability**

All measures agreed with Troika are presented in Section 4 under CSR 2.

#### **4. COUNTRY SPECIFIC RECOMMENDATIONS**

In the context of the second European Semester, the Commission carried out a comprehensive analysis of Cyprus's economic policy, by assessing both the Stability Programme and the National Reform Programme on EU2020, and by also carrying out an in-depth review. Following on this assessment, the Commission proposed to the European Council seven recommendations which were officially adopted by the Council on 6 July 2012.

In this section an analysis of the progress achieved towards the implementation of the recommendations 3-7 that relate to the NRP, is given:

##### ***CSR 1: Concerns the Stability Programme***

*Take additional measures to achieve a durable correction of the excessive deficit in 2012. Rigorously implement the budgetary strategy to ensure the achievement of the medium-term budgetary objective (MTO) by 2014 and compliance with the expenditure benchmark and ensure sufficient progress with the debt reduction benchmark. Accelerate the phasing-in of an enforceable multiannual budgetary framework with a binding statutory basis and corrective mechanism. Take measures to keep tight control over expenditure and implement programme and performance budgeting as soon as possible. Improve tax compliance and fight against tax evasion.*

In the context of the Programme, the following measures have been implemented:

##### **1. Containment of public sector wage bill:**

- A scaled reduction in emoluments of public and broader public sector pensioners and employees as follows: EUR 0-1.000: 0%; EUR 1.001-1.500: 6,5%; EUR 1.501-2.000: 8,5%; EUR 2.001-3000: 9,5%; EUR 3.001-4.000: 11,5%; above EUR 4.001: 12,5%.
- Implementation of a scaled reduction in emoluments of public and broader public sector pensioners and employees as follows (to be applied retroactively from 1 January 2013): €0-2.000: 0,8%; €2.001-3.000: 1%; €3.001-4.000: 1,5%; above €4.001: 2,0 %.
- Extension of the suspension of the practice of COLA for the public and broader public sector until the end of the Programme (2016). Extension of the freeze of increments and general wage increases in the public and broader public sector and temporary contribution in the public, broader public and private sectors on gross earnings and pensions by three additional years until 31 December 2016.
- Reduction of the number of public sector employees by at least four thousand five hundred over the period of 2012-16 by: i) freezing the hiring of new personnel on first entry posts in the broader public sector for three additional years until 31 December 2016; ii) implementing a policy of recruiting one person for every four retirees (horizontal); iii) introducing measures to increase the mobility of civil

servants within and across line ministries; and iv) implementing a four-year plan aimed at the abolition of at least 1.880 permanent posts.

- Freeze of the hiring of new hourly paid employees and enforce immediate application of mobility within and across ministries and other government entities. In the case of health and security posts, recruitment of one person for every five retirees will be possible to meet urgent needs.
- Reduction of at least €9 mln in the total outlays of allowances for employees in the public and broader public sector.

Moreover, in the Programme, the following additional measures are included:

- Adjust working time in the Public Service by making it more flexible so that to reduce overtime and related costs to the public sector wage bill. Working hours outside regular working time should be limited by enforcing strict controls, including requiring pre-approval of any non-emergency work outside regular working time.
- The Government will commission an independent external review of possible further reforms of the public administration based on the terms of reference already agreed with the programme partners.

### **Budgetary Framework**

For ensuring fiscal sustainability, a modern framework for fiscal management has been promoted, with the enactment of a Law on Budgetary Stability, establishing principles of transparency and reliability and incorporating a set of fiscal rules and an automatic correction mechanism in primary legislation. The Law provides for the achievement of the Medium-Term Budgetary Objective over the medium term, through the introduction of an expenditure and debt brake rules. The Law also provides for the introduction of a Medium-Term Budgetary Framework, which intends to lead to a containment of expenditures by line ministries and, at the same time, promote the reallocation of expenditure in favour of growth - enhancing activities, consistent with the priorities set by the National Reform Programme.

It is noted that the budgetary target for 2013 was accompanied by expenditure ceilings for the budget years 2013-2015 for each government entity. The 2013-2015 expenditure ceilings will evolve into a full-fledged Fiscal Strategy Statement in line with the MTBF requirements contained in Directive 2011/85/EU. Any deviation from the budgetary objectives contained in the 2013-2015 framework will be properly documented and reasons for such deviations will be provided.

#### ***CSR 2: Concerns the Stability Programme***

*Further harmonise the supervisory and the regulatory framework for the cooperative credit societies in line with the standards applied for the commercial banks. Strengthen regulatory provisions for the efficient recapitalisation of the financial institutions in order to limit exposure of the financial sector to external shocks.*

The political agreement reached by the Eurogroup on 25 March 2013, included the restructuring and substantial downsizing of the banking sector. The domestic banking sector, including the cooperative credit institutions, represented until recently 550% of GDP. The necessary downsizing and restructuring of the banking sector is already under

way. The House of Representatives adopted legislation on 22 March 2013 establishing a comprehensive framework for the recovery and resolution of credit institutions.

Under the terms of that legislation, the Central Bank of Cyprus (CBC) is the single resolution authority for banks and cooperative credit institutions. Using this new framework, the Government has proceeded with (i) the carve-out of the Greek operations of the largest Cypriot banks, (ii) the resolution of Cyprus Popular Bank and the absorption of selected assets and liabilities by the Bank of Cyprus and (iii) the recapitalisation of the Bank of Cyprus through a debt to equity conversion, without the use of public money. As a result of these actions, the Cypriot banking sector was downsized significantly.

Furthermore, Cyprus has agreed with Troika to undertake the following measures:

- ensure that the liquidity situation of the banking sector will be closely monitored and appropriate measures to maintain sufficient liquidity in the system in line with Eurosystem rules will be taken. The regulations on the minimum liquidity requirements will be updated to prevent concentration in euro-denominated assets in the future. To preserve the liquidity of the Cypriot banking sector, administrative measures have also been imposed.
- establish an independent valuation of the assets of Bank of Cyprus and Cyprus Popular Bank and quickly integrate the operations of Cyprus Popular Bank into Bank of Cyprus. The valuation should be completed quickly so as to enable the unfreezing of the relevant parts of the uninsured deposits at the Bank of Cyprus;
- adopt the necessary regulatory requirements regarding an increase in the minimum core tier 1 capital adequacy ratio to 9% by end of 2013;
- ensure that a credit register is created, that the current regulatory framework on loan processes is reviewed and amended, if necessary, and that legislation strengthening the governance of commercial banks is adopted;
- strengthen banks' governance, including by prohibiting lending to independent board members or their connected parties;
- maximise recovery for non-performing loans, while minimising incentives for strategic default by borrowers. This will include easing constraints on the seizure of collateral and proper monitoring and managing of non-performing loans. The Central Bank of Cyprus will issue guidance to classify as non-performing all loans past due by more than 90 days;
- align the regulation and supervision of cooperative credit institutions to those of commercial banks;
- ascertain the viability of cooperative credit institutions and develop, in consultation with the Commission and informing the ECB and the IMF, a strategy for the future structure, functioning and viability of the cooperative credit institution sector.

*CSR 3: Further improve the long-term sustainability and adequacy of the pensions system and address the high at risk of poverty rate for the elderly. Align the statutory retirement age with the increase in life expectancy.*

Within the context of combating the effects of demographic ageing on the Social Insurance Scheme, the Government has adopted in 2009 measures to safeguard the long-term financial sustainability of the Social Security Scheme at least until 2048.

On the basis of Council Recommendation 3, Cyprus introduced in 2012 additional measures which were also the subject of substantive negotiations with Troika following the request by the Republic of Cyprus for a financial bailout.

Within this framework, Cyprus has introduced measures which took effect as of 1 January 2013. These measures include: an actuarial reduction for early retirement in conjunction with a planned increase in the minimum age for entitlement to an unreduced pension to reach 65 by 2016, an increase of the contributions, as of 1 January 2014 of salaried employees and employers to the General Social Insurance Scheme (GSIS) by an additional 1p.p. of the increase which was provided to be implemented in 2014 on pensionable earnings and the freeze of pensions under the Social Security Fund for the period 2013-2016.

Measures were also taken to ensure the long term sustainability of the supplementary occupational pension scheme of government employees (GEPS) and of the supplementary pension schemes of the broader public sector. The measures include a gradual increase of the statutory retirement age by 2 years, an increase of the minimum age for entitlement to an unreduced pension to be in line with the statutory retirement age; while preserving acquired rights, an introduction of an early retirement penalty of 0,5% per month of early retirement so as to make early retirement actuarially neutral, and the freeze of public sector pensions for the period 2013-2016.

The General Social Insurance scheme as well as the occupational pension schemes of the government employees and of the employees in the broader public sector have also introduced an automatic adjustment of the statutory retirement age every 5 years in line with changes in life expectancy at the statutory retirement age, to be applied in 2018 and the first revision will cover the period 2018-2023.

CSR 3 also calls for Cyprus to address the high at-risk-of-poverty rate for the elderly. In this respect, despite the large cuts in public expenditure the government has implemented (as a result of the request of Cyprus for a financial bailout), the Council of Ministers in direct response to CSR3 has approved the continuation of the Income Support Scheme for Low Income Pensioners for 2013.

Furthermore, in order to address the **high-at-risk-of poverty rate for the elderly** low income pensioners received in 2012 **the Easter Grant to pensioners with low income**, a one off payment of €70 that was granted to every pensioner in a household whose total annual income was below €13.390 (household of one person). As per the provisions of the Programme there will be **further streamlining of the Easter allowance to pensioners** by limiting the benefit to pensioners with a monthly per capita pension of at most €500.

The poverty rates are monitored and the decreases in the rate of poverty among pensioners aged 65+ indicate that the measures already implemented in respect of low pensions are on the right track. Poverty among pensioners aged 65+ continues to decline from 40% in 2010 to 36,9% in 2011. In addition, a study will be carried out using micro simulation modelling techniques to assess/monitor the impact of those measures on an individual/household basis.

In addition, an actuarial study for the GSIS will be carried out by end of June 2013 to provide additional reform options to ensure the long-run viability of the national



pension system. The actuarial study will project the scheme's finances on a cash basis. The study will analyse the impact of additional reform options while considering adequacy taking into account the impact on labour costs.

*CSR 4: Complete and implement the national healthcare system without delay, on the basis of a roadmap, which should ensure its financial sustainability while providing universal coverage.*

At the end of June 2012, the Council of Ministers approved the proposal for the Implementation of the National Health Insurance System (NHIS). According to the roadmap prepared by the Health Insurance Organisation (HIO) for the implementation of the National Health System (NHS), commencement of the scheme is envisaged for 2015. Within the Programme the following measures are related to the implementation of the NHS and for improving the quality and efficiency of the health care system:

**a) Complete and implement the national healthcare system:**

To strengthen the sustainability of the funding structure and the efficiency of public healthcare provision, the following measures will be adopted prior to the granting of the first disbursement of financial assistance:

- a) abolish the category of beneficiaries class "B" and all exemptions for access to free public health care based on all non-income related categories except for persons suffering from certain chronic diseases depending on illness severity. Introduce as a first step towards a system of universal coverage a compulsory health care contribution for public servants and public servant pensioners of 1.5% of gross salaries and pensions. The measure will be reviewed by Q2-2014 with the programme partners. For families with three or more dependent children, the participation in this health care scheme will be voluntary;
- b) increase fees for medical services for non-beneficiaries by 30% to reflect the associated costs of medical services and create a co-payment formula with zero or low admission fees for visiting general practitioners, and increase fees for using higher levels of care for all patients irrespective of age;
- c) introduce effective financial disincentives for using emergency care services in nonurgent situations;
- d) introduce financial disincentives (co-payment) to minimise the provision of medically unnecessary laboratory test and pharmaceuticals; and
- e) adopt a new decision by the Council of Ministers concerning a restructuring plan for public hospitals, improving quality and optimising costs and redesigning the organisational structure of the hospital management, by putting into practice recommendations from the 2009 "Public Hospital Roadmap".

In addition, the programme partners will review and be consulted on the following measures before their implementation:

- f) assess and publish, before parliamentary discussion, the potential risks and benefits of the planned introduction of the National Health System (NHS) in an updated actuarial study, taking into account possible proposals for implementing NHS in stages by Q2- 2013;
- g) make the award of the tender for the IT-infrastructure conditional upon the results of the study and the decision for implementing the NHS;

- h) review income thresholds for free public health care in comparison to the eligibility criteria for social assistance while ensuring that co-payments to public health care are set so as to protect individuals/households effectively from catastrophic health expenditures by Q4-2013;
- i) create protocols for laboratory tests and the prescription of pharmaceuticals based on thorough scientific evidence;
- j) introduce a coherent regulatory framework for pricing and reimbursement of goods and services based on the actual level of costs incurred in accordance with Article 7 of Directive 2011/24/EU of the European Parliament and of the Council of 9 March 2011. An interim report will be ready by Q3-2013;
- k) conduct an assessment of the basket of the top 4 publicly reimbursable healthcare products in terms of annual spending and prepare a report to establish an integrated system for health-technology assessment to increase the cost-effectiveness of the basket of publicly reimbursed products; and prepare the implementation of 10 new clinical guidelines focusing on high annual volume and high cost diseases by Q2-2013;
- l) start coding inpatient cases by the system of diagnosis-related groups (DRGs) with the aim of replacing the current hospital payment system by payments based on DRGs by Q3-2013;
- m) in a first step, establish working time in the Health Service, in conjunction with moving the starting time by half an hour (from 7.30 to 8.00) and extending the flexibility period from a half to one hour. With this modification, the weekly working hours of public officers remain unchanged, but are distributed throughout the year as follows: 37 ½ hours per week, 7 ½ hours per day, daily (Monday to Friday): 8.00/9.00 to 15.30/16.30. The same applies for the transitional period of 1.1.2013-31.8.2013 but the starting time remains the same (7:30) and thus the ending time is moved back by half an hour (15:00/16:00). Following a review, in a second step, revise the regular working hours and stand-by shifts of healthcare staff, including rules to increase the mobility of staff; revise current regulations on overtime pay and fully implement existing laws on recording/monitoring overtime payments (see 3.11) by Q1-2014; and
- n) define a basket of publicly-reimbursable medical services based on objective, verifiable, criteria, including cost-effectiveness criteria by Q2-2013.

Furthermore, the Cypriot authorities will consider establishing a system of family doctors acting as gate-keepers for access to further levels of care.

**b) ensure its financial sustainability while providing universal coverage:**

As per provisions in the Programme, the Cypriot authorities have prepared a revised Bill concerning the billing of both in out-and in-public medical care which currently is at the consultation stage with Troika.

The following cost containing and structural measures are included in the Programme and currently considered by the Ministry of Health with the cooperation of the HIO before their implementation within the time margins attached to each measure:

- abolish the category of beneficiaries class "B" and all exemptions for access to free public health care based on all non-income related categories except for persons suffering from certain chronic diseases depending on illness severity, while leaving the current threshold for beneficiaries class "A" unchanged [Q2-2013]

- increase fees for medical services for non-beneficiaries by 30% to reflect the associated costs of medical services and create a co-payment formula with zero or low admission fees for visiting general practitioners, and increasing fees for using higher levels of care for all patients irrespective of age [Q1-2013].

*CSR No. 5: Improve the skills of the workforce to reinforce their occupational mobility towards activities of high growth and high value added. Take further measures to address youth unemployment, with emphasis on work placements in companies and promotion of self-employment. Take appropriate policy measures on the demand side to stimulate business innovation.*

In response to the measures for the 2012 CSR, the following actions were promoted:

- Post Secondary Institutes of Vocational Education and Training were established and are currently operating in all major cities of the Republic offering training and retraining opportunities to 196 students
- The Restructuring and Modernising the education system by modernising and upgrading the curriculum for all public schools (pre-primary to upper secondary education) with a budget of €1,5 mln per year (2011-2016) continues as an ongoing priority
- The Pre-service Training Program of Candidates for Appointment of Teachers of Lower and Upper Secondary Education (€15,1 mln co-funded by ESF) as well as the In-Service Training Program of teachers (€5,7 mln co-funded by ESF) continue their implementation.

To address the policy objective as regards to the increase of technical and vocational education opportunities and the attractiveness and matching of specialisations offered with the current needs of the labour market, an upgrade of Vocational Education and Training measure has been foreseen (implementation period 2012-2015, with no estimated budget at present).

Continuation of measures taken previously are the following:

Continuation of the measures that were introduced with a three year time frame implementation in 2009 were continued or adapted. The actual expenditure for these schemes in 2012 was €6,8 mln (co funded by ESF) and included: company incentive schemes, job placements, training of the unemployed, training programmes for upgrading the skills of the unemployed, on the job training programmes for the prevention of layoffs, and enhancement of Public Employment Service.

For the promotion of flexible forms of employment a subsidy scheme which provides incentives to employers to hire unemployed or inactive individuals was continued and social care services to women was subsidised (actual expenditure for both in 2012: €1,45 mln) for the reconciliation of work and family life.

A series of annual and ad hoc studies and surveys are in place to anticipate the needs of the economy, the employment and training needs, such as the study for the identification of the green skills needs and the study on the identification of employment and training needs for the effective utilisation of natural gas in Cyprus.

Emphasis on youth employment:

As regards the measures for the promotion of youth employment, a total budget of 30,9 mln has been allocated (mostly co funded by ESF) for improving the basic skills and address the drop-out and early school leaving by providing alternative pathways to young

people such as the New Modern Apprenticeship Scheme that was launched in September 2012, job placements and training of young unemployed tertiary education graduates and introduction of a new subsidised employment scheme that was launched in May 2012 targeting the young and the long term unemployed. In addition to the above measures which are in line with the priorities set in the AGS of 2012 and the guidelines of the Youth Opportunities Initiative, two new schemes will be introduced to increase youth employment or enhance their employability. One of the two schemes was launched in March 2013 and it is a grant scheme to support youth employment by subsidizing new businesses to hire young unemployed (€3 mln), and the other project that is expected to be launched in June 2013 will offer guidance and /or placements in companies to the young unemployed to gain work experience (€4,2 mln).

#### Measures to stimulate business innovation:

- A scheme that promotes the development of innovative products and services by SMEs. The deadline for the first call was on 30 October 2012. 83 proposals have been accepted and are being evaluated. The next step is to award the contracts to the best proposals and issue a new call if the budget is not exhausted. 10% of the evaluation of the proposals is for the contribution to the Europe 2020 target. Some proposals will hire new personnel for the project while others when the project succeeds in the market. The planned budget for this scheme is €4 mln.
- More measures to stimulate business innovation include a scheme for grants to companies in the manufacturing sector in order to upgrade their technology and to promote innovation and a grant scheme in the manufacturing and trading of agricultural and forestry products in order to invest in new machinery/equipment and the transfer of know-how (please see Section 2.6).

*CSR No. 6: Remove unjustified obstacles in service markets, in particular by improving the implementation of the Services Directive in service sectors with the most growth potential (including tourism) and by opening up the provision of professional services.*

In order to remove unjustified obstacles in services markets several measures have been promoted. The amending legislation that entered into force in 2012 concerns the Law and Regulations on Tourism & Travel Offices and Tourist Guides, the Law on Car rental services, the Law on Scientific and Technical Chamber of Cyprus (ETEK) and the Code of Conduct of ETEK members Regulation/Architects, Engineers, the Regulations on Private Gyms, the Law and Regulations on Private Employment Agency, the Municipalities' Law and the Communities' Law.

The sector specific legislation pending before the House of Representatives (discussions have already started in the relevant Parliamentary Committees) concerns the Law on Registration and Control of Building Contractors and Contractors for Civil engineering Work/Construction Services, the Foreshore Protection Law and Regulations/Tourism services on beaches and the Private Higher Education Institutes Law.

Finally, for completing the sectoral transposition in relation to the Services Directive and in accordance with the provisions of the Programme and the consultations between the Ministry of Finance and Troika, in early January 2013 the Ministry of Finance sent to Troika for comments the two last pieces of legislation with respect to the Law on Driving schools and Driving Instructors and the Opticians Law.

Troika came back with written comments and requested clarifications on the above two legislations. In response to the above the competent authorities revised draft amending laws (driving instructors/driving schools, opticians) which were subsequently forwarded to Troika for endorsement prior to their submission to the Council of Ministers for approval and thereafter to the House of Representatives for enactment.

*CSR 7: Improve competitiveness including through the reform of the system of wage indexation, in consultation with social partners and in line with national practices, to better reflect productivity developments. Take steps to diversify the structure of the economy. Redress the fiscal balance by restraining expenditure.*

To ensure that wage growth better reflects developments in labour productivity and competitiveness, in both expansions and recessions, the Cypriot authorities will reform the wage-setting framework for the public and private sector in such a way as to improve real wage adjustment. To this end, the effective application of the reform of the wage indexation system (COLA) applicable to the broader public sector, as determined in the budget of 2013 and embedded in the Medium-Term Budget, will be ensured. This reform acts on relevant elements of the indexation system, as follows:

- a lower frequency of adjustment, with the base period for calculating the indexation (COLA) being lengthened from the current period of six months to twelve months. Indexation would take place on 1st January each year;
- a mechanism for automatic suspension of application and derogation procedures during adverse economic conditions, such that if in the second and third quarters of a given year negative rates of growth of seasonally adjusted real GDP are registered, no indexation would be effected for the following year; and
- a move from full to partial indexation, with the rate of wage indexation being set at 50% of the rate of increase of the underlying price index over the previous year.

The suspension of wage indexation in the wider public sector will remain in place until the end of the programme (end-Q1-2016).

A tripartite agreement will be pursued with social partners for the application of the reformed system in the private sector [end-2013]. Furthermore, based on the current economic outlook, wage and salary indexation is foreseen not to be applied in the private sector until 2014.

## ANNEX I

Table 1: General government budgetary prospects

	ESA Code	Year 2012	Year 2012	Year 2013	Year 2014	Year 2015	Year 2016
		Level	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
<i>Net lending (EDP B.9) by sub-sector</i>							
<b>1. General government</b>	S.13	-1,127.3	-6.3	-6.0	-7.6	-5.7	-2.2
<b>2. Central government</b>	S.1311	-1,289.8	-7.2	-4.9	-6.7	-5.0	-1.6
<b>3. State government</b>	S.1312	M	M	M	M	M	M
<b>4. Local government</b>	S.1313	-8.0	0.0	0.0	-0.1	0.0	0.0
<b>5. Social security funds</b>	S.1314	170.5	1.0	-1.1	-0.9	-0.6	-0.6
<i>General government (S13)</i>							
<b>6. Total revenue</b>	TR	7,150.2	40.0	41.3	42.3	42.6	42.5
<b>7. Total expenditure</b>	TE <sup>1</sup>	8,277.5	46.4	47.3	49.9	48.3	44.7
<b>8. Net lending/borrowing</b>	EDP B.9	-1,127.3	-6.3	-6.0	-7.6	-5.7	-2.2
<b>9. Interest expenditure</b>	EDP D.41	564.1	3.2	3.6	3.4	3.5	3.4
<b>10. Primary balance<sup>2</sup></b>		-563.2	-3.2	-2.4	-4.2	-2.1	1.2
<b>11. One-off and other temporary measures<sup>3</sup></b>		-159.0	-0.9	1.4	0.0	0.0	0.0
<i>Selected components of revenue</i>							
<b>12. Total taxes (12=12a+12b+12c)</b>		4,623.3	25.9	28.3	29.2	29.3	29.4
<b>12a. Taxes on production and imports</b>	D.2	2,640.1	14.8	15.4	15.7	15.9	15.9
<b>12b. Current taxes on income, wealth, etc</b>	D.5	1,980.8	11.1	12.9	13.4	13.4	13.5
<b>12c. Capital taxes</b>	D.91	2.4	0.0	0.0	0.0	0.0	0.0
<b>13. Social contributions</b>	D.61	1,634.0	9.2	8.5	9.3	9.4	9.4
<b>14. Property income</b>	D.4	137.1	0.8	1.1	0.6	0.6	0.6
<b>15. Other<sup>4</sup></b>		755.8	4.2	3.4	3.3	3.3	3.1
<b>16=6. Total revenue</b>	TR	7,150.2	40.0	41.3	42.3	42.6	42.5

<b>p.m.: Tax burden</b> (D.2+D.5+D.61+D.91-D.995) <sup>5</sup>		6,254.9	35.0	36.8	38.4	38.7	38.8
<i>Selected components of expenditure</i>							
<b>17. Compensation of employees + intermediate consumption</b>	D.1+P.2	3,727.0	20.9	22.3	22.7	22.2	21.4
17a. Compensation of employees	D.1	2,819.6	15.8	16.7	16.9	16.4	15.7
17b. Intermediate consumption	P.2	907.4	5.1	5.6	5.8	5.8	5.6
<b>18. Social payments</b> (18=18a+18b)		2,700.6	15.1	16.2	16.8	16.7	16.4
18a. Social transfers in kind supplied via market producers	D.6311, D.63121, D.63131	8.7	0.0	0.1	0.1	0.1	0.1
18b. Social transfers other than in kind	D.62	2,691.9	15.1	16.1	16.8	16.6	16.4
<b>19=9. Interest expenditure</b>	EDP D.41	564.1	3.2	3.6	3.4	3.5	3.4
<b>20. Subsidies</b>	D.3	94.8	0.5	0.6	0.6	0.6	0.6
<b>21. Gross fixed capital formation</b>	P.51	484.7	2.7	2.7	2.8	2.9	2.9
<b>22. Other<sup>6</sup></b>		706.3	4.0	2.0	3.5	2.4	0.1
<b>23=7. Total expenditure</b>	TE1	8,277.5	46.4	47.3	49.9	48.3	44.7
p.m.: Government consumption (nominal)	P.3	3,499.3	19.6	20.9	21.4	20.8	20.1
<sup>1</sup> Adjusted for the net flow of swap-related flows, so that TR-TE=EDP B.9.							
<sup>2</sup> The primary balance is calculated as (EDP B.9, item 8) plus (EDP D.41, item 9).							
<sup>3</sup> A plus sign means deficit-reducing one-off measures.							
<sup>4</sup> P.11+P.12+P.131+D.39+D.7+D.9 (other than D.91).							
<sup>5</sup> Including those collected by the EU and including an adjustment for uncollected taxes and social contributions (D.995), if appropriate.							
<sup>6</sup> D.29+D4 (other than D.41) + D.5+D.7+D.9+P.52+P.53+K.2+D.8.							

**Table 2: General government expenditure by function**

<i>% of GDP</i>	COFOG Code	<b>Year 2010</b>	<b>Year 2015</b>
1. General public services	1	10.7	12.0
2. Defence	2	2.4	1.5
3. Public order and safety	3	2.4	2.0
4. Economic affairs	4	3.9	5.0
5. Environmental protection	5	0.3	0.5
6. Housing and community amenities	6	2.8	2.0
7. Health	7	3.3	3.5
8. Recreation, culture and religion	8	1.3	1.5
9. Education	9	7.5	7.5
10. Social protection	10	11.7	12.8
11. Total expenditure (=item 7=23 in Table 2)	<b>TE</b>	<b>46.4</b>	<b>48.3</b>



**Table 3: General government debt developments**

<i>% of GDP</i>	ESA Code	Year 2012	Year 2013	Year 2014	Year 2015	Year 2016
<b>1. Gross debt<sup>1</sup></b>		86.0	108.8	118.4	120.7	118.4
<b>2. Change in gross debt ratio</b>		14.9	22.9	9.6	2.3	-2.3
<b><i>Contributions to changes in gross debt</i></b>						
<b>3. Primary balance<sup>2</sup></b>		-3.2	-2.4	-4.2	-2.1	1.2
<b>4. Interest expenditure<sup>3</sup></b>	EDP D.41	3.2	3.6	3.4	3.5	3.4
<b>5. Stock-flow adjustment</b>		11.7	20.4	5.3	0.2	-1.1
<i>of which:</i>						
- Differences between cash and accruals <sup>4</sup>		0.0	0.0	0.0	0.0	0.0
- Net accumulation of financial assets <sup>5</sup>		0.6	0.6	0.6	0.6	0.6
<i>of which:</i>						
- privatisation proceeds		0.0	0.0	0.0	0.0	0.0
- Valuation effects and other <sup>6</sup>		0.0	0.0	0.0	0.0	0.0
<b>p.m.: Implicit interest rate on debt<sup>7</sup></b>		4.4	3.9	3.1	3.1	2.9
<b><i>Other relevant variables</i></b>						
<b>6. Liquid financial assets<sup>8</sup></b>		2.0	0.3	0.2	0.3	0.4
<b>7. Net financial debt (7=1-6)</b>		83.9	108.6	118.2	120.4	117.9
<sup>1</sup> As defined in Regulation 3605/93 (not an ESA concept).						
<sup>2</sup> Cf. item 10 in Table 2.						
<sup>3</sup> Cf. item 9 in Table 2.						
<sup>4</sup> The differences concerning interest expenditure, other expenditure and revenue could be distinguished when relevant.						
<sup>5</sup> Liquid assets, assets on third countries, government controlled enterprises and the difference between quoted and non-quoted assets could be distinguished when relevant.						
<sup>6</sup> Changes due to exchange rate movements, and operation in secondary market could be distinguished when relevant.						
<sup>7</sup> Proxied by interest expenditure divided by the debt level of the previous year.						
<sup>8</sup> AF1, AF2, AF3 (consolidated at market value), AF5 (if quoted in stock exchange; including mutual fund shares).						

**Table 4: Cyclical developments**

<i>% of GDP</i>	ESA Code	<b>Year 2012</b>	<b>Year 2013</b>	<b>Year 2014</b>	<b>Year 2015</b>	<b>Year 2016</b>
<b>1. Real GDP growth (%)</b>		-2.4	-8.7	-3.9	1.2	1.9
<b>2. Net lending/borrowing of general government</b>	EDP B.9	-6.3	-6.0	-7.6	-5.7	-2.2
<b>3. Interest expenditure</b>	EDP D.41	3.2	3.6	3.4	3.5	3.4
<b>4. One-off and other temporary measures<sup>1</sup></b>		-0.9	1.4	0.0	0.0	0.0
5. Potential GDP growth (%)		-0.7	-1.5	-1.2	-0.5	0.0
contributions:						
- labour						
- capital						
- total factor productivity						
6. Output gap		-2.1	-2.2	-1.7	-0.4	0.0
7. Cyclical budgetary component		-0.8	-0.9	-0.7	-0.2	0.0
8. Cyclically-adjusted balance (2 - 7)		-5.5	-5.1	-7.0	-5.5	-2.2
9. Cyclically-adjusted primary balance (8 + 3)		-2.4	-1.5	-3.5	-2.0	1.2
10. Structural balance (8 - 4)		-4.6	-6.6	-7.0	-5.5	-2.2
<sup>1</sup> A plus sign means deficit-reducing one-off measures.						

**Table 5: Divergence from previous update**

	ESA Code	Year 2012	Year 2013	Year 2014	Year 2015	Year 2016
<b>Real GDP growth (%)</b>						
<b>Previous update</b>		-0.5	0.5	1	1.5	n/a
<b>Current update</b>		-2.4	-8.7	-3.9	1.2	1.9
<b>Difference</b>		-1.9	-9.2	-4.9	-0.3	n/a
<b>General government net lending (% of GDP)</b>						
<b>Previous update</b>		-2.7	-0.7	0	0	n/a
<b>Current update</b>		-6.3	-6.0	-7.6	-5.7	-2.2
<b>Difference</b>		-3.6	-5.3	-7.6	-5.7	n/a
<b>General government gross debt (% of GDP)</b>						
<b>Previous update</b>		72.1	70.2	67.8	65.4	n/a
<b>Current update</b>		86.0	108.8	118.4	120.7	118.4
<b>Difference</b>		13.9	38.6	50.6	55.3	n/a