Republic of Cyprus
Ministry of Finance
Public Debt Management Office

Annual Report
Public Debt Management

2017

March 2018

PUBLIC DEBT MANAGEMENT ANNUAL REPORT 2017

Republic of Cyprus
Ministry of Finance
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Contents

Disclaimer iii
Mission Statement v
The timeline of Public Debt Management in Cyprus (2008-2017) vi
Organisational Structure of the Public Debt Management Office vii
List of abbreviations viii
List of Figures ix
List of Tables and Boxes xi
I. Introduction 12
II. Objectives and Evaluation 15
A. Mandate 15
B. Legal Framework for public debt management 16
C. MTDS guidelines and targets 17
D. Annual Funding Programme 2017 18
E. Evaluation of MTDS guidelines and progress to date 19
III. Sovereign Debt Markets Developments 24
A. Eurozone sovereign debt market developments 24
B. Cyprus sovereign debt market developments 29
IV. Financing of the Central Government in 2017 31
A. Introduction 31
B. Financing actions in 2017 31
C. Liability management transactions and Debt redemptions in 2017 40
D. Review of the annual financing plan 42
V. The size and Composition of Government Debt 45
A. Introduction 45
B. Statistical description 45
B.1 Size and evolution of General Government Debt 45
B.2: Composition of the General Government Debt 49
B.3: Investments of the SSF and Administered Funds 57
VI. Cost and risks 60
A. Introduction 60
B. Cost of the public debt 60
C. Risks 69
C.1: Introduction 69
C.2: Financial and non financial risks 70
C.3: Contingent liabilities 83
VII. Cash Management 86
VIII. Sovereign Credit Ratings of the Republic of Cyprus 90
IX. Public Debt Management Office Action Plan 97
References 100
Appendix 101

Mission Statement

The core mission of the Public Debt Management Office is the design and implementation of the appropriate government policy in the field of debt management, depending on the domestic and international economic conditions and prospects.

The above mission is accomplished on the basis of two different but interrelated pillars: first, through the exercise of the medium-term debt management strategy of the Government, and second, through the implementation of the approved action plan by the Council of Ministers for the further development and strengthening of the infrastructure for public debt management.

The implementation of the above actions constitutes a necessary condition for the achievement of the ultimate objective of debt management: i.e. to ensure the timely coverage of the financial needs of the Government at the lowest possible medium-term cost, within an acceptable range of financial risks.

The developments relating to the above-mentioned two pillars of debt management for the last financial year are described in this report 2017.

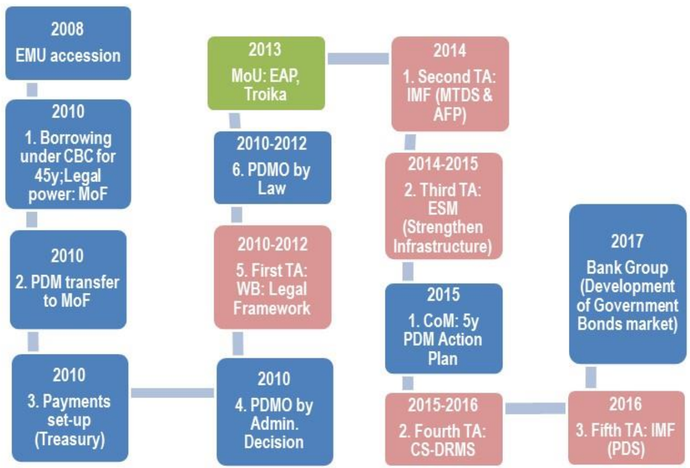
(Phaedon Kalozois), Director of Finance

Head of PDMO

Ministry of Finance

March 2018

The timeline of Public Debt Management in Cyprus (2008-2017)

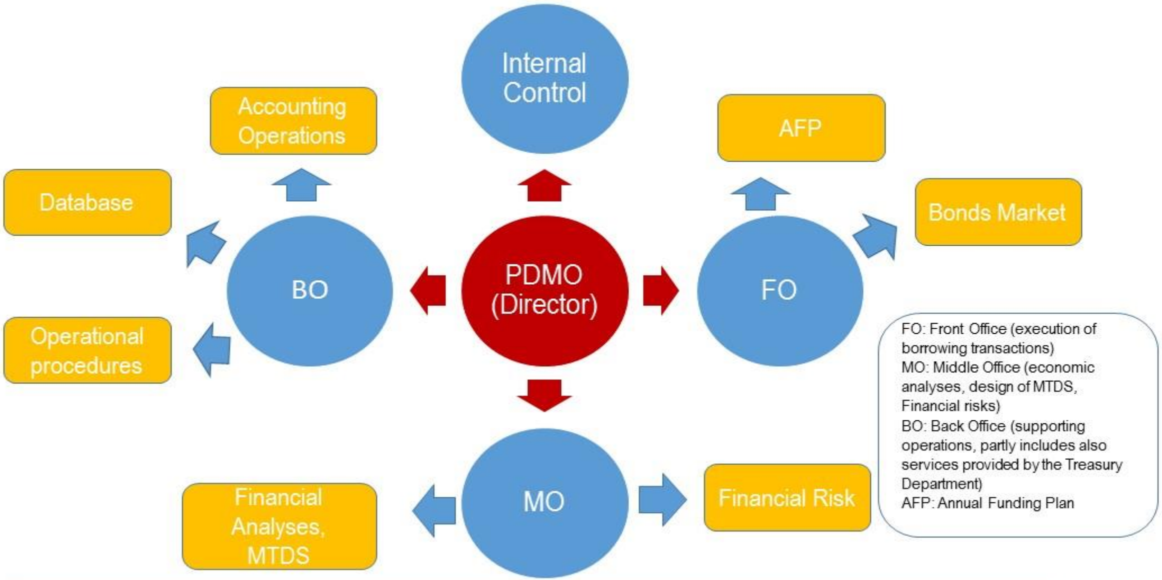


AFP: Annual Funding Plan
CBC: Central Bank of Cyprus
CoM: Council of Ministers
CS: Common Wealth Secretariat
EMU: Economic and Monetary Union
ESM: European Stability Mechanism

EAP: Economic Adjustment Programme IMF: International Monetary Fund
MoF: Ministry of Finance
MoU: Memorandum of Understanding
MTDS: Medium Term Debt Strategy

PDM: Public Debt Management
PDS: Primary Dealer System
PDMO: Public Debt Management Office
TA: Technical assistance
WB: World Bank

Organisational Structure of the Public Debt Management Office



- The Minister of Finance has the exclusive power to borrow funds on behalf of the Republic of Cyprus
- The PDMO of the Ministry of Finance is the responsible office for the above borrowing
- PDMO actions are under the supervision of the Permanent Secretary of the Ministry of Finance.

List of abbreviations

AFP	Annual Financing Programme: ‘’Annual Funding Plan’’
bn	Billion (one thousand million)
CBC	Central Bank of Cyprus
CEDB	Council of Europe Development Bank
CRAs	Credit Rating Agencies
CS	Commonwealth Secretariat
CYPGB	Cyprus Euro Medium Term Note (EMTN)
DMCs	Debt Management Committees
DRMS	Debt Recording Management System
EAP	Economic Adjustment Programme
EC	European Commission
ECB	European Central Bank
EFC	Economic and Financial Committee of the EU
EFSF	European Financial Stability Facility
EIB	European Investment Bank
EMTN	Euro Medium Term Note
ESDM	European Sovereign Debt Markets (EFC Sub-Committee)
ESM	European Stability Mechanism
EUR	Euro
GDP	Gross Domestic Product
GG	Government Guarantees
GGD	General Government Debt
IMF	International Monetary Fund
MFIs	Monetary Financial Institutions
MTDS	Medium Term Public Debt Management Strategy
mn	Million
PDML	Public Debt Management Law
PDMO	Public Debt Management Office
SDR	Special Drawing Rights
SSF	Social Security Fund
TBs	Treasury Bills
WACD	Weighted Average Cost of Debt

List of Figures

Figure 1: Secondary market yield curve levels of Cyprus and selected Eurozone States (10-year government bonds) in 2017 25
Figure 2: Secondary yield levels for Cyprus international bonds in 2017 26
Figure 3: Cyprus sovereign yield spread to selected euro area countries (bonds maturing 2025) 28
Figure 4: Treasury Bills yields and auction bid/cover ratio in 2015-2017 30
Figure 5: Monthly series of Retail bond sales in 2017 36
Figure 6: Evolution of stock of TBs by investor distribution in 2017 37
Figure 7: Change of public debt maturity profile through 2017 actions . 43
Figure 8: Impact of 2017 liability management transactions on debt maturity profile 44
Figure 9: Debt to GDP ratio evolution in 2000-2017 47
Figure 10: Trend in the consolidated general government debt in 1996-2017 49
Figure 11: General government debt redemption profile as at the end of 2017 50
Figure 12: Share of general government debt by financing instrument in 2017 51
Figure 13: Historical breakdown of GGD by financing instrument in 2010-2017 53
Figure 14: Distribution of loans by source as at the end of 2017 54
Figure 15: Distribution of retail bond sales by citizenship in 2014-2017 55
Figure 16: Distribution of interest payable on public debt during 1995-2016 62
Figure 17: Distribution of Interest payable$_{(t)}$ to Debt $_{(t-1)}$ in 2006-2016 ... 63
Figure 18: Distribution of interest payable to tax revenue in 2006-2016 64
Figure 19: Weighted average cost of debt in 2010-2017 65
Figure 20: Evolution of investor distribution for EMNTs by type during 2014-2017 66

Figure 21: Evolution of investor distribution for EMNTs by geography during 2014-2017 67
Figure 22: Distribution of retail bonds by interest rate structure 68
Figure 23: Share of debt refinancing due within 1 year and 5 years in 2012-2017 72
Figure 24: Total debt[1/] refinancing distribution as a percent of GGD at the end of 2017 73
Figure 25: Weighted average maturity of debt (in years) in 2012-2017 as at the end of 2017 74
Figure 26: Cash liquidity levels in 2010-2017 75
Figure 27: Cash liquidity levels on a monthly basis in 2017 76
Figure 28: Evolution of interest rate distribution of debt in 2010-2017 78
Figure 29: Composition of floating-rate debt as at the end of 2017 78
Figure 30: Currency composition of debt as at the end of 2017 80
Figure 31: Outstanding GGs in percent as at the end of 2017 85
Figure 32: Institutional structure of the government cash management 87
Figure 33: Distribution of cash balances and amount of debt that falls due within one year in 2010-2017 89
Figure 34: Historical evolution of credit ratings of the Republic of Cyprus in 2011-2017 93
Figure 35: Government Bond rating in long-term local currency of the Republic of Cyprus and selected Eurozone States as at the end of 2017 96

List of Tables and Boxes

List of Tables

Table 1: Annual borrowing by financial instrument in 2017 32
Table 2: Distribution of total annual borrowing by maturity in 2017 33
Table 3: Summary of the use of the annual funding in cash terms in 2017 34
Table 4: Long term debt redemptions and liability management transactions in nominal terms in 2017. 41
Table 5: Change in the public debt structure in 2017 42
Table 6: Solicited sovereign credit ratings as at December 31, 2017.....92

List of Boxes

Box 1: Republic of Cyprus EUR 850 mn, 2.75% 7-year benchmark bond due 27 June 2024.................................... **Error! Bookmark not defined.**

I. Introduction

Following the exit of Cyprus from the three-year European Commission (EC) – European Central Bank (ECB) – International Monetary Fund (IMF) Economic Adjustment Program in March 2016 underpinned by a sizeable correction of public finances and on-going reforms of the banking sector, the year 2017 was another year towards the desired direction.

Public finances have improved further exhibiting positive budget balances and primary surpluses. The continuation of these outcomes constitutes a prerequisite to safeguard the debt sustainability of the Republic of Cyprus in the future. Another important element in 2017 was the increased confidence of international investors for Cyprus which was highlighted in the benchmark EMTN (Euro Medium Term Note) issuance in June 2017.

The secondary market yields of the Cypriot EMTN have evolved smoothly and demonstrated overall resilience during 2017 despite the international political uncertainty related to major international events whilst the Cyprus sovereign spreads of the 2025 bond over selected bonds of euro area countries showed a clear downward trend.

The main financing source of the Republic in 2017 was the international market supplemented by domestic market sources of both the institutional and retail segments. The international market is expected to be strategically the main source of funding in the years to come due to the possibilities offered by the available large, diversified pool of investors.

The public debt as a ratio of Gross Domestic Product (GDP) exhibited a material reduction due to prudent fiscal management delivering strong results. The central government's liquid assets were maintained at a sufficient level in the reference period (2017) to allow full coverage of the next 12-month period financing needs. Towards the end of the year and taking into account the easier market access of the Republic, the liquid assets were reduced but only for a short period since from January 2018 the said assets were increased around the same level as before.

All debt portfolio risk indicators are in line with the Medium Term Debt Management Strategy (MTDS) guidelines and on track for the targets set for the year 2020. Actions in liability management on future maturities have contributed to this improvement. The average cost of servicing the public debt, reached an all-time low benefiting from official borrowing, liability management transactions and the low interest rate environment in the European capital markets. Significant progress was marked in the development of the government securities market with the appointment of a market group of seven international investment banks.

The active cash management framework has continued to be implemented in 2017 in order to ensure a satisfactory return on the high liquid funds levels, maintaining refinancing risk to a minimum level.

The sovereign's creditworthiness was upgraded and set to a positive outlook by all Credit Rating Agencies (CRAs). By year-end the outlook of the credit rating remained positive by the four main credit rating agencies (Standard & Poor's, Moody's, Fitch, DBRS), with the long-term rating ranging between 1 to 3 notches sub-investment grade.

Over the reference period, the Public Debt Management Office (PDMO) continued its infrastructure development as part of its five-year Action Plan 2015 (Dec.) – 2020 (Dec.). The implementation process of the CS-DRMS was completed and the operation of the system was initiated.

The PDMO participated inter alia in the Subcommittee of the EU Economic and Financial Committee on European Sovereign Debt Markets (ESDM), the IMF Spring meetings and the European Stability Mechanism (ESM) activities, specifically related to public debt management matters.

Following this introduction, the strategic objectives on public debt management, the Annual Funding Plan (AFP) and the progress to date are presented in Chapter 2. The main developments in the debt capital markets for bills and bonds are presented in Chapter 3.

Chapter 4 outlines the financing actions of the central government in 2017 as well as the debt redemptions (flow analysis), while Chapter 5 presents the main structural characteristics of public debt and their evolvement over time (stock analysis). The cost-risk profile is analysed in Chapter 6.

The operations on liquidity management are presented in Chapter 7 whereas sovereign rating developments are outlined in Chapter 8. The report concludes with Chapter 9 on the developments of the PDMO Action Plan for infrastructure and systems development in 2017.

II. Objectives and Evaluation

A. Mandate

On behalf of the Republic of Cyprus, the Minister of Finance borrows funds by raising loans or issuing securities both in the domestic and foreign markets in local or foreign currency. Pursuant to article 4 of the Public Debt Management Law (PDML), the PDMO is responsible among other functions for executing all borrowing transactions, the management of liquidity of the government and handling all other debt management operations, including the drafting of the MTDS and the AFP.

Government borrowings aim mainly at: (i) covering the fiscal deficit; (ii) maintaining the desired level of cash reserves; (iii) refinancing the outstanding public debt; and (iv) covering other government policy needs.

The ultimate objective of debt management strategy is to ensure that financing needs are always met in time and that the cost of borrowing is the lowest possible in the medium term[1], within the framework of an acceptable[2] level of risk[3].

---

[1]Any decision-making based on the minimization of the borrowing cost of the transaction (in raising a loan or a bond offering) i.e. using as a sole criterion the interest rate, constitutes a sub-optimal action that might undermine the ultimate objective of PDM. This is why the minimisation of the borrowing cost is related to the medium term horizon.

[2]Borrowing has to be within reasonably acceptable and manageable levels of financial risks.

[3]In this context, the main financial risks are: (a) refinancing risk; (b) Interest rate risk; (c) Foreign exchange risk

B. Legal Framework for public debt management

Pursuant to article 2 of the PDML, the debt management operations are concentrated on the preparation of the MTDS and of the AFP as well as on the execution of the necessary borrowing transactions in order to facilitate the implementation of the AFP and to meet the objectives of the MTDS.

The MTDS is a 3-5 year strategy and is submitted for final approval to the Council of Ministers by the Minister of Finance, after informing the Budget and Finance Committee of the Parliament. According to the Law, the AFP is designed by the PDMO, and approved by the Minister of Finance. The execution of the necessary borrowing and other debt management transactions form the implementation of the financing plans in order to ultimately meet the guidelines of the Strategy. The current active Strategy covers the period 2016-2020. It was published in early 2016.

The PDMO functions as an integral part of the Ministry of Finance, under the general supervision of the Permanent Secretary.

C. MTDS guidelines and targets

The guidelines of the MTDS and the actions/quantitative targets under each guideline related to the reference year 2017 are presented below. It is noted that after an approval of the Council of Ministers in September 2017, the main pillars and targets of the MTDS 2016-2020 remain the same.

1. **Smoothening of debt maturity profile and extension of the maturity of marketable debt**

   - *Maintain average maturity of marketable debt, not less than 5 years;*
   - *Maintain short term debt equal or less than 4 percent of total debt stock; and*
   - *Maintain long term debt equal or more than 96 percent of total debt stock and respecting the maturity limits:*
     - ➢ *Long term debt maturities 2016-2018: up to EUR 1,2 bn per annum;*
     - ➢ *Long term debt maturities of 2019 and thereafter: up to EUR 2,2 bn per annum.*

2. **Risk mitigation**

   - *Maintain total liquid funds to cover the financing needs of at least the 9 months;*
   - *Maintain marketable debt foreign exchange exposure not more than 5 percent of the total debt stock;*
   - *Maintain total debt foreign exchange exposure not more than 10 percent of total debt stock;*
   - *Maintain marketable debt floating interest rate exposure not more than 5 percent of total debt stock; and*
   - *Maintain total debt floating interest rate exposure not more than 55 percent of total debt stock.*

3. Development of the government securities market

- *Improvement in the price discovery mechanism of the domestic market and increase accessibility to international investors;*
- *Introduce a suitable structure to enable a price discovery mechanism and liquidity provision in the foreign market; and*
- *Buildup of a long-term sovereign yield curve.*

4. Minimisation of marketable debt borrowing cost

- *Improvement of the investor relations and market intelligence;*
- *Expansion of the investor base in terms of geography, type and size.*

D. Annual Funding Programme 2017

Pursuant to article 10 of the PDML, the PDMO prepares an AFP, which covers the projected accumulated borrowing needs of the Republic of Cyprus in one calendar year. The AFP is based on the MTDS and the annual cash flow forecast of the Republic. The AFP is approved by the Minister of Finance and is updated at least twice a year.

The objectives of the AFP 2017 were the following:

1. Maintain Cyprus' presence in the international capital markets and buildup of a long-term sovereign yield curve;
2. Mitigate the refinancing risks by setting reserve on liquid funds to cover the financing needs of the next 12 months;
3. Redeem a share of the debt due in 2019 in order to smoothen-out the debt maturity profile; and

4. Renewal of short-term debt and maintain the swift functioning of the Treasury Bills market;

By the end of 2017 and taking into consideration the projected annual cash flows and the successful market access of Cyprus, the PDMO submitted an updated AFP to the Minister of Finance for the next year.

E. Evaluation of MTDS guidelines and progress to date

Although it is premature to evaluate to what extent the overall MTDS objectives are being fulfilled especially given that some of them are not quantitative, the two years passed since the commencement of the implementation of the said strategy, provide a good picture where we stand today.

Given the outcomes presented in this Annual Report 2017, the overall MTDS guidelines have been fulfilled at a very satisfactory level following the projected trajectory. The assessment of the process of each guideline is presented below.

Smoothening of debt maturity profile and extension of the maturity of marketable debt

A substantial improvement has been marked on the debt maturity profile during the year 2017. The share of outstanding short term debt stood at 1 percent of the total outstanding debt at the end of 2017, in line with the target set in the strategy. It is noted that Treasury bills (TBs) issuances are necessary to maintain pricing points, enrich funding instruments and reach out to investors interested in this particular segment.

The share of outstanding long term debt at end 2017 stood at 99 percent, in line with the strategy. The outstanding annual maturities profile comply with the corresponding minimum limits set in the strategy for the length of debt maturity. After the proactive liability management transactions on years with peak maturities have been executed and new issuance of bonds with maturities falling beyond these years have been completed, the new maturities profile is much more comfortable. Up to 2021, our intention is to issue one benchmark EMTN per year and thereafter one or two benchmark EMTN issuances in order to cover the financing needs of the Government.

With regards to the average remaining maturity of marketable debt, it was maintained to 4,9 years at the end of 2017 as was at the end of 2016. The value of the said indicator is very close to the relevant MTDS target i.e. to be not less than 5 years. The continuation of longer term benchmark EMTN issuances is anticipated to increase the maturity of marketable debt above 5 years.

Risk mitigation

The size of the liquid funds throughout the year of 2017 was in line with the relevant target set in the strategy, to cover the financing needs of the next 12-month period. For a short time, the size of the liquid funds was not in line with the relevant target due to the use of funds for additional liability management transactions.

Moreover, the target for the total and marketable foreign exchange exposure has been achieved to date. The approach, generally followed, is to go for euro denominated issuances only. The partial early repayment of the IMF loan made in 2017, which is denominated in Special Drawing Rights (SDR), reduced further the only non-euro debt outstanding, at around 4 percent of the total debt. A substantial amount of instalments payable to the IMF loans was done in 2017 of the order of EUR 271 mn.

The debt metrics comply with the target set for floating-fixed interest rate composition. Securities are generally issued in fixed interest rate form only. There is no outstanding marketable debt in floating or index type of interest. There is a sizeable share of outstanding debt in floating interest rates, mainly due to disbursements of ESM and IMF loans and to a lesser extent to a number of loans granted by European Investment Bank (EIB) and Council of Europe Development Bank (CEDB). The total of the said debt with floating interest rates formed 46 percent of the outstanding public debt at the end of 2017. The variable rate debt is anticipated to decline with its gradual redemption of the instalments payable to loans.

Developments of the government securities market

With regards to the efforts for improving the price discovery mechanism of the domestic market and increase accessibility to international investors, some progress has been marked. The main objective is how clearing and settlement of domestic bonds listed at the Cyprus Stock Exchange can be undertaken indirectly through the international depositories which are easily accessible by international investors. This project is still underway.

A significant improvement has been marked in the development of a suitable market structure to improve the price discovery mechanism and liquidity provision in the foreign market. A market group with seven international investment banks was formed and has started to work towards this goal. The initial mandate of banks is to post indicative prices of the Cypriot international bonds on a voluntary basis in a platform jointly decided by the issuer and the banks. The international banks have already submitted their suggestions with regards to the selection of the platform and it is anticipated that the selected platform will operate by the end of 2018 or early 2019.

The target of buildup of a sovereign yield curve, is ongoing. A new point was added in the sovereign yield curve in 2017. According to the existing debt maturity profile, the PDMO aims at centralizing the funding efforts around one international bond issuance per year up to 2021 and one or two international bond issuances per year thereafter to serve as benchmark bonds.

Minimisation of marketable debt borrowing cost

The outcome for the said guideline is envisaged to materialize gradually through the successful implementation of the other guidelines and the realisation of their targets. The contact list of investors has been expanded considerably throughout the years. As the secondary yields of the Cypriot international bonds continue to follow a downward trend and the sovereign credit ratings tend to move to investment grade, the composition of investors will change over time. The efforts now need to be placed in the analysis of investors in order to approach investors with longer investment horizon and link marketing efforts to this type of investors.

The target of the provision of information to investors has been achieved by the PDMO through the production and dissemination directly to investors of two regular publications, namely Cyprus economy newsletter (bi-monthly) and Public debt quarterly bulletin. Furthermore, an investor presentation is updated at intervals and published at the PDMO website informing the investors about the main developments of the Cypriot economy.

With regards to market intelligence, the PDMO continues to monitor and analyse the financial markets observing the new issue premiums and new issue performance of peers compared to the Republic. It is expected that more information on flows, volumes and investor statistics will be gathered by the newly established Bank group.

For the expansion of the investor base in terms of geography, type and size, the PDMO has focused on marketing activities which are conducted well ahead of any intended bond placements. A number of non-deal related roadshows were executed well ahead the benchmark EMTN issuance in June 2017 both in core and non-core EU market as well as in the US market. The investor base has improved both in terms of geography and type in the 2017 EMTN issuance.

The results of this target are evident through the investors distribution statistics by geography and type in the benchmark bond issuances which are shown in Chapter 6.

III. Sovereign Debt Markets Developments

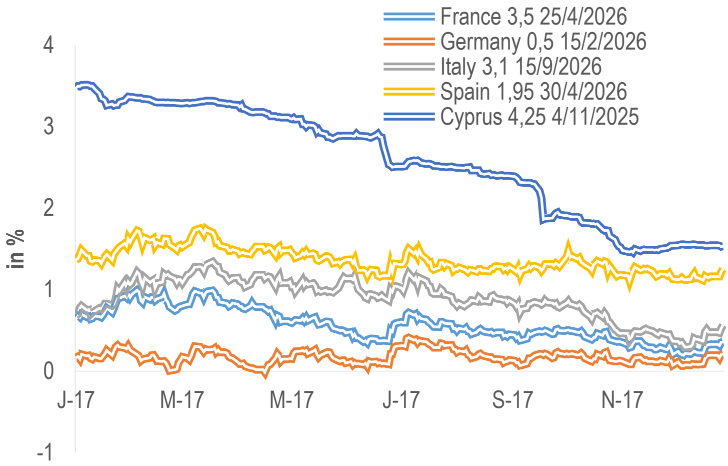
A. Eurozone sovereign debt market developments

According to the notes issued by Directorate General Financial Stability, Financial Services and Capital markets Union, during the first two months of the year 2017, developments in bond markets sovereign bond yields have marked an increase in most euro area Member States. The developments in bond markets were marked by rising inflation expectations and political uncertainty connected to upcoming elections in several EU member States such as France and Germany.

Over the same period, the yield spreads of the long-term government bonds over German Bunds for the more core euro area member States showed a clear upward trend. From the mid-June to end October 2017, the main benchmark sovereign bond yield curves flattened and the yield spreads of long-term government bonds over German Bunds for the said member States remained relatively stable.

The yield developments of 10-year bonds, where available, for selected Eurozone States throughout the year 2017 are illustrated in Figure 1. The 10-year Cyprus government bond yield after a minor increase in the first 12 days of January, followed a downward trend throughout the year and decreased by 194 basis points compared to the beginning of the year. As a result, the gap between Cyprus government bond and other selected bonds presented in the figure below, narrowed.

Figure 1: Secondary market yield curve levels of Cyprus and selected Eurozone States (10-year government bonds) in 2017



(Source: Bloomberg)

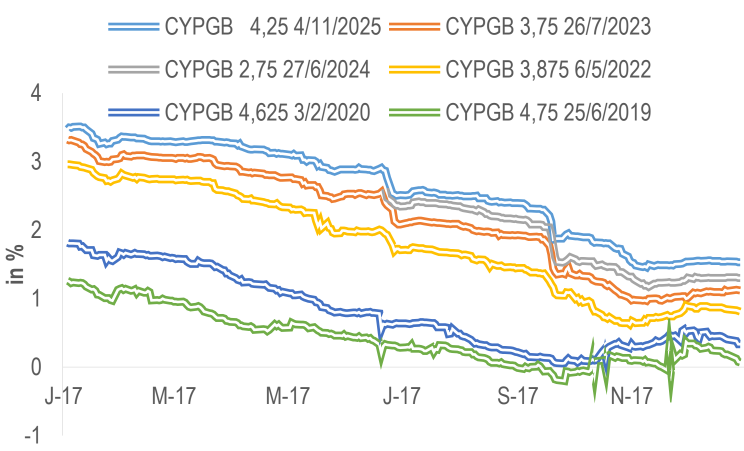
Regarding the implementation of the AFP, a new 7-year benchmark bond (EMTN) was issued in June 2017, adding a further point in the sovereign yield curve of Cyprus. All Cyprus government bonds demonstrated overall resilience with some short periods of yield steepening. The Cyprus government bond yields have responded in a rather silenced way despite the political uncertainty related to major events internationally, namely elections in several EU member States and the question of how Europe and the UK will handle Brexit.

The market behaviour indicated a disaggregation of the six benchmark (EMTN) bonds of the Republic of Cyprus into two main groups. The four longer-dated bonds due in 2025, 2023, 2022 as well as the newly issued benchmark bond due in 2024 moved in a similar pattern, tightened stronger and over-performed vis-à-vis the other two bonds with shorter-dated maturities. Specifically, the longer-term bonds performed very well in the secondary market with the year closing around 200 basis points tighter than their launch with the exception of the newly issued bond, where yield narrowed by 130 basis points by the end of the year than its launch.

The second group of bonds due in 2019 and 2020 performed also well in the secondary market with the year closing 119 and 148 basis points tighter than their launch respectively.

Figure 2 below, illustrates the yield development of Cyprus' international benchmark bonds in 2017, launched under the EMTN Programme and listed on the London Stock Exchange.

Figure 2: Secondary yield levels for Cyprus international bonds in 2017

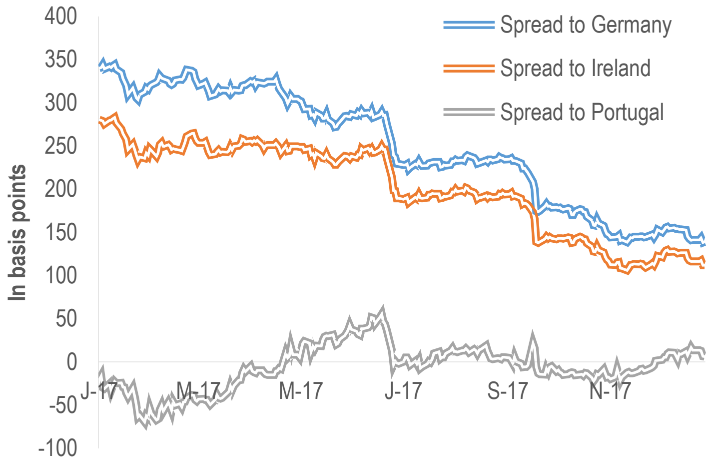


(Source: Bloomberg)

With regards to yield spreads developments, the Cyprus sovereign spreads of the 2025 bond over selected bonds of euro area countries showed a clear downward trend, as presented in Figure 3 below.

The Cyprus sovereign yield spread of the 2025 bond (4,25%) over German Bund (1,0%) maturing in August 15 2025 decreased throughout the year 2017 and towards the end of year had reduced by 201 basis points compared to the beginning of the year reaching 139 basis points. The spread to the Irish bond (5,40%) maturing in March 13 2025 moved in a similar pattern closed to the spread over German Bund and towards the end of year was reduced by 169 basis points compared to the beginning of the year reaching 112 basis points. Regarding the yield spread over Portuguese bond (2.875%) maturing in October 15 2025 was more volatile throughout the year since opened the year in negative territory at minus 21 basis points, retained in a negative territory for around 4 months (January-April) and towards the end of year had closed at 6 basis points.

Figure 3: Cyprus sovereign yield spread to selected euro area countries (bonds maturing 2025)



Source: Bloomberg

The secondary market activity and the clearly downward trend of Cyprus sovereign yield spreads have contributed to the funding cost reduction of issuing new debt in the primary market. An overview of the financing of the central government in 2017 is presented in the next chapter.

B. Cyprus sovereign debt market developments

The activity of the domestic government bond market has continued throughout the year 2017 with regular monthly 13 week TBs auctions. TBs issuances are euro-denominated and the PDMO does have regular announced auctions of TBs.

Although the annual outstanding amount of TBs is on a downward pattern since 2013, the TBs programme remains the short-term funding vehicle for Cyprus. In 2017, the total cumulative amount of TBs auctions was EUR 1200 mn whilst the total stock of TBs at the end of the year was EUR 200 mn or 1 percent of the total public debt compared to EUR 300 mn at the beginning of the year.

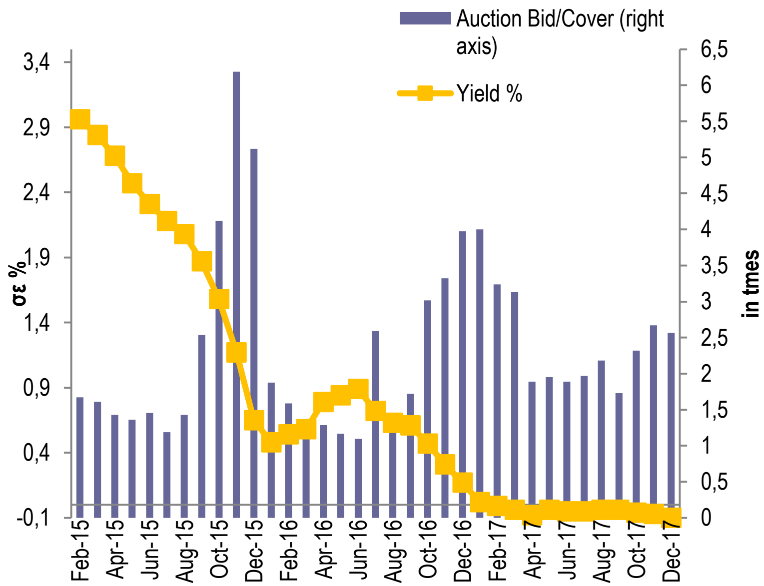
Figure 4 below, illustrates the historical evolution of TBs yields and auction bid to cover ratios[4] during the years 2015-2017. With regards to yields developments, the Cyprus TBs yields showed a clear declining pattern with the weighted average yield reaching -0,05 percent in 2017 compared to 0,59 percent in 2016. It is noted that, TBs yields is on a negative territory since February 2017 reaching -0,10 percent in the last auction in December 2017.

Regarding the bid to cover ratios, it seems that the auction participation after a decline around the time of exit from the EAP (Economic Adjustment Programme) in March 2016, investor interest has returned by mid-year 2016 and strengthened thereafter. The annual average auction bid to cover ratio in 2016 was 1,9 times the auction amount whilst in 2017 the said ratio has improved significantly reaching 2,5 times the auction amount. The improved outcome of the TBs auctions in 2017 can be regarded as a positive signal for the creditworthiness

[4] The total value of bids received to the issuance amount announced.

of the government whilst the continuation of high bid to cover ratios along with the Eurosystem's low interest rates is expected to help maintain low yields.

Figure 4: Treasury Bills yields and auction bid/cover ratio in 2015-2017



(Source: PDMO)

IV. Financing of the Central Government in 2017

A. Introduction

The financing of the Central Government during 2017 was done through a number of financing instruments and mainly through the issuance of EMTN indicating the continuation of the successful presence of the Republic of Cyprus in the international market.

Following the introduction of this Report, the second sub-chapter illustrates the financing of the borrowing needs in 2017 by source and by maturity. The next sub-chapter focuses on the debt redemptions and liability management transactions executed in 2017. The chapter concludes with a review of the year’s financing profile.

B. Financing actions in 2017

The central government annual borrowing by financing instrument in 2017 is illustrated in Table 1 below. The total borrowed amount of the Republic in 2017 reached EUR 1,6 bn, excluding rollovers (TBs) during the year. The financing of the Republic was mainly done through the issuance of government securities in the domestic and foreign market.

The main component of the annual financing, around half of the annual funds, was the issuance of the foreign bond underpinned by strong participation of domestic investors. In general, about 51 percent of the annual funds originated by domestic investors with both legal entities, mainly Monetary Financial Institutions (MFIs) investing in foreign bond, domestic bonds and TBs issuances as well as natural persons investing in retail bonds. An amount of EUR 121 mn or about 7 percent of the total annual financing was formed by foreign loans granted by

European Investment Bank (EIB) and the Council of Europe Development Bank (CEDB) throughout the year for ongoing infrastructure projects.

Table 1: Annual borrowing by financial instrument in 2017

			EUR mn	%	%
1	**Government Securities**		**1529**		**93**
	of which:				
	TBs	300		18	
	Domestic bonds	302		18	
	Retail bonds	77		5	
	Foreign bond (EMTN)	850		52	
2	Loans by EIB-CEDB		**121**	7	**7**
	Total annual borrowing[1/]		**1650**	**100**	**100**

1/= Debt issued and redeemed within the year 2017 is not included.

(Source: PDMO)

Table 2 below, shows the distribution of total annual borrowing by maturity in 2017. The maturity of the annual borrowing in 2017 ranged between 0,25 years to 21 years with the majority of the debt ranged in the medium to long-term spectrum of 6 to 10 years. The said debt was mainly composed of the EMTN issuance whilst the remaining amount was originated from domestic and retail bonds issuances throughout the year. About 7 percent of the annual borrowing ranged in the long-term spectrum of over 10 years and comprised loans provided by EIB and CEDB for ongoing infrastructure projects.

The weighted average maturity of new issued debt during 2017 was increased by 1 year compared to the respective debt during 2016, reaching 6,6 years, supporting the quantitative target of the MTDS to extend the maturity of marketable debt.

Table 2: Distribution of total annual borrowing by maturity in 2017

		EUR mn	%
1	0,25 years	300	18
2	6 -10 years	1229	75
3	Over 10 years	121	7
	Total net annual borrowing	**1650**	**100**

(Source: PDMO)

As presented in Table 3 below, in terms of the utilization of borrowed funds, about half of the annual funding was used to implement liability management transactions either for bond buybacks due in 2019 and 2020 or for partial early repayment of IMF loan instalments due within the period 2017-2026. A substantial amount of funding was used to pay the scheduled debt redemptions in 2017 whilst the loans provided by EIB/CEDB were used for the implementation of infrastructure projects.

Table 3: Summary of the use of the annual funding in cash terms in 2017

		EUR mn	EUR mn	%
1	Debt maturities		689	42
2	Debt buybacks[1/]		569	35
	of which price premium	54		
3	Partial early repayment of IMF loan		271	16
4	Infrastructure projects		121	7
	Total net annual borrowing		**1650**	**100**

(Source: PDMO)

1/= Excluding accrued interest and the Central Bank of Cyprus transaction executed within the framework of Public Sector Purchase Program of the EIB

The overview of financing actions implemented during 2017 are presented in more details below.

In January 2017 one domestic bond was auctioned in the local market to meet demand by domestic investors and to maintain market activity. The 7-year bond of the order of EUR 300 mn was priced at a yield of 3,25% and the investor was a domestic MFI.

The main financing of 2017 took place in June 2017 through the issuance of a 7-year benchmark EMNT of the order of EUR 850 mn at a coupon rate of 2,75 percent and yield of 2,80 percent. The coupon rate of the said bond was 1 percentage point lower than the corresponding coupon rate of the 7-year benchmark EMTN issued in

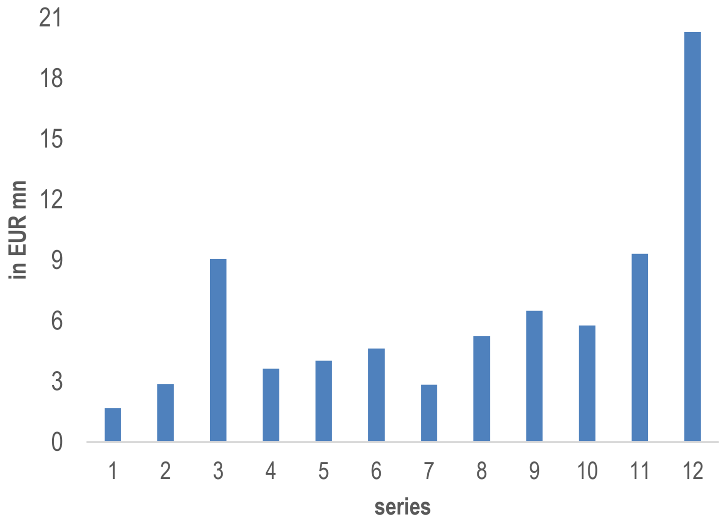
July 2016 highlighting the strong support from the international investor community for the Republic of Cyprus due to the continuation of recovery of Cyprus' economy, the strong growth rates and the number of upgrades by CRAs throughout the year.

The benchmark bond added a further point in the sovereign bond yield curve of Cyprus after the 4 EMTN issuances during the period 2014-2016 underpinned by the largest order book for Cyprus benchmark and diversified pool of investors both from Europe and the US market (see further Box 1).

In addition, monthly series of the domestic retail bonds amounted to EUR 76 mn were issued throughout the year. The domestic retail bonds are designed to meet the characteristics of natural persons as investors, have a 6 years' maturity and can be redeemed by the holder earlier at a minimum notice of one month without a penalty. The interest rate follows a step-up structure and has a positive correlation with the time of holding.

Figure 5 below, illustrates the monthly series of retail bond sales in 2017. The increased demand for retail bonds series in November and December 2017 was partly attributed to the expected amendment of the interest rates for 2018 series of retail bond sales, which was announced by Government in October 2017.

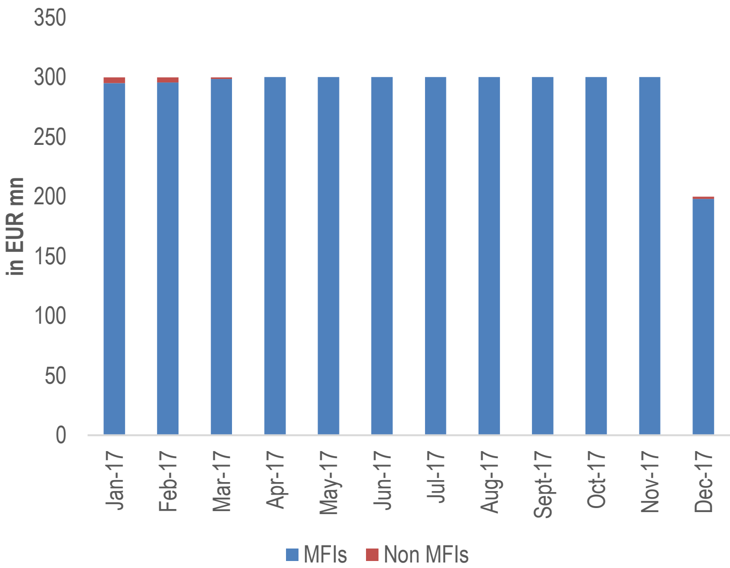
Figure 5: Monthly series of Retail bond sales in 2017



(Source: PDMO)

The annual funding in 2017 has been completed through monthly TBs auctions of the order of EUR 100 mn. As presented in Figure 6 below, MFIs dominated the Treasury Bill investor base. Regarding the participation of Non-MFIs in monthly TBs auctions such as pension funds and state-owned enterprises, this is on a downward path since January 2016 as the TBs offered low (negative) returns compared to alternative investments particularly bank deposits.

Figure 6: Evolution of stock of TBs by investor distribution in 2017



(Source: PDMO)

Box 1: Republic of Cyprus EUR 850 mn, 2.75% 7-year benchmark bond due 27 June 2024

Given the strategic objectives under the MTDS to build out an international bond yield curve and smooth out the debt maturity profile and taking into account the stable market backdrop and the upgrades by both DBRS and S&P's, the Republic launched a new 7-year benchmark transaction.

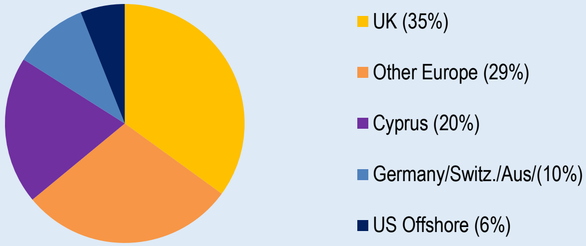
The intention in 2017 was for the proceeds to be used for liability management transactions. The transaction was done in conjunction with a switch offer of the 4,75% June 2019, 4,625% February 2020 and 6,50% May 2020 bonds.

The mandate for lead management was extended to Citi, Goldman Sachs International and HSBC with an announcement made on 19th June. On 19th June Initial Pricing Thoughts were released for a 7-year benchmark bond at 3% yield area due in 2024. The 7-year tenor was chosen given the availability in the debt maturity profile and in line with the strategic target of increasing the average maturity of marketable debt as well as the positive feedback received from investors.

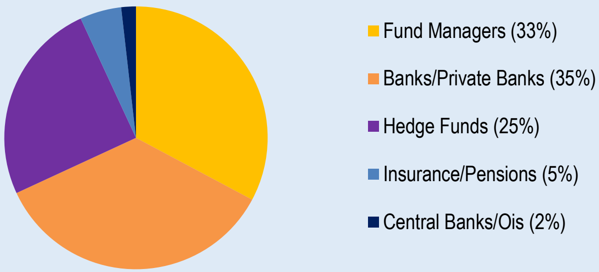
The order book was officially opened on 20th June with a revised price guidance of 2,9% while the demand continued to grow allowing the issuer to further tighten the yield by 10 basis points and set at 2,8%. By the closing of the order book on 20th June midday, the combined final demand reached EUR 4,2 bn representing the largest order book generated for the Republic of Cyprus benchmark transaction since June 2014.

Geographically, the placement achieved a broad distribution attracting in particular a significantly higher number of investors from Europe than previous issuances. The UK market continued to be the largest single origin market of investors with 35% share in the final participation. The remaining increased participation of investors came from various European countries, excluding Cyprus, with total European accounts reaching 39% of the final distribution of which about a third from German, Austrian and Swiss investors. There was also an increased participation from Cypriot investors with 20% share of the issuance. With regards to the investor type the largest pool of investors were Banks/Private banks (35%) followed by Fund Managers at 33% of the final distribution. Hedge funds participation was at 25%, higher than previous issuance at 7% due to switch offer, whilst a second participation was recorded by the insurance and pension fund segment at 5%.

Distribution by region



Distribution by type



Summary of terms and conditions

Issuer	The Republic of Cyprus
Format	Reg S Registered only, Cat 1
Pricing	20 June 2017
Settlement	27 June 2017
Maturity	27 June 2024
Size	EUR 850,000,000
Coupon	2,750%
Re-offer Yield	2,800%
Spread vs MS	+242,2 bps
Denominations	EUR 1K+1K
Listing/Law	London Stock Exchange/English Law
ISIN	XS1637276848
Lead Managers	Citi, Goldman Sachs International, HSBC

C. Liability management (LM) transactions and Debt redemptions in 2017

The first strategic objective of the MTDS for the years 2016-2020 is the smoothening of the public debt maturity profile and the extension of the maturity of marketable debt. In 2017, the main attention with regards to debt maturity profile was in years 2019 and 2020 where peaks were evident. In addition, specific attention was given to early repayments of loans in an attempt to reduce the total interest payment in the future and the weighted average cost of debt.

Government LM operations to smoothen out the debt maturity profile in 2017 involved buyback transactions of EMTNs and two partial early repayments of loans amounted to EUR 1432 mn. The total debt buybacks in nominal terms amounted to EUR 546 mn and were executed on three EMTNs due in June 2019 (4,75%), in February 2020 (4,625%) and in May 2020 (6,50%). The weighted average coupon of repurchased bonds was 4,97% which was higher than the coupon rate (2.75%) of new benchmark EMTN issued in June 2017 in conjunction with a switch offer of the above bonds. As the bonds were trading above par, the repurchase amount in cash terms, excluding accrued interest rate, was EUR 569 mn or EUR 54 mn above their nominal value. Including the CBC transaction, the total repurchase amount in cash terms, excluding interest rate payments, was EUR 602 mn.

The first partial early repayment of loan was made in July 2017 and concerned the fund credit provided by the IMF. The total amount of early repayment was EUR 271 mn, carrying interest rate of 3,60%. The second partial early repayment of loan was made in July 2017 and was related to the credit provided by the CBC before the year 2002. The total amount of early repayment to the CBC was EUR 615 mn, carrying interest rate of 3,00%.

The details of buyback operations as well as the debt redemptions in the domestic/foreign market and loan amortisations by creditor in 2017 are shown in the Appendix.

Table 4 below shows all long term debt redemptions and liability management transactions in 2017. The scheduled long term redemptions of the year, excluding buyback transactions and early repayments, amounted to EUR 439 mn and related to domestic bonds, instalments for domestic and foreign loans as well as to retail securities.

With regards to short term debt, an amount of EUR 300 mn was rolled over throughout the year and towards the end of 2017, the amount of TBs was reduced to EUR 200 mn.

Table 4: Long term debt redemptions and liability management transactions in nominal terms in 2017

		EUR mn	%
1	Domestic Bonds	283	15,1
2	EMTNs	546	29,2
	of which: buybacks (EUR 546 mn)		
3	Loans	1024	54,7
	of which: early repayments (EUR 886 mn)		
4	Retail securities	18	1,0
	Total	**1871**	**100**

(Source: PDMO)

D. Review of the annual financing plan

This section illustrates how the annual financing plan changed the debt structure of the year 2017. The debt structure has changed significantly in 2017 compared to the previous years. This change was mainly attributed to the early repayments of loans and buyback transactions of EMTNs, underpinned by the objectives set in the MTDS. The reduction of the public debt by EUR 610 mn at the end of 2017 was mainly attributed to the reduction of loans by EUR 904 mn and the buyback transaction of EUR 546 mn executed in June 2017 reducing the recording amount of EMTN issuance in terms of debt change. However, a noticeable decrease in the stock of domestic bonds was recorded reflecting the increased importance of foreign markets as a financing source.

With regards to retail securities, a noticeable decrease was recorded in 2017 compared to the year 2016 whilst for the TBs, as mentioned earlier, the amount was reduced by EUR 100 mn by the end of the year.

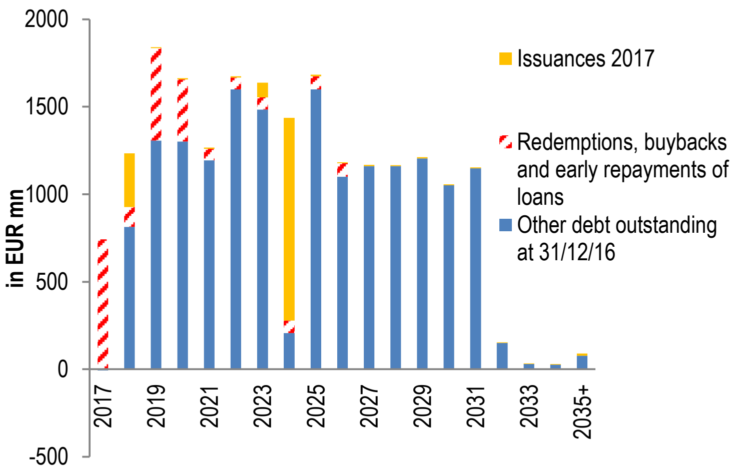
Table 5: Change in the public debt structure in 2017

		in EUR mn
1	Domestic Bonds	19
2	EMTN	304
3	Treasury Bills	(100)
4	Loans	(904)
5	Retail securities	71
	Total	**-610**

(Source: PDMO)

Figure 7 below, shows how public debt maturity profile changed due to funding and liability management transactions in 2017. A total amount of new issuances of the order of EUR 1650 mn was added to the public debt maturity profile. An amount of EUR 1150 mn or about 70% of the new debt issuances falls in the year 2024. The second largest amount of new issuances of the order of EUR 300 mn due in 2018 (which was rolled over throughout the year) concerns TBs whilst the remaining amount spreads between 2018-2037.

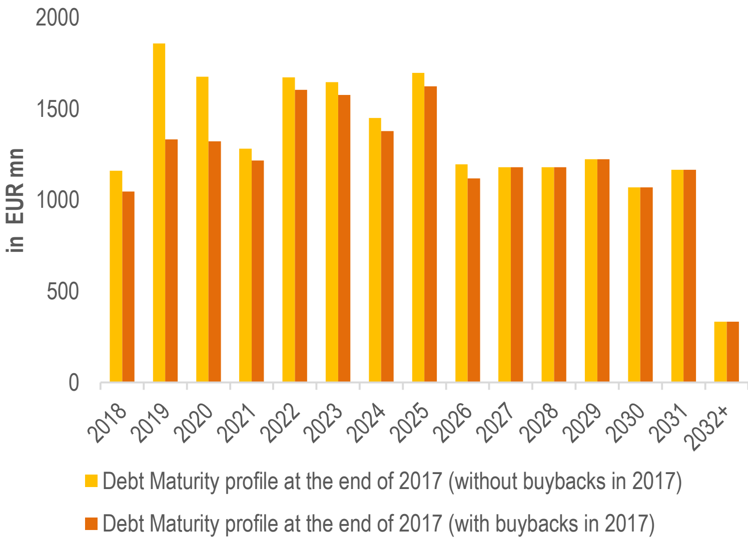
Figure 7: Change of public debt maturity profile through 2017 actions



(Source: PDMO)

The liability management transactions implemented by the PDMO in 2017 on debt maturity profile has resulted in further smoothening out of public debt maturities and reduced further the peaks of maturities in 2019 and 2020. As a result, the maturity profile at the end of 2017 was within comfortable manageable levels and within the targets set in the MTDS. The impact of liability management transactions on debt maturity profile is presented in Figure 8 below. A comparative analysis of the impact of liability management transactions in 2017 on debt maturity profile at the end of 2017 is presented in Appendix.

Figure 8: Impact of 2017 liability management transactions on debt maturity profile



(Source: PDMO)

V. The size and Composition of Government Debt

A. Introduction

Statistical methodology and valuation for public debt is based on concepts defined in the European System of Accounts 2010. According to the consolidated version of the Treaty on the Functioning of the European Union (2012), the government debt is defined as “the total gross debt at nominal value outstanding at the end of the year and consolidated between and within the sectors of general government”. In the case of Cyprus, the relevant subsectors are the central government, the local authorities and the Social Security Fund (SSF).

Following the introduction of this Report, the second sub-chapter which is organized in three sections, provides the statistical description of government debt. The first and second sections deal with the size, historical evolution and structure of the consolidated general government debt, whereas section 3 deals separately with the unconsolidated general government debt.

B. Statistical description

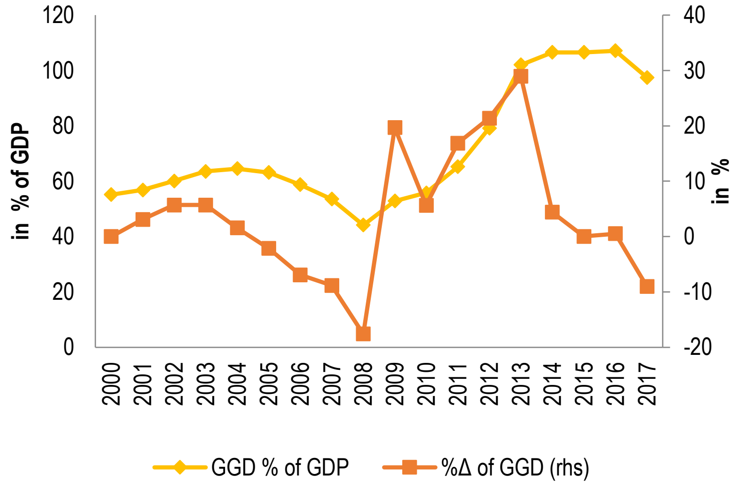
B.1 Size and evolution of General Government Debt

After four consecutive years of an upward path of general government debt, in 2017 the said debt has declined substantially by EUR 700 mn reaching EUR 18,7 bn at the end of 2017. This was mainly due to two partial early repayments of loans financed by liquid assets which were in excess of the necessary cash buffer accumulated throughout the previous years in order to ensure that the Government has sufficient liquidity to execute its payments in a timely manner in case the market conditions are not favorable.

The debt to GDP ratio marked a major decrease over 2017 from 107 percent in 2016 to 97 percent, as presented in Figure 9 below. The Figure also shows that the percentage change of debt as a ratio of GDP was on a downward pattern since 2013 and after a stabilisation at around zero percent in 2015-2016, a negative sign was marked in 2017 reflecting the reduction of public debt in absolute terms.

The net debt to GDP ratio which excludes accumulation of cash reserves, marked a substantial reduction by 8 percentage points reaching 94 percent at the end of 2017 compared to the previous year. It is noted that according to the MTDS, the level of cash reserves should satisfy the total financing needs of the forthcoming 12-month period. On the other hand, and taking into consideration that there is an opportunity cost of maintaining high cash reserves since the funding cost of the Republic is higher than the return of the buffer stock, the PDMO deposited a proportion of government cash with the banking system through proposals. More details about cash management are presented in Chapter 7.

Figure 9: Debt to GDP ratio evolution in 2000-2017



(Source: PDMO and Ministry of Finance)

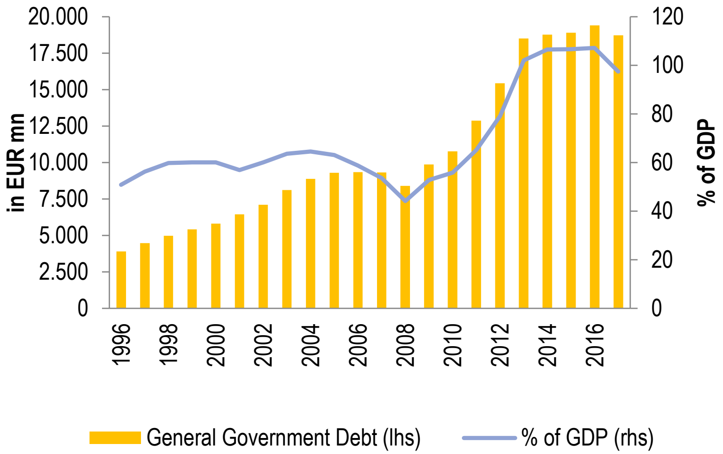
The historical debt evolution over the years 1996 to 2017 is presented in Figure 10 below. During the period 1996-2004, the general government debt followed an increasing path from 49 percent of GDP in 1996 to 64 percent of GDP in 2004. Following years of fiscal consolidation, and due to the use of available sinking funds, the debt-to-GDP ratio reached a low of 44 percent of GDP in 2008. Since then, fiscal slippage and low to negative growth rates and as well as capital injection into the banking sector and corrective measures under the Memorandum of Understanding, contributed to a considerable increase in the debt to GDP ratio.

During 2009-2011 the fiscal deterioration was the main contributor to the increase in the public debt. During 2012-2013 both the fiscal deficit and the negative growth rate contributed to the debt deterioration, but additionally the state capital support of the Cyprus Popular Bank (ex Laiki Bank) in 2012 and of the cooperative sector in 2013 increased the public debt by a total amount of EUR 3,5 bn, excluding interest payments.

The banking crisis resulted in state support to the domestic financial sector of currently EUR 3,6 bn or about 20 percent of the gross public debt by end 2014 excluding interest payments. These funds were related to the state recapitalisation of Cyprus Popular Bank and the cooperative sector via debt securities. In late 2015 the Government provided an injection of EUR 175 mn or about 1 percent of GDP of additional public funds into the cooperative sector.

It is important to highlight that despite the sharp increase in the public debt of the past few years, the strong fiscal outcome and the fact that the budget outcome was close to balance in 2014-2015 and positive in 2016, as well as, the positive real GDP growth of 2,0 percent and 3,0 percent in 2015 and 2016 respectively, indicate that debt is stabilising earlier and at lower levels than originally anticipated. The year 2017 was another year of strong fiscal outcome with positive real GDP growth of 3,9 percent and positive primary balance of 4,4 percent of GDP. The historical evolution of gross general government debt in values and as a percent of GDP for the period 1996-2017 is presented in table 4 in Appendix.

Figure 10: Trend in the consolidated general government debt in 1996-2017

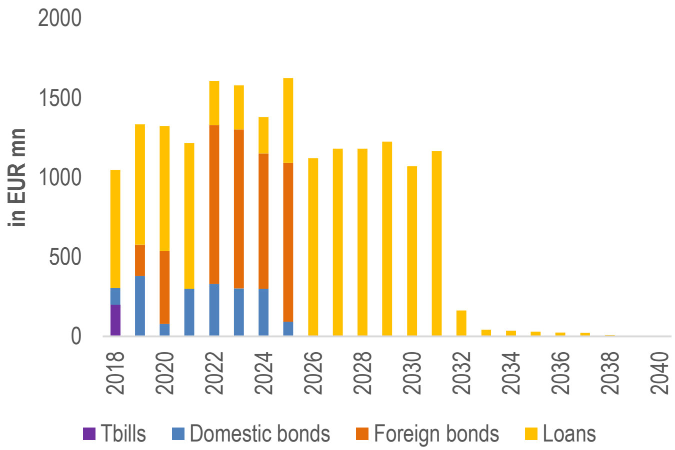


(Source: PDMO and Ministry of Finance)

B.2: Composition of the General Government Debt

This section presents the composition of the general government debt (GGD) at the end of 2017. The maturity structure of the GGD gives a clear picture of the distribution profile among different outstanding liabilities. Figure 11, illustrates the size of the debt sums maturing in each individual year given the outstanding GGD, excluding debt for European Financial Stability Facility (EFSF) loans as at the end of 2017. The said maturity profile shows moderate maturity sizes in 2018 and reduced maturities during the years 2019 to 2021, due to liability management transactions which were implemented in years 2014-2017. As a result, the debt maturities are within comfortable levels and within the objectives set in the MTDS 2016-2020. During the period 2018-2021, an amount of EUR 2500 mn or about 51 percent of the total debt due in the said period concerns the repayments of the bilateral loan granted by the Russian Federation.

Figure 11: General government debt redemption profile as at the end of 2017



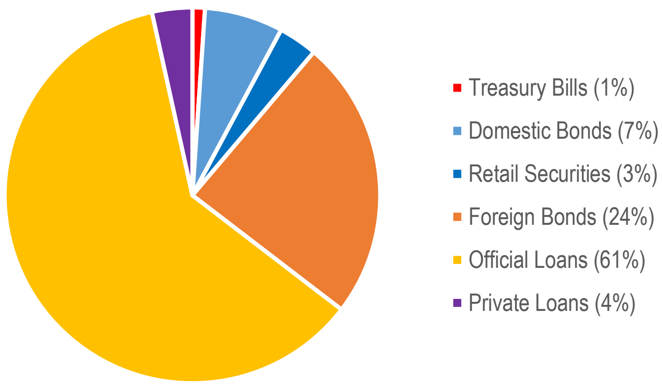
(Source: PDMO)

The share of the government debt by financing instrument, as at the end of December 2017, is illustrated in Figure 12 below. About half of the outstanding public debt in 2017 comprised loans disbursed to the Republic of Cyprus of which the vast majority, about 95 percent or EUR 11,4 bn, concerned official loans. About 60 percent of the official loans related to loans disbursed by the ESM and IMF during the years 2013-2016, whilst the remaining comprised other bilateral loans which were mainly disbursed by the Russian Federation, the EIB and the CEDB.

The second largest category of the outstanding government debt concerned foreign-law securities amounting to EUR 4,5 bn or about 24 percent of the total debt reflecting the increased importance of foreign market as a financing source.

The remaining share of the outstanding public debt (about 11 percent) concerned securities issued in the domestic market indicating that the said market will continue to serve as a complimentary financing source. This is not due to any deficiencies of the domestic market, but it is the result of our strategic decision for Cyprus to be a frequent issuer in the international markets. The outstanding central government debt as at the end of 2017 is presented in Tables 5, 6 and 7 in Appendix.

Figure 12: Share of general government debt by financing instrument in 2017

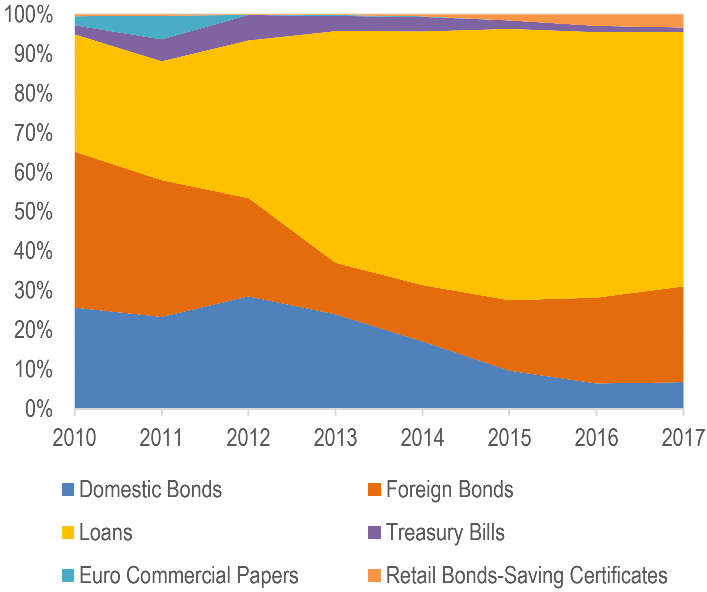


(Source: PDMO)

Figure 13 below, illustrates the historical breakdown of GGD by financing instrument during the years 2010-2017. During the said period, it is obvious that the vast majority of government debt concerned loans which increased abruptly in 2013 by 19 percentage points compared to 2012 and followed an upward trend until the end of 2015 reaching 69% mainly due to the official loans provided by ESM and IMF. In 2016 the level of loans was stabilized at 67% of public debt, whilst in 2017 the outstanding amount of loans marked a reduction by 3 percentage points. While in the past, domestic bonds were one of the main financing instruments with an average contribution of around 25 percent in years 2010-2013, since 2014 the contribution of domestic bonds to the general government debt has marked a significant reduction reaching 7 percent in 2017 compared to the peak of 29 percent in 2012. Nevertheless, domestic debt market is expected to continue to serve as an important complimentary financing source, due to its strategic importance.

On the other hand, EMTN securities have increased by 11 percentage points since 2013 reaching 24 percent at the end of 2017 reflecting the intention of Cyprus to maintain its presence in international capital markets and build up a pertinent sovereign yield curve.

Figure 13: Historical breakdown of GGD by financing instrument in 2010-2017

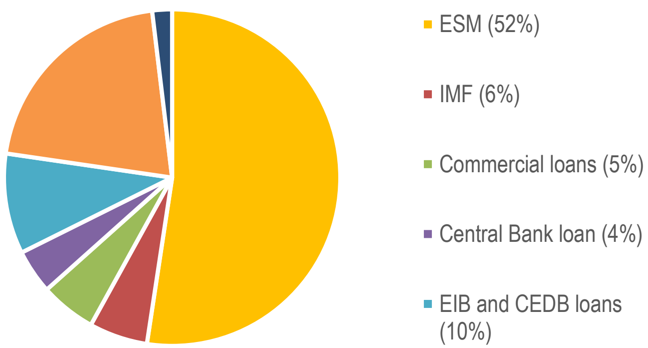


(Source: PDMO)

The distribution of outstanding loans by source as at the end of 2017 is presented in Figure 14 below. As mentioned above, the majority of the stock of outstanding loans as at end 2017 concerned the programme loans provided by ESM and IMF and the intergovernmental loan by the Russian Federation. The said loans stood at 79 percent of the outstanding loans at the end of 2017. The total value of Cyprus' loans from domestic sources was reduced significantly after the partial early repayment of the CBC loan in November 2017 reaching 9 percent of the outstanding loans at the end of 2017. Another important funding source was the loans disbursed by the EIB and the CEDB for the implementation of ongoing infrastructure projects. These loans constitute 10% of GGD as at the end of 2017. The said loans are provided to finance different projects such as the extension and modernisation of the facilities of the University of Cyprus, other projects for small-medium enterprises to enhance the growth and encourage the entrepreneurship, the construction of sewerage systems and rural settlements.

Finally, about 2 percent of the outstanding loans granted via the European Financial Stability Facility (EFSF) to Greece, Ireland and Portugal, as attributed to the creditor countries including Cyprus, are included in the debt statistics[5]. The government debt by instrument and lender as at the end of 2017 is presented in Table 7 in Appendix.

Figure 14: Distribution of loans by source as at the end of 2017

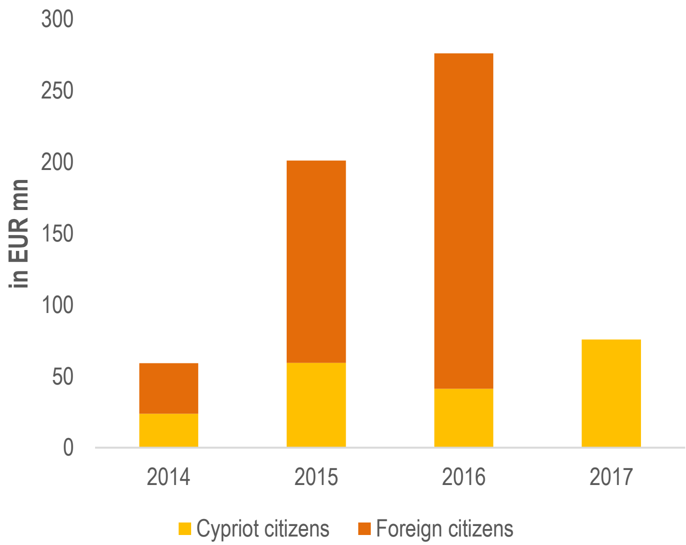


(Source: PDMO)

[5]The creditor countries have an equal amount of assets, as loans granted, in their balance sheet corresponding to the share of liabilities, i.e. the accumulated debt by the EFSF. However, any assets which may offset debt are not included in the general government debt, as this is reported on a gross basis.

Figure 15 below, shows the outstanding amount of retail bond sales by citizenship during the years 2014-2017. The majority of retail bond buyers during the years 2014-2016 were foreign investors due to the criteria for the obtainment of the Cypriot citizenship, as a measure to further encourage foreign investment and to attract high net worth individuals into doing business in the Republic of Cyprus. Since the launch of the scheme in 2014 and before the amendment of the criteria for the exceptional obtainment of the Cypriot citizenship in October 2016, foreign investors purchased about 76% of the total retail bond sales in years 2014-2016. After this amendment, the retail bond sales have been directed mainly to Cypriot citizens.

Figure 15: Distribution of retail bond sales by citizenship in 2014-2017



(Source: PDMO)

As mentioned earlier, in the case of the Republic of Cyprus, the three subsectors of the general government are the Central Government, the Local Authorities and the SSF. The Central Government includes all activities under the State Budget and two State-Owned Enterprises[6]. It is worth-noting, that the responsibilities of the PDMO in practice are currently limited to the debt management operations of the Central Government.

According to the Eurostat definition, as described above, the public debt is reported in consolidated form and as a result, any obligations among the general government subsectors are not shown explicitly.

The highest percentage of the consolidated GGD, in gross terms, is made up of the central government debt. As at the end of 2017, the share of outstanding central government debt, excluding debt to SSF, accounted for 98 percent of the general government debt on a consolidated basis. This share has historically been fairly constant.

Regarding the local authorities' loans, it is noted that the said loans were EUR 300 mn at the end of 2017. The borrowing of local authorities is related normally to infrastructure projects and typically the creditors are mainly local credit and cooperative institutions. This debt is thus in the form of long term bank loans with a floating interest rate. The stock of State-Owned Enterprises loans has also been declining due to continuous amortisation and absence of new borrowing reaching EUR 47 mn at the end of 2017 compared to EUR 58 mn at the end of 2016.

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[6]The State Owned Enterprises categorised within the central government and which have an outstanding debt balance are the Cyprus Sports Organisation and Cyprus Theatrical Organisation.

The third subsector of the general government, the SSF, does not have an outstanding debt balance. On the contrary, the Fund records an annual surplus which is invested with the central government, the total balance of which constitutes intra-governmental borrowing. This intra-governmental asset-liability relation is presented in section B:3 below.

B.3: Investments of the SSF and Administered Funds

Due to its historical annual surpluses the SSF has a very large stock of investments with the Central Government. Investments of the SSF in the form of deposits with the government or by ownership of government securities, at year end of 2017, amounted to EUR 7798 mn (Source: Social Insurance Services). The Funds, which are reported as a single account, in fact, comprise five different accounts:

1. The Social Security Fund;
2. The Unemployment Benefits Account;
3. The Central Holiday Fund;
4. The Termination of Employment Fund; and
5. The Insolvency Fund

Intra-governmental deposits

The majority of assets of the SSF are in the form of deposits with the Central Government. Annually, the surplus of the SSF is invested with the Government. By the end of 2017, the balance of the SSF in the form of deposits stood at EUR 7798 mn exhibiting minor increase in relation to the previous year balance of EUR 7663 mn.

Intra-governmental investments in government securities

In addition, the SSF in an effort to increase its revenue, has invested in Government EMTN bonds and Government domestic bonds. The total outstanding amount of investments in government paper was EUR 214 mn as at end 2017 and is presented in further detail in Table 8 in the Appendix.

It is noted that the SSF maintains also deposits with local credit institutions amounting to a total of EUR 84 mn at the end of 2017.

Intra-governmental investments by Administered Funds

In addition to the SSF, intragovernmental investments (debt) are done through other five Administered Funds. There are five Administered Funds of the central government with an outstanding balance at year end 2017 of EUR 123 mn of which EUR 61 mn concerned investments of the Turkish Cypriot Properties Fund, EUR 57 mn of the Government Hourly Employees Provident Fund and EUR 4 mn of the Hunting Fund. The other two administered Funds are:

1. The Human Resources Development Authority Fund; and
2. The Agricultural Insurance Organisation Fund.

It is noted that the outstanding balance of the above two Funds at year end 2017 was equal to zero. The surpluses of these Funds are invested in Government Promissory Notes.

Finally, the only intragovernmental debt existing between the local authorities and the central government are two loans which were granted in 2011[7] by the Municipality of Nicosia to the central government at a variable interest rate extending to 2035 and 2026 respectively, with a 5-year grace period. The total outstanding balance of the said loans at year end 2017 was EUR 9,0 mn.

[7] That was before the enactment of the Public Debt Management Law (2012) and of the Fiscal Responsibility and Budgetary System Law (2014).

VI. Cost and risks

A. Introduction

The analysis of cost and risk was incorporated in the MTDS for the years 2016-2020. The cost-risk trade off was examined using the MTDS Analytical tool, which captures scenario analyses on various borrowing strategies.

This chapter is organized into two sub-chapters. The first one provides the cost of the public debt in terms of interest payments and average interest rate. The second one discusses a number of risks of public debt.

B. Cost of the public debt

In this sub-chapter, the cost of the public debt is presented mainly on the basis of the interest payments to service the debt as well as by the weighted average cost of public debt.

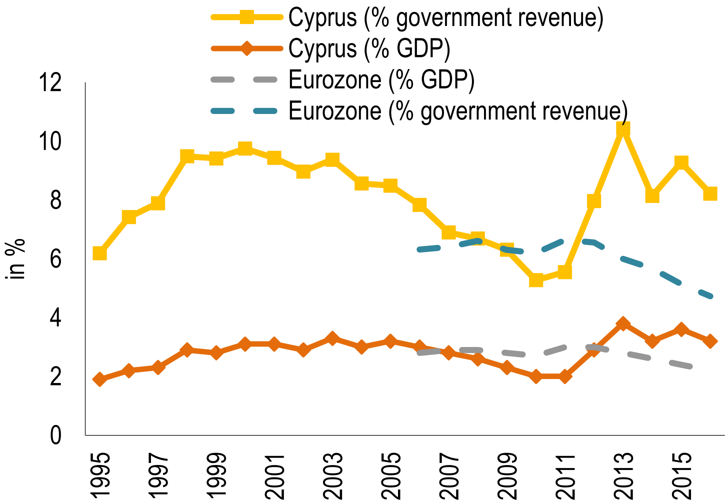
Historically, during the years 1995-2006 the average share of government revenue spent on the servicing of the public debt was 9 percent, with the highest share reaching 10 percent in 2000. The decrease of the public debt by around 9 percent in 2008 compared to 2007, contributed to the reduction in interest payments towards 7 percent of the government revenue and remained at around 6 percent in 2009-2010.

Then, due to the sharp increase of public debt in the next years as well as the rise in the borrowing cost itself, the share of government revenue for interest payments followed an upward path reaching 10 percent at the end of 2013. It then followed a downward direction reaching 8 percent at the end of 2016, as presented in Figure 16 below. It is noted that the increase of interest payable was partially offset by the low base rates.

Additionally, the interest payments as a percentage of GDP were close to 3 percent during the years 2000-2008 and then remained stable at around 2 percent until the end of 2011. Since 2012, the interest payments of Cyprus as a percentage of GDP have started to increase remaining above the corresponding values of the Eurozone average, as presented in Figure 15. It is important to highlight that despite the sharp increase of public debt during 2011-2013, the amount of interest payments was restricted by the considerable improvement in the borrowing cost due to official sources.

By the end of 2016, interest payments to GDP ratio was estimated at 3,2 percent compared to 3,6 percent of the previous year. This is explained by lower amounts of interest payments due to lower borrowing cost because of low interest rate environment in the Eurozone and improvements in the sovereign credit ratings and outturn for the Cypriot economy as well as higher GDP. As presented in the following Figure, the gap of interest payments as a share of GDP between the Republic of Cyprus and the Eurozone marked a reduction by 0,3 percentage points reaching 1,0 percent in 2017. The historical debt servicing in 2010-2017 is presented in Table 9 in Appendix.

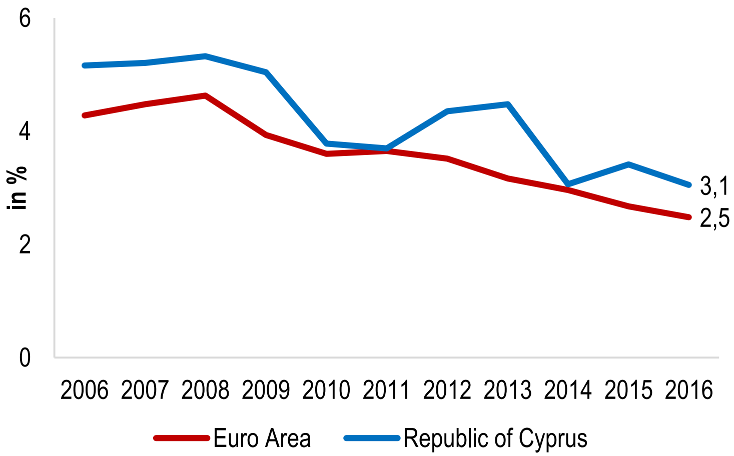
Figure 16: Distribution of interest payable on public debt during 1995-2016



(Source: PDMO and Eurostat)

Figure 17 illustrates the distribution of interest payable over debt for the Republic of Cyprus compared to Euro area countries in 2006-2016. Since 2013, interest payable to debt ratio is on a downward path exhibiting minor fluctuations. Regarding the gap between the Republic and Euro area countries, there is a convergence reaching 0,6 percent at the end of 2016 compared to 1,3 percent in 2013.

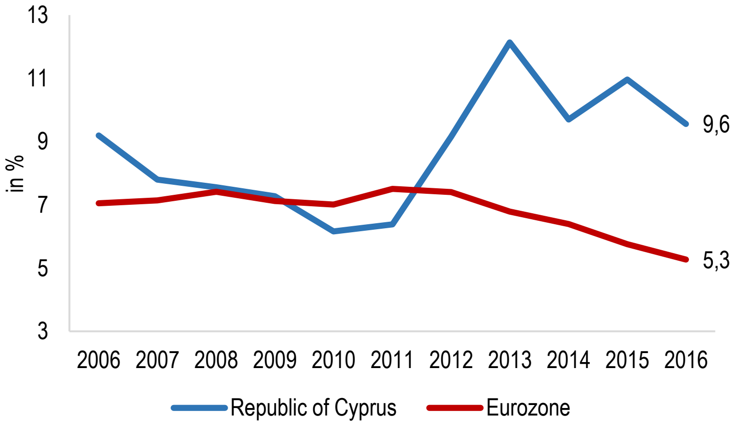
Figure 17: Distribution of Interest payable$_{(t)}$ to Debt $_{(t-1)}$ in 2006-2016



(Source: PDMO and Eurostat)

Figure 18 illustrates the distribution of interest payable to tax revenue for the Republic of Cyprus compared to Euro area countries in 2006-2016. Since 2013, the gap is on a downward path exhibiting fluctuations towards the end of 2016 where the gap close to 4,3 percent. Although there is a significant difference, we expect a reduction of the gap underpinned by further improvement of public finances in the next years.

Figure 18: Distribution of interest payable to tax revenue in 2006-2016



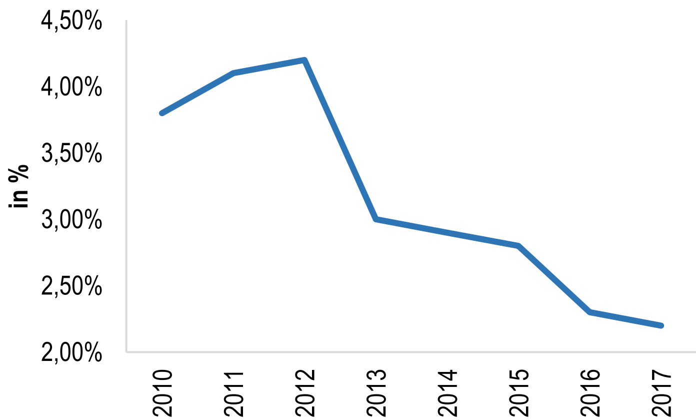
(Source: PDMO and Eurostat)

Another measure reflecting the overall rate being paid by the State on public debt financing is the weighted average cost of debt (WACD), although this alone does not indicate its burden on the public finances or the economy as a whole. This indicator provides to investors information concerning the creditworthiness or the riskiness of the State implying that riskier States generally have a higher WACD. Within this framework, this indicator is very important for the sustainability of the public debt.

As presented in Figure 19 below, during the years 2010-2012, the WACD followed an upward trend reaching 4,2 percent at the end of 2012. One year later the WACD marked a significant reduction by 1,2 percentage points in relation to 2012 mainly due to the official funding provided by ESM and IMF at low interest rates. During 2013-2017 the

WACD followed a downward trend reaching 2,2 percent at year end of 2017 as a result of the positive impact from the low cost ESM and IMF loans as well as from the liability management transactions implemented by the PDMO and the environment of low interest rates in the European capital markets. A necessary pre-condition to enhance the sustainability of public debt, is to achieve and maintain the WACD in the area below the level of the nominal growth rate of GDP.

Figure 19: Weighted average cost of debt in 2010-2017



(Source: PDMO)

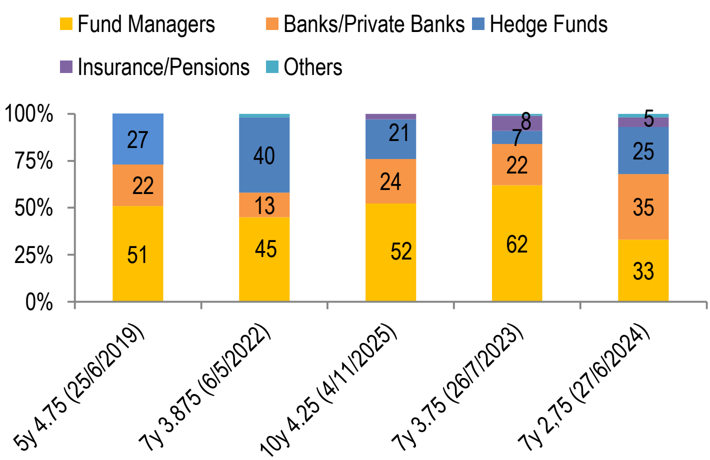
As mentioned in chapter 2, in order to minimise the marketable debt borrowing cost, the PDMO increased its efforts to further expand the investor base for EMTN issuances. Since 2016, marketing activities are increased covering more financial centres in US and EU markets.

The evolution of investor distributions by geography and type are presented in the Figure 20 and 21 respectively.

During the last issuance in June 2017 (due in 2024), the increased participation from Hedge Funds of the order of 25 percent was attributed to the switch offer transaction. The new benchmark EMTN in June 2017 was issued in conjunction with a switch offer of three EMTNs due in 2019 and 2020 and as a result a priority was given to existing bond holders including Hedge Funds.

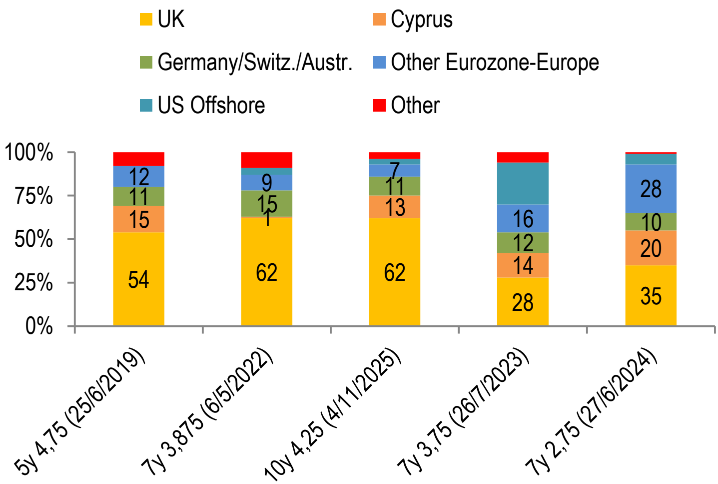
With regards to investor distribution for EMTNs by geography, it is worth-noting that during the last two issuances in July 2016 (due in 2023) and in June 2017 (due in 2024), a more balance distribution was achieved between investors. Investors from UK took the lion's share of final allocations, whilst an increased participation marked from Cypriot investors.

Figure 20: Evolution of investor distribution for EMNTs by type during 2014-2017



(Source: PDMO)

Figure 21: Evolution of investor distribution for EMNTs by geography during 2014-2017



(Source: PDMO)

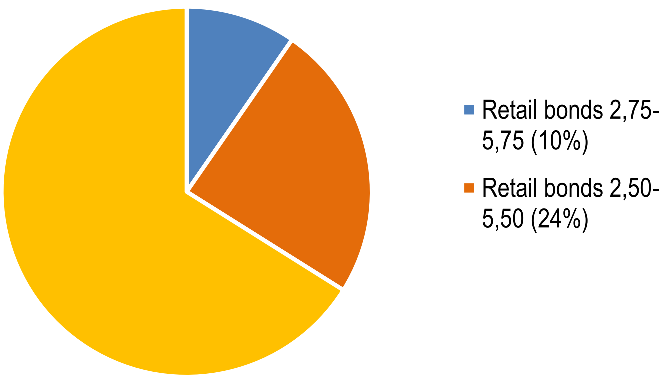
Furthermore, it is important to highlight that the refinancing of the short term debt was achieved at negative interest rates since February 2017 reaching -0,08 percent at the end of 2017. The weighted average yield of short term debt in 2017 exhibited a significant reduction reaching -0,05 percent from 0,6 percent which was in 2016.

Regarding the interest rates of retail bonds, it is noted that in October 2017, the PDMO announced the reduction of interest rates under the terms of issuance on six-year government bonds for natural persons as of the 1st series of 2018. The new step-up structure of interest rate starts from 2.25 percent in the first year and gradually increases to 3.00

percent if retained until the sixth year (see Announcement in Appendix).

Figure 22 below, shows the distribution of retail bonds by interest rate structure at the end of December 2017. About 2/3 of the outstanding amount of retail bonds ranged in the spectrum between 2,50 percent to 3,25 percent. The second largest category concerned retail bonds with interest rates between 2,50 percent to 5,50 percent.

Figure 22: Distribution of retail bonds by interest rate structure



(Source: PDMO)

C. Risks

C.1: Introduction

Risk management has become an increasingly important tool for achieving strategic debt targets. Therefore, the risk management framework is an integral part of the MTDS for the years 2016-2020 in which a number of quantitative risk targets were set by the PDMO.

The process of establishing and executing a strategy for managing the public debt contains unavoidable both financial risks as well as non-financial risks such as operational risks. All of these risks are added to existing fiscal risks for the Government.

The most important categories of financial risks are the refinancing risk, the interest rate risk and the foreign exchange risk. In general, the developments of 2017 on the debt portfolio risks were positive. The liability management transactions executed in 2017 have certainly led to an improvement in the debt maturity profile, thereby mitigating refinancing and liquidity risks. The floating rate debt provided by ESM remained stable as was in the previous year whilst the rate by IMF recorded a decrease, albeit still high, taking into consideration that these loans are indexed at low interest rates, the interest rate risk is limited.

Debt maturity profile marked an improvement with the high concentration of maturities in the years 2019-2020 reduced significantly at manageable levels. The current MTDS 2016-2020 is focusing on longer-term issuances in order to avoid the need to mitigate portfolio risks through liability management transactions, which are costly.

It is important to highlight that risk management of public debt does not, in the ordinary application, cover the debt sustainability assessment since the latter is related mostly to fiscal and macroeconomic indicators, conventionally the GDP and the fiscal balance. Thus, the debt sustainability analysis focuses on macroeconomic factors and prospects and is not the subject of public debt management. However, the evolution of these parameters in conjunction with the WACD is closely monitored by the PDMO.

C.2: Financial and non financial risks

This section has twofold objectives, of which the first one is to cover the analysis of the most important financial risks associated with the debt management operations whilst the second one is focusing on a discussion about the operational risks.

C.2.1: Financial risks

Refinancing risk

Refinancing risk is the probability (risk) for the Government to face a situation where a share of debt reaching maturity can only be replaced with the issuance of new loans at very high cost or, in the extreme case, can not be refinanced at all.

In order to capture the refinancing risk of the Government, two indicators were used. The first one is the share of debt due within 1 year and the second one is the share of debt due within 5 years.

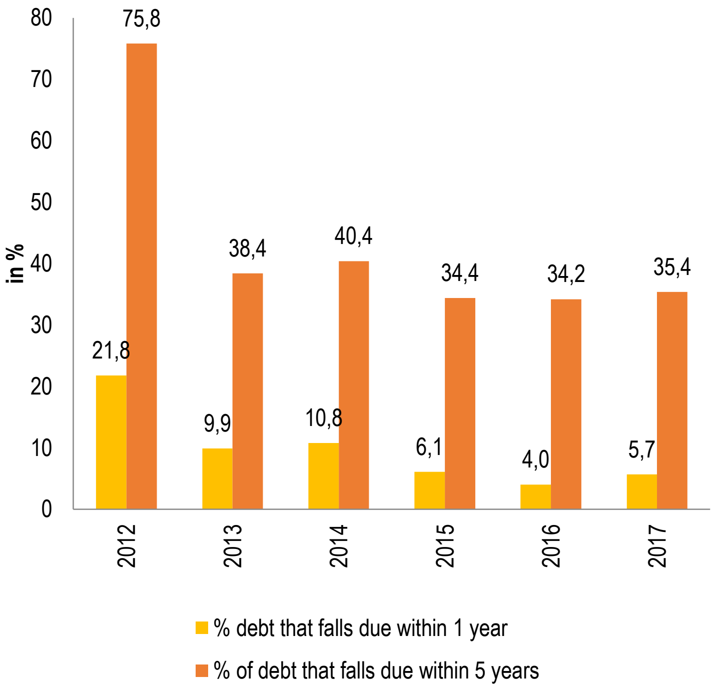
As presented in Figure 23 below, the share of debt due within 1 year followed a decreasing path since 2012. The large reduction of share of debt due within 1 year from 22 percent in 2012 to 10 percent in 2013 was attributed to the long term official funding granted by ESM and IMF. In the following years, the said indicator has continued to improve underpinned mainly to the disbursements granted by ESM and IMF and to a lesser extent to the liability management transactions implemented during 2014-2017.

The debt redemptions due within 1 year at the end of the year 2017 marked an increase reaching 5,7 percent compared to 4,0 percent in 2016 reflecting the commencement of Russian loan repayment in 2018 with a total amount of EUR 625 mn per year. Taking into consideration that the share of debt due within 1 year decreased significantly reaching comfortable levels, the refinancing risks exposure is at an acceptable level of risk.

Regarding the share of debt due within 5 years, there has been also an improvement since the said share was reduced by more than 40 percentage points in only 3 years reaching 35,4 percent of the public debt at the end of 2017 compared to 75,8 percent in 2012.

Although the share of debt due within 5 years exhibited a significant improvement, in order to mitigate the refinancing risk exposure, the Republic of Cyprus is focusing on longer term issuances improving further the debt maturity profile.

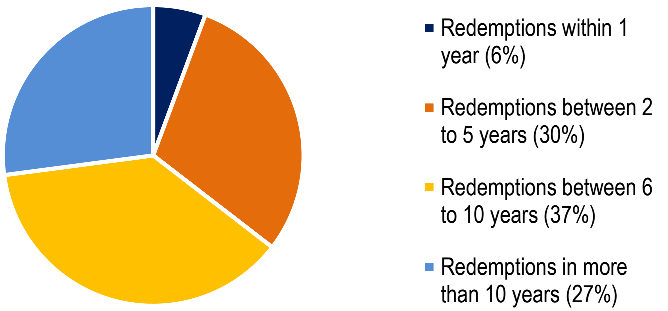
Figure 23: Share of debt refinancing due within 1 year and 5 years in 2012-2017



(Source: PDMO)

Figure 24 below, shows the debt refinancing distribution of the total debt of the Republic of Cyprus in four categories as at the end of 2017. The majority of the debt redemptions fall due in the segment between 6 to 10 years similar at the end of 2016 since ESM loans will start to be repaid as from 2025. The second largest category of redemptions of the order of EUR 5,8 mn fall in the segment between 2 to 5 years. About 43 percent of the redemptions fall in this segment related to Russian loans, which is expected to be fully repaid by 2021. However, about 28 percent of redemptions in the said segment concerns three EMTNs due in 2019, 2020 and 2022.This might constitute an indicator which justifies the adoption of additional MTDS operations in order to mitigate further the refinancing risk exposures.

Figure 24: Total debt[1/] refinancing distribution as a percent of GGD at the end of 2017

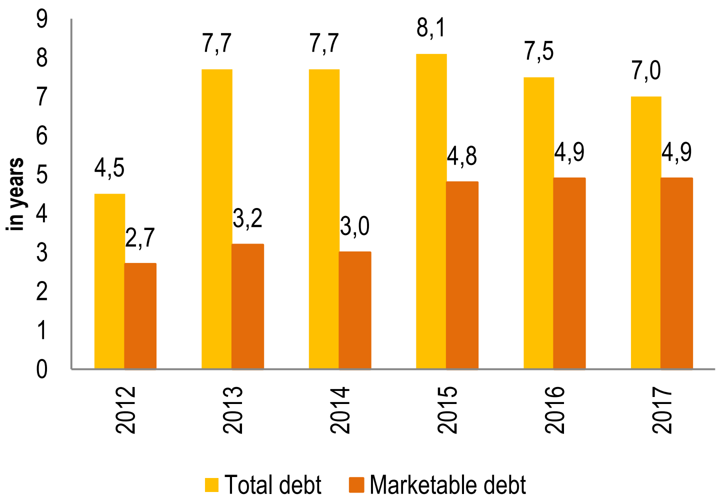


(Source: PDMO)
1/ = Loans to EFSF are excluded

Another risk indicator which captures the refinancing risk is the weighted average maturity of debt. As presented in Figure 25 below, the outstanding average maturity was 7,0 years for the total debt and 4,9 years for the marketable debt. Comparing these sizes with the corresponding sizes at the end of 2012, the situation has improved significantly showing the positive contribution of both long term official loans by ESM and IMF and other bilateral loans such as by EIB, CEDB and Russian loan as well as of liability management transactions implemented by the PDMO.

Thus, the outstanding loans were spread over a long maturity and this reduces the share of debt that has to be refinanced every year indicating a reduction of the refinancing risk. The focus on longer-term issuances under the MTDS 2016-2020 is expected to improve further the weighted average maturity of marketable debt.

Figure 25: Weighted average maturity of debt (in years) in 2012-2017 as at the end of 2017



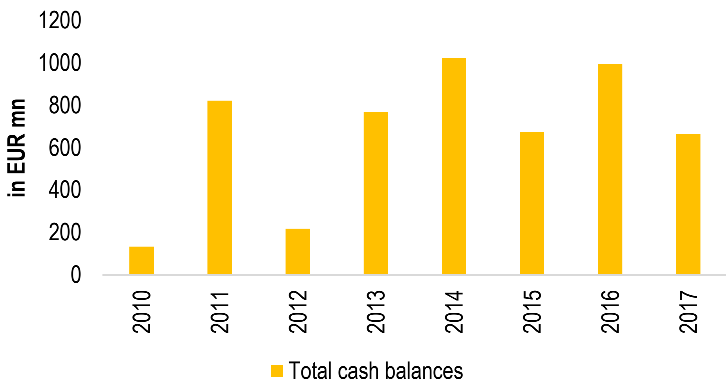
(Source: PDMO)

Liquidity risk

The annual cash balances in years 2010-2017 are presented in Figure 26 below. The liquidity levels of the Government were comfortable since 2013 due to the fiscal outcomes being better than expected as well as to the successful EMTN issuances, allowing the enhancement of the cash reserves. The total cash balances reached EUR 664 mn at the end of 2017. This amount was sufficient to cover the needs of the next 9 months excluding rollovers (TBs) during the year.

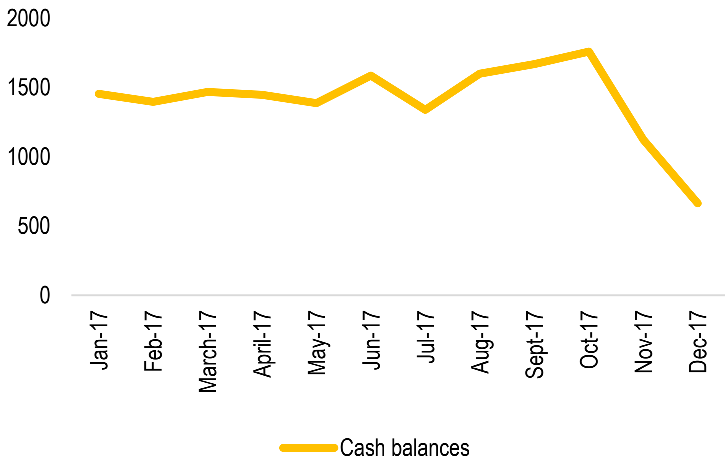
As presented in Figure 27 below, the total liquid funds exhibited a large reduction in November 2017 due to the partial early repayment of the CBC loan financed by cash balances. Two months later, the total liquid funds marked a significant increase. The financing needs cover ratio of 2017 is illustrated in Figure 33 under the Chapter “Cash management”.

Figure 26: Cash liquidity levels in 2010-2017



(Source: CBC)

Figure 27: Cash liquidity levels on a monthly basis in 2017



(Source: CBC)

Interest rate risk

Interest rate risk for the Government refers to the risk it will have due either to the refixing of interest rates at the time of refinancing of outstanding debt or to the fluctuation of interest rates at the time of interest payments for debt carrying floating rates.

The interest rate distribution of debt has changed dramatically in 2013, as presented in the Figure 28 below. Following the Memorandum of Understanding in March 2013 on EAP, the interest rate distribution has changed significantly mainly due to the borrowing by the ESM and IMF[8] at floating interest rates. In fact, the loans from the ESM and IMF were used to refinance the Cyprus debt which had fixed interest rate

[8]Actually the IMF loans have a large predefined fixed component and a smaller floating rate component.

reducing therefore share of the fixed rate debt. Another reason for the above change on the interest rate distribution was the borrowing by the EIB and CEDB at floating interest rates with low margins over the Euribor. It should be noted that the extension of the weighted average maturity of marketable debt restricted the interest rate risk.

Therefore, the floating interest debt was increased by 24 percentage points reaching 36 percent at the end of 2013 compared to 12 percent at the end of 2012, prior to the loan agreement of EAP.

As the loan disbursements by ESM and IMF were released, the proportion of debt at floating rate followed an upward path reaching 46 percent at the end of 2016 which was the last year of the financial assistance programme. Taking into consideration that the vast majority of floating rate debt is indexed at low interest rates, as presented in Figure 29 below, the interest rate risk is expected to be limited. Specifically, loans by ESM and IMF[9] of EUR 6,9 bn or about 81 percent of total floating rate debt are indexed at low rates whilst an amount of EUR 1,3 bn or about 15 percent of the total floating rate debt by EIB, CEDB and Cyprus Cooperative Bank are indexed at low margins over the Euribor rate. Also, other loans to local authorities as well as to State-Owed Enterprises carry floating rate interest.

Given, however, the historically current low interest rate period, interest rates in general are expected to gradually rise.

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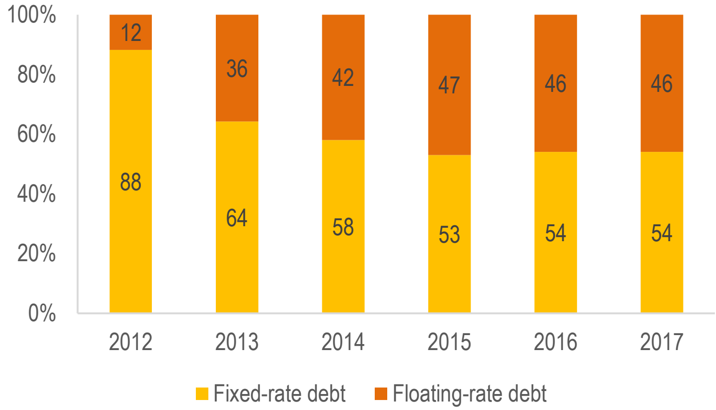
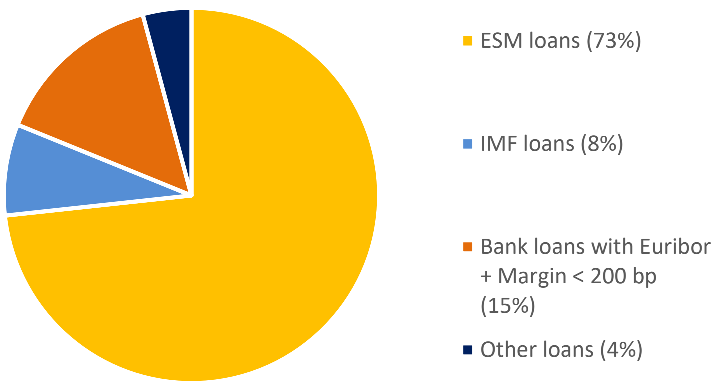
[9] IMF loan was estimated according to the exchange rate of Euro/SDR as at 29 December 2017.

Figure 28: Evolution of interest rate distribution of debt in 2010-2017



(Source: PDMO)

Figure 29: Composition of floating-rate debt as at the end of 2017



(Source: PDMO)

Furthermore, it is important to highlight that in 2017 ESM proceeded with amendment of its borrowing guidelines for non-EUR issuances in order to expand the investor pool and reduce the risks arising from adverse circumstances in the euro markets. This amendment is expected to affect the borrowing cost of the ESM either positively or negatively affecting ultimately the cost of debt held by beneficiary member states of ESM/EFSF funding, including Cyprus, and therefore it should be noted. The first non-EUR issuance was executed in October 2017 in US currency in the US market.

Foreign exchange risk

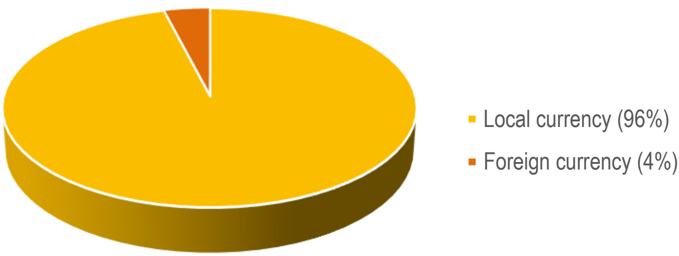
Although foreign currency debt has many benefits such as access to a large investor base and the geographical independence with possible interest rates benefits, foreign currency financing has substantial risks. Some of the risks are the increase of the country's external vulnerability to exchange rates in case of large-scale foreign issuance (new borrowing) and the increase of outstanding debt servicing and debt burden in case of a significant depreciation of the domestic currency.

Figure 30 shows the currency composition of debt as at the end of 2017. The majority of the public debt is denominated in domestic currency whilst only EUR 676 mn or about 4 percent of the outstanding GGD is denominated in foreign currency. This percentage refers to the loans from the IMF which, are denominated in SDR[10].

[10]The SDR is an international reserve asset, created by the IMF in 1969 and it was defined as a basket of currencies. The SDR basket consists of the U.S dollar, the euro, the Chinese renminbi (RMB), the Japanese yen, and the British pound sterling (Source: IMF).

Taking into account that the capital payments for the IMF loan due to an early partial repayment made in 2017 reduced the outstanding balance of the said loan and the fact that SDR includes also the euro, we conclude that the foreign exchange risk is limited. The exchange rate of EUR/SDR decreased by almost 6,9 percent reaching to EUR 1,18747 per SDR at the end of 2017 from EUR 1,27534 per SDR at the end of 2016 indicating a significant depreciation of foreign debt denominated in SDRs.

Figure 30: Currency composition of debt as at the end of 2017



(Source: PDMO)

Credit risk

Credit risk or counterparty risk for the government is the risk relating to the government's credit exposure to individual counterparties through swap transactions and the investment of liquid assets.

During 2017, there were no outstanding derivative exposures for the Republic of Cyprus. Regarding the deposit levels in the money market, there was an amount of EUR 430 mn since January 2017, which was deposited in MFI. During the period June-July 2017, the said amount exhibited a reduction by EUR 100 mn and toward the end of the year 2017, the deposit levels in the MFIs marked an increase reaching EUR 380 mn or about 57 percent of the total cash balances. The deposits are overcollaterised. More information is presented in Chapter 7.

In conclusion, the credit risk for the government in the reference period is material and cannot be ignored, nevertheless taking into consideration that the said deposits are under collateral, the credit risk is partially mitigated.

C.2.2: Non Financial risks

Operational risks

Operational risk may arise mainly from the potential difficulties of implementing effective internal procedures, the lack of human resources, the internal control systems and the possible lack of appropriate software and computer systems. In order to enhance the above infrastructure, at the request of Cyprus, technical assistance was received by the ESM. The technical assistance provided by the ESM covered both an evaluation of internal organisation and IT infrastructure of the PDMO as well as proposals for the creation of a pool of information and knowledge about capital markets and further enhance relationships with investors. Appropriate technical assistance was also provided by the IMF for issues concerning MTDS as well as by the C for the appropriate software.

The roadmap for actions for the period 2015 (Dec.) -2020 (Dec.) concerning the internal organization and IT infrastructure of the PDMO was approved by the Council of Ministers of the Republic in September 2015. The implementation progress is described under the final chapter, namely “PDMO action plan”.

The implementation of the roadmap for actions will enable the PDMO to further reduce the operational risks while undertaking public debt management operations and strengthen its capacity for effective market access, executing economic analyses, monitoring developments and designing an effective strategy.

C.3: Contingent liabilities

C.3.1: Introduction

Granting government guarantees (GG) to financial institutions is a common feature of government policy all over the world. In some cases, the cost for certain borrowers is too high due to asymmetry of information and therefore, the provision of GG may help to overcome the said issue. GG enhance the scope of financial intermediation within the financial system.

On the other hand, GG legally and explicitly bind the government to make loan repayments on behalf of a borrower that defaults. Therefore, they constitute a contingent liability that might impose fiscal costs on the government, which adversely affect the public finances and the public debt sustainability.

C.3.2: Government guarantees framework

Pursuant to a decision of the Council of Ministers in June 2015, the responsibility of management and coordination of procedures relating to guarantees was assigned to the Treasury of the Republic of Cyprus. For this purpose, an amendment of the PDML was enacted.

C.3.3: Statistical description of Government Guarantees

Taking into consideration the above amendment of the PDML, this section describes only the main developments[11] regarding GG.

[11] Detailed analysis of explicit contingent liabilities is presented in the website of the Treasury of the Republic

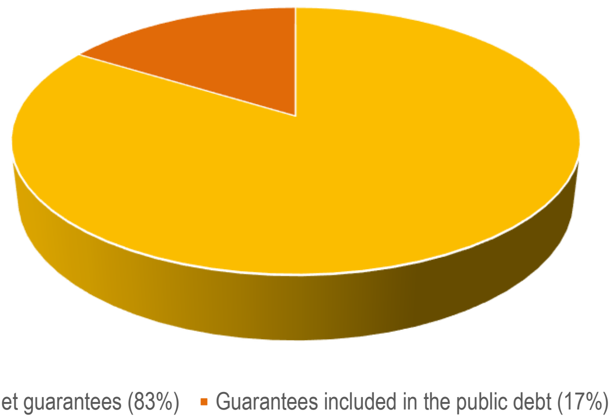
The Republic of Cyprus had outstanding GG[12] for loans as at end 2017 of EUR 1,93 bn or about 10 percent of GDP, which is slightly lower than the relevant stock of EUR 1,97 bn at the end of 2016. Excluding the GG granted to entities of the general government (since the outstanding amount of these guarantees is also included in the general government debt), the net value of outstanding GG was EUR 1,64 bn or about 8,5 percent of GDP as at end 2017. It is noted that the GG portfolio is denominated fully in euro. Analysis of the outstanding stock of government guarantees as at end 2017 is presented in table 10 in Appendix.

http://www.treasury.gov.cy/treasury/treasurynew.nsf/page22_en/page22_en?OpenDocument

[12] Called guarantees and guaranteed loans which have been given by the Cyprus Cooperative Bank to refugee cooperative companies for settle the deposits of the refugees are excluded.

Figure 31 shows that an amount of EUR 313 mn or about 16 percent of the total value of outstanding guarantees is also included in the public debt as at end 2017.

Figure 31: Outstanding GGs in percent as at the end of 2017



(Source: Treasury)

Regarding the called guarantees, an amount of EUR 36 mn or about 2 percent of the outstanding amount of government guarantees at the end of 2017 was called. The majority of the called guarantees concerned natural persons. More information is presented in the website of the Treasury of the Republic.

VII.Cash Management

Governments need to ensure an effective implementation of a cash management framework in order to meet with a high degree of certainty their financial obligations of debt servicing payments in a timely manner as well as to avoid the accumulation of idle cash balances which can increase the cost of holding cash. Furthermore, liquid financial assets can provide a high degree of flexibility in debt and cash management operations and enable governments to absorb shocks where access to borrowing in capital markets is costly. An efficient cash management framework enables debt managers to manage the trade-offs between expected cost and risk in the public debt portfolio.

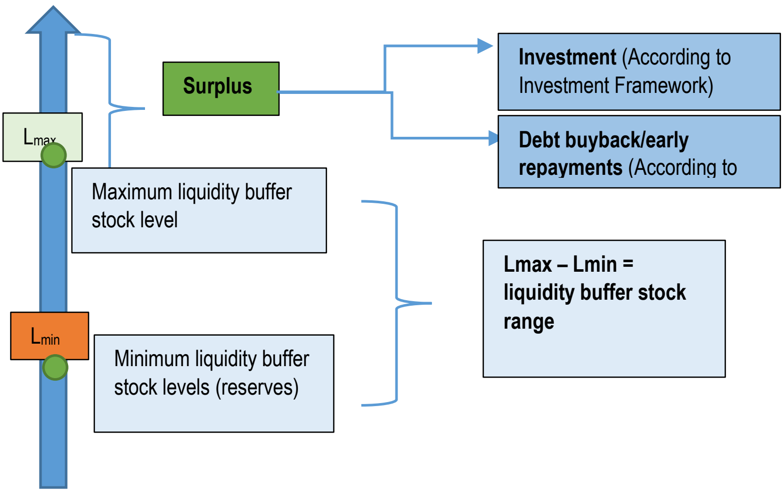
Pursuant to article 21 of the PDML, the PDMO has the responsibility to retain the liquidity buffer stock range by borrowing the necessary funds in time. The PDML authorizes the PDMO to operate an active cash management framework in order to ensure a satisfactory return on the liquid funds maintaining refinancing risk to a minimum level.

The institutional structure of the government cash management pursuant to articles 20 and 21 of the PDML, that has been set, via a decision of the Council of Ministers is presented in Figure 32. A maximum and a minimum liquidity buffer stock level are determined by the PDMO within the General Government Account taking into account, among others, the variability of the markets and the current credit facilities of the Republic of Cyprus.

When the cash amount exceeds the maximum buffer stock level, the said surplus can be invested by the PDMO according to the Investment Policy Framework for cash management or it can be used either to buyback outstanding securities of the Republic or for the early repayment of loans according to the AFP.

During the year 2017 and taking into consideration that the government liquidity was above the maximum liquidity buffer stock level, the PDMO pursuant to article 21 of the PDML, proceeded with three offers for government deposits within the banking sector of the Republic of Cyprus according to the provisions of the cash investment policy. The total government deposits at MFIs at the end of 2017 was EUR 380 mn. The annual interest earned by the above said transactions was close to EUR 2 mn. Table 11 in Appendix, shows the historical distribution of total cash balances held with the CBC and cash deposited with MFIs.

Figure 32: Institutional structure of the government cash management

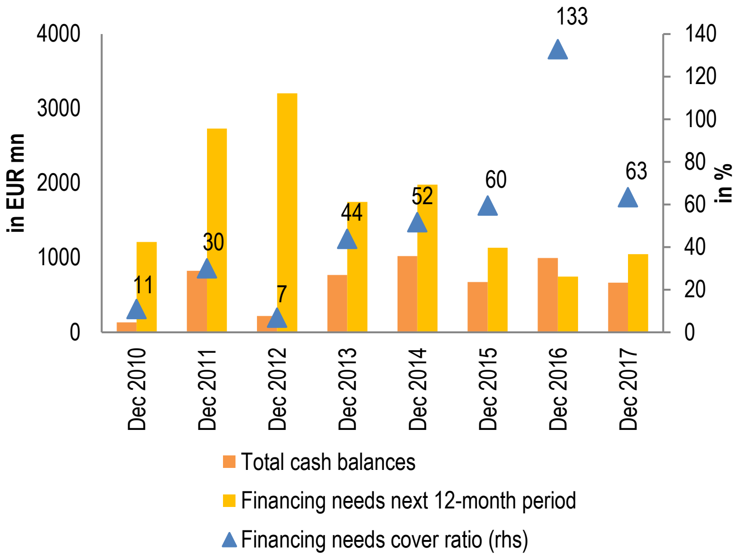


(Source: PDMO)

Figure 33 below, shows a comparative analysis between the historical distribution of total cash balances and the amount of debt which falls due within next year based on the statistical information at the end of the current year. The financing needs of the next 12 months has peaked at the end of 2012 with the financing needs cover ratio reaching only at 7 percent. Taking into consideration the implementation of an active cash management on the one hand and the liability management transactions on the other hand in conjunction with the long-term loans issued by the ESM-IMF, the PDMO has achieved since 2012 to reduce the short-term financing needs and improved significantly the share of debt that falls due within the next year covered by cash balances.

The enhancement of the liquidity position of the Republic of Cyprus at the end of 2016 has reduced significantly the refinancing risk. On the other hand, in order to minimize the cost of idle cash balances and taking into account the low interest rate environment to invest cash balances in combination with the fact that the ability of the sovereign to access capital markets on increasingly favourable terms has improved, the State has decreased the amount of cash reserves in year 2017.

Figure 33: Distribution of cash balances and amount of debt that falls due within one year in 2010-2017



(Source: PDMO and CBC)

VIII. Sovereign Credit Ratings of the Republic of Cyprus

Credit Rating Agencies (CRAs) play a pivotal role in financial markets by helping reduce any information asymmetry between lenders and investors, on the one hand, and different sovereign issuers on the other hand regarding the creditworthiness and the prospects of individual economies.

Pursuant to article 26 of the PDML 2012-2016, the PDMO is the Liaison with the International CRAs and it can enter into contracts on behalf of the Republic of Cyprus with the CRAs.

It is noted that the Republic as a sovereign issuer, maintains a contractual (solicited) relationship with four CRAs, namely DBRS, Fitch, Moody's and Standard and Poor's.

The Cypriot economy continued to improve its economic resilience and record a stronger positive rate of growth in 2017 compared to the previous year which was reflected in the upgrade of the credit profile of the Republic of Cyprus. During 2017 Cyprus' government bond rating was upgraded and the outlook was changed/maintained to positive by the above four CRAs.

Standard & Poor's upgraded Cyprus' government bond by 1 notch to 'BB+' in March 2017 with stable outlook while in September 2017 changed the outlook to positive from stable indicating a likelihood of an upgrade within the next 12 months if specific conditions are met.

In June 2017 DBRS upgraded Cyprus' government bond by 2 notches to 'BB (low)' from 'B' with stable outlook while in December 2017 changed the trend to positive from stable indicating a likelihood of an upgrade within the next 12 months if specific conditions are met.

In July 2017, Moody's upgraded Cyprus' government bond by 1 notch to 'Ba3' and changed the outlook to positive from stable. It is noted that based on Moody's Press release for Cyprus issued in July 2017, the decision to maintain the outlook to positive after an upgrade reflects Moody's view that improvements in economic resilience and continuing fiscal performance are likely to be sustained.

Similar decision had been taken by Fitch in October 2017 since it upgraded Cyprus' long-term issuer default ratings by 1 notch to 'BB' from 'BB-' and maintained the outlook to positive indicating a likelihood of an upgrade within the next 12 months if specific conditions are met.

Table 6 below, illustrates where the Republic of Cyprus stood at end 2017 in terms of credit ratings comparing with the corresponding ratings in 2013. The situation has been improved significantly. For the reference year 2017 and specifically since March 2017, the Republic of Cyprus is one notch below investment grade by Standard & Poor's and it is in positive outlook by all four CRAs.

Table 6: Solicited sovereign credit ratings as at December 31, 2017[13]

Long-term debt

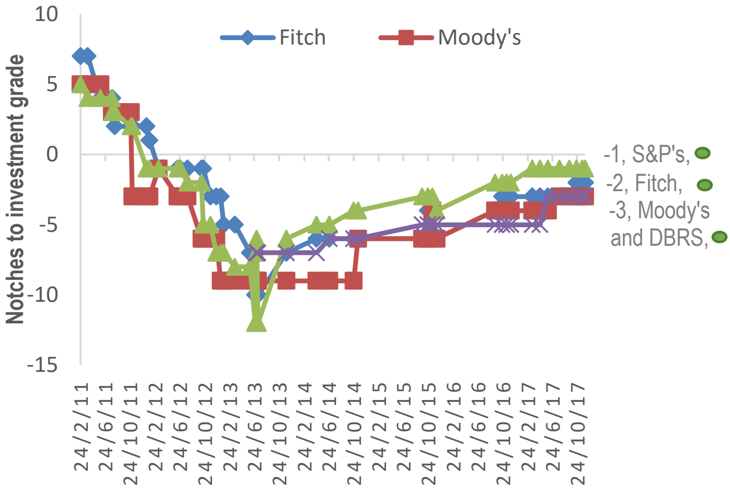
	Rating as at 31/12/2017			Rating as at 30/6/2013		
CRAs	**Rating**	**Outlook**	**Notches to investment**	Rating	Outlook	Notches to investment
DBRS	**BB (low) (Dec. 2017)**	**Positive**	**3**	CCC[1/]	Negative	7
Fitch	**BB (Oct.2017)**	**Positive**	**2**	RD	Negative	10
Moody's	**Ba3 (Nov. 2017)**	**Positive**	**3**	Caa3	Negative	9
Standard & Poor's	**BB+ (Sept. 2017)**	**Positive**	**1**	SD	Negative	12

Source: PDMO
1/ = The first rating of the DBRS for the Republic of Cyprus done in 12/7/2013

The historical credit ratings of the long-term issuer rating of the Republic of Cyprus during the years 2011-2017 are illustrated in Figure 34 below. The Republic of Cyprus is on an upgrading path of up to 11 notches since 2013 which reflects the economy's turnaround. At the end of 2017, as mentioned earlier, the outlook remains positive by all CRAs.

[13] More recent developments in the sovereign credit rating of the Republic of Cyprus are available at the website of the PDMO.

Figure 34: Historical evolution of credit ratings of the Republic of Cyprus in 2011-2017



(Source: PDMO)

= positive outlook

Regarding the rationale of the rating and outlook developments of the Cypriot economy in 2017, the upgrade of the Republic by DBRS[14] was attributed to Cyprus's strong fiscal outcomes during the past two years as well as to the decline of imbalances in the private sector. The two key drivers for the rating upgrade were the improvements in the 'Fiscal Management and Policy' and the 'monetary policy and financial stability sections'. DBRS made a reference to the solid fiscal performance, Cyprus attractiveness as a business centre and a tourist destination as well as its favourable public debt maturity structure.

[14] DBRS Press Release in June 2, 2017.

However, the rating agency underlined the depth of Cyprus challenges such as the high levels of private and public sector debt, the sizeable non-performing loans in the banking sector, the external imbalances as well as the small size of its service-driven economy.

In the case of Fitch's rating[15], the upgrade was based on the strong improvement in the public finances, the broadening of the economic recovery and the strong track record of GDP growth over performance on forecasts over recent years. The CRA made references to the main weaknesses of the Republic relative to rated peers which are the external finances and structural features. The first factor reflects the very high net external debt relative to peers and the fact that the Republic is not fully benefiting from the euro's reserve currency status influencing the fiscal and external financing flexibility.

The government bond rating of Cyprus upgraded by Moody's[16] due to the improvements in economic resilience observed during the past two years as well as the consistent outperformance on fiscal targets and at the same time on continuing favourable fiscal outlook. The key rating challenges of the Republic by Moody's are the high stock of public and private debt, the very high level of non-performing loans coupled with gradually improvement of asset quality as well as the small and relatively undiversified economy.

Regarding the rationale of the rating action executed by Standard & Poor's[17], the upgrade of the Republic, based on the CRA, was attributed to the country's stronger than expected economic growth and fiscal progress allowing a gradual reduction in general government

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[15] Fitch Rating Action report in October 20, 2017.
[16] Moody's Press Release and Rating Action Report in July 28 and in November 24, 2017 respectively.
[17] Standard & Poor's Rating Action Report in September 15, 2017.

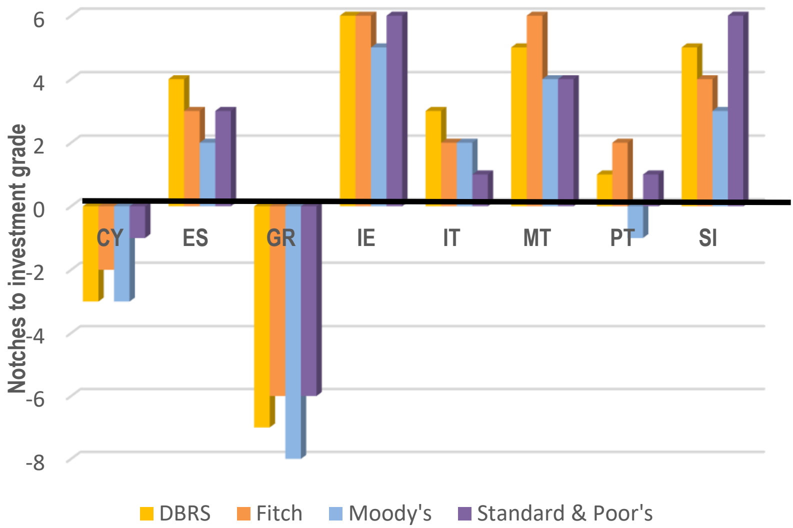
and private debt and supporting the banking sector's efforts towards the reduction of non-performing loans. Standard & Poor's underlined as the main weaknesses of the Republic, two of the five key rating factors of credit rating framework, namely external assessment and fiscal assessment (debt burden).

The key drivers for the upgrade of Cyprus' government bond in the near future, based on CRAs latest rating review in 2017, could result from continued ability of the Government to sustain the expectations of growth at current levels for the next years, from further reduction in the debt-to-GDP ratio and the stock of bank non-performing loans.

The historical credit ratings of the Republic of Cyprus during the period 1989-2017 are presented in Table 12 while the sovereign rating review calendar by CRAs for 2017 is presented in Figure 2 in the Appendix.

Figure 35 below, illustrates where did Cyprus stand in long-term rating scale compared to selected Eurozone States at end 2017. The horizontal axis of zero illustrates the investment grade line while the vertical axis shows the number of notches to investment grade.

Figure 35: Government Bond rating in long-term local currency of the Republic of Cyprus and selected Eurozone States[18] as at the end of 2017



(Source: Bloomberg)

[18] The abbreviations in the Figure are interpreted as following: CY=Cyprus, ES=Spain, GR=Greece, IE=Ireland, IT=Italy, MT=Malta, PT=Portugal and SI=Slovenia.

IX. Public Debt Management Office Action Plan

In September 2015, a five –year action plan 2015 (Dec.) – 2020 (Dec.) was approved by the Council of Ministers covering both the internal re-organisation and the IT infrastructure of the PDMO as well as the establishment of a market intelligence function.

Although, a number of actions within the said action plan have been completed, many of them are ongoing and have to be updated, reviewed and strengthen when needed.

The main actions implemented/continued or updated by the PDMO during 2017 are the following:

i. Continuation of the operation of Debt Management Committee: The said Committee with a narrow and larger composition has continued its meetings during the previous year discussing various issues such as cash management policy, fiscal and financial developments and prospects, debt sustainability analysis, investors presentation and in general the implementation of the debt management strategy;

ii. Continuation of an appropriate risk & control environment: The PDMO has continued to implement stricter procedures to follow throughout the transactions. Further to the adoption of audit checklists on the transactions and segregation of duties in order to minimise the operational risks for each function, the PDMO proceeded with the writing of an internal control procedures manual underscoring the PDMO policy regarding the recording and updating of the procedures governing its operations. The said manual was completed during 2017 and submitted to the Commissioner of Internal Audit of the Republic of Cyprus to provide relevant advice.

This action is ongoing and it is expected to be finalised in 2018;

iii. Risk management – operational risk: The PDMO has continued to update the database of operational risk incidents other than the one related to execution of transactions. It is noted that this action is also ongoing and it is updated and reviewed on a regular basis;

iv. Contacts started with the market group of international investment banks: The appointment of seven international banks by the Republic of Cyprus has already be done under the PDML 2012-2016 which is expected to increase the efficiency of the secondary market for government bonds of the Republic of Cyprus and enhance market intelligence on investor behavior.

v. Investor' Relations Function: The PDMO has continued to undertake a number of interrelated activities in order to keep investors apprised on a timely basis. During 2017, these activities concern the organisation of roadshows in foreign financial centres, teleconferences, physical meetings with investors in Cyprus, production and distribution of marketing information, maintenance and enrichment of investors database and investor list with contact details.

vi. IT Strategy: The implementation process of the CS-DRMS software which has started in October 2016, was completed by the end of 2017. The recording of the various debt instruments and transactions as well as the debt data validation in the said system, have been performed by a dedicated team comprising of officers from the PDMO and the Treasury of the Republic with the technical support of the IT Department. It is worth-noting, that the PDMO represented the Republic of Cyprus which has been selected to take part among other few countries on a user acceptance testing workshop in India in November 2017 in order to assess and ensure that the new public debt management system, namely 'Meridian' is suitable for purpose. The said system which will replace the current debt management system CS-DRMS, incorporates advanced and improved functionalities in order to address debt management requirements in a better way. According to an announcement of the Common Wealth Secretariat, the new system is expected to be released in the last quarter of 2018 to all countries which use the CS-DRMS.

Further to the above actions, it is important to underline that during 2017 the officers of the PDMO have participated in a number of seminars, conferences, meetings of the Economic and Financial Committee Sub-Committee on EU sovereign debt markets (ESDM) and other events both in Cyprus and abroad. Table 13 in Appendix illustrates the said participations in more detail.

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Appendix

List of Tables, Figures and Announcements

Table 1: Liability management transactions: EMTNs buybacks details in 2017
Table 2: Matured securities (1/1/2017-31/12/2017)
Table 3: Loan amortisations by creditor (1/1/2017-31/12/2017)
Figure 1: Impact of liability management transactions on debt maturity profile at the end of 2017
Table 4: Historical evolution of gross general government debt in 1995-2017
Table 5: Outstanding Central Government debt (in details) at the end of 2017
Table 6: Outstanding Central Government debt as at the end of 2017
Table 7: Government debt by instrument and lender at the end of 2017
Table 8: Investments of the Social Security Fund with the central government as at the end of 2017
Table 9: Historical debt servicing in 2010-2016
Announcement 1: Interest rate reduction on 2018 retail bonds series
Table 10: Stock of outstanding government guarantees as at the end of 2017
Table 11: Central government liquid assets and cash/debt ratios in 2012-2017
Table 12: Historical credit ratings 1989-2017 (Long term-short term rating)
Figure 2: Sovereign Rating Review Calendar for the Republic of Cyprus in 2018
Table 13: Participation of PDMO officers to seminars, EU Committees and other events in 2017

Table 1: Liability management transactions: EMTNs buybacks details in 2017

Bond characteristics		Maturity date	Buyback Nominal amount	Buyback price	Cash amount paid
ISIN code	Interest rate (in %)		EUR mn	Per 100	EUR
XS1081101807	4,75%	25/6/2019	367.36	109.10	400,84
XS0483954144	4,625%	3/2/2020	101,99	110,55	112,75
XS1064662890	6,50%	2/5/2020	76,35	116,00	88,57
			545.70		**602,16**

(Source: PDMO)

Table 2: Matured securities (1/1/2017 to 31/12/2017)

I. Domestic market

A. Treasury Bills

Issue date	Maturity (in weeks)	Weighted average yield (in %)	Maturity date	ISIN	Nominal amount in EUR mn
7/10/2016	13	0,47	9/1/2017	CY0146800814	100
4/11/2016	13	0,31	3/2/2017	CY0146870817	100
2/12/2016	13	0,17	3/3/2017	CY0146950817	100
9/1/2017	13	0,02	7/4/2017	CY0147040816	100
3/2/2017	13	-0,01	5/5/2017	CY0147090811	100
3/3/2017	13	-0,04	2/6/2017	CY0147120816	100
7/4/2017	13	-0,08	7/7/2017	CY0147150813	100
5/5/2017	13	-0,04	4/8/2017	CY0147210815	100
2/6/2017	13	-0,05	1/9/2017	CY0147230813	100
7/7/2017	13	-0,05	6/10/2017	CY0147280818	100
4/8/2017	13	-0,04	3/11/2017	CY0147330811	100
1/9/2017	13	-0,04	1/12/2017	CY0147380816	100
6/10/2017	12	-0,06	29/12/2017	CY0147420810	100
					1300

B. Domestic Bonds

Issue date	Maturity (in years)	Coupon rate (in %)	Maturity date	ISIN	Nominal amount in EUR mn
4/1/2007	10	4,5	4/1/2017	CY0140160819	85
15/2/2007	10	4,5	15/2/2017	CY0140190816	82
2/4/2007	10	4,5	2/4/2017	CY0140330818	85
15/4/2002	15	5,6	15/4/2017	CY0048900811	13
28/9/2007	10	4,5	28/9/2017	CY0140500816	18
					283

C. Repayments of Saving Certificates/Retail Bonds

	Nominal amount in EUR mn
Saving certificates	13
Retail bonds	5
	18

II. Foreign market
A. Euro Commercial Papers

	Nominal amount in EUR mn
	0

B. Euro Medium Term Notes[1/]

	Nominal amount in EUR mn
	0

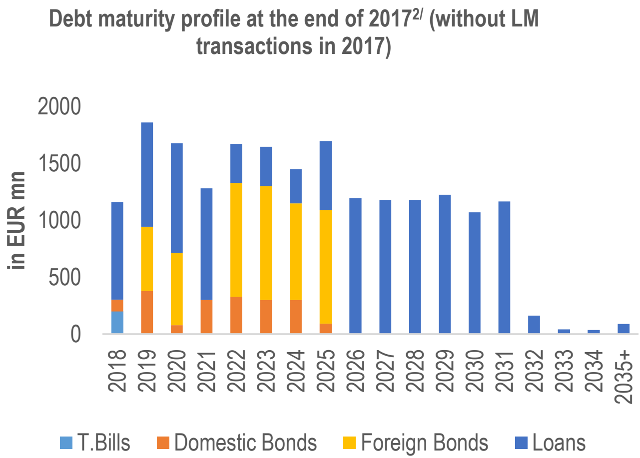
1/= Debt reduction due to buyback transactions are not included.

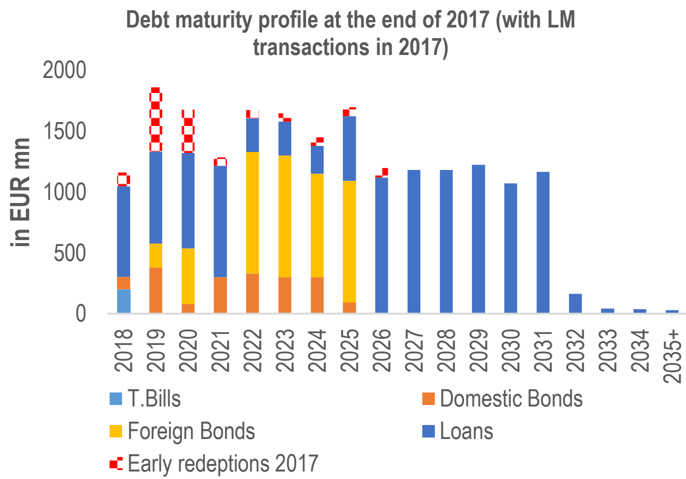
Table 3: Loan amortisations[1/] by creditor (1/1/2017 to 31/12/2017)

	Remaining amount in EUR mn	Principal payments in EUR mn
Central Bank of Cyprus	510,9	673,7
International Monetary Fund	676,4	271,1
European Investment Bank	923,8	33,7
Cyprus Cooperative Bank	347,3	23,1
Council of Europe Development Bank	236,0	22,5
Government of France	0,0	0,1
		1024,2

1/= Early repayments transactions are included

Figure 1: Impact of liability management (LM) transactions on debt[1/] maturity profile at the end of 2017





(Source: PDMO)

1/ = Excludes debt for EFSF loans
2/ = This debt maturity profile indicates how the profile would be without LM transactions done in 2017

Table 4: Historical evolution of gross general government debt[1/] in 1995-2017

Year	Consolidated gross general government debt (in EUR mn)	Consolidated gross general government debt (% of GDP)
1995	3589,5	46,8
1996	3896,2	48,8
1997	4478,1	53,5
1998	4981,6	55,0
1999	5416,8	56,7
2000	5813,5	54,9
2001	6452,7	56,5
2002	7096,3	59,7
2003	8108,5	63,1
2004	8882,6	64,1
2005	9299,8	62,7
2006	9330,9	58,3
2007	9307,3	53,1
2008	8462,0	44,5
2009	9946,9	53,3
2010	10862,0	56,3
2011	12966,2	65,7
2012	15526,7	79,7
2013	18614,7	102,6
2014	18922,1	107,5
2015	19072,4	107,5
2016	19417,5	106,6
2017	18724,8	97,5

1/ = Since 2010 figures include also liabilities due to the issuance of euro coins

Table 5: Outstanding Central Government[1/] debt as at the end of 2017

A. TREASURY BILLS

Issue date	Maturity (in weeks)	Weighted average yield (in %)	Maturity date	Currency of issue	ISIN code	Discount value in EUR mn
3/11/2017	13	-0.07	2/2/2018	EUR	CY0147460816	100,0
1/12/2017	13	-0,10	2/3/2018	EUR	CY0147520817	100,0
						200,0

B. DOMESTIC BONDS

Issue date	Maturity (in years)	Coupon rate (in%)	Maturity date	Currency of issue	ISIN code	Nominal value in EUR mn
18/1/2016	2	2,00	18/1/2018	EUR	CY0146220815	75,0
29/1/2003	15	5,10	29/1/2018	EUR	CY0048440818	13,7
23/4/2003	15	4,60	23/4/2018	EUR	CY0048610816	5,1
23/10/2003	15	4,60	23/10/2018	EUR	CY0048870816	0,8
26/2/2004	15	4,60	26/2/2019	EUR	CY0049070812	1,6
24/6/2004	15	6,10	24/6/2019	EUR	CY0049250810	7,2
1/7/2013	6	4,50	1/7/2019	EUR	CY0143820815	367,7
20/4/2005	15	6,10	20/4/2020	EUR	CY0049570811	11,1
9/6/2005	15	5,35	9/6/2020	EUR	CY0049630813	8,4
1/7/2013	7	4,75	1/7/2020	EUR	CY0143830814	0,0
9/6/2011	10	6,00	9/6/2021	EUR	CY0141990818	43,6
1/7/2013	8	5,00	1/7/2021	EUR	CY0143790810	1,1
25/8/2011	10	6,50	25/8/2021	EUR	CY0142120811	23,1
30/11/2015	5	2,00	29/1/2021	EUR	CY0146070814	31,4
1/7/2013	9	5,25	1/7/2022	EUR	CY0143800817	52,7
1/7/2013	10	6,00	1/7/2023	EUR	CY0143810816	3,2
18/1/2016	7	3,25	18/1/2023	EUR	CY0146250812	221,9
24/1/2017	7	3,25	24/1/2024	EUR	CY0147060814	300,0
18/12/2015	10	4.00	18/12/2025	EUR	CY0146120817	92,0
						1259,6

C. RETAIL/SPECIAL RETAIL BONDS-SAVING CERTIFICATES

Coupon rate	(in %)	Maturity year	Currency of issue	Nominal value in EUR mn
Retail Bonds	2,75-5,75	2020	EUR	59,1
Retail Bonds	2,50-5,50	2021	EUR	148,6
Retail Bonds	2,50-3,25	2021	EUR	52,6
Retail Bonds	2,50-3,25	2022	EUR	276,2
Retail Bonds	2,50-3,25	2023	EUR	75,8
Special Bonds	0,75	2024	EUR	0,8
Saving certificates	3,85	perpetual	EUR	11,4
				624,5

TOTAL DOMESTIC SECURITIES AS AT 31/12/2017 [EUR MN] ***2084,1***

D. EURO COMMERCIAL PAPERS

Issue date	Maturity (in months)	Yield (in %)	Maturity date	Currency of issue	ISIN code	Discount value in EUR mn
						0,0
						0,0

E. EURO MEDIUM TERM NOTES (EMTN)

Issue date	Maturity (in years)	Coupon rate (in%)	Maturity date	Currency of issue	ISIN code	Nominal value in EUR mn
25/6/2014	5	4,750	25/6/2019	EUR	XS1081101807	199
3/2/2010	10	4,625	3/2/2020	EUR	XS0483954144	454
2/5/2014	6	6,500	2/5/2020	EUR	XS1064662890	4
6/5/2015	7	3,875	6/5/2022	EUR	XS1227247191	1000
26/7/2016	7	3,750	26/7/2023	EUR	XS1457553367	1000
27/6/2017	7	2,750	27/6/2024	EUR	XS1637276848	850
4/11/2015	10	4,250	4/11/2025	EUR	XS1314321941	1000
						4506,6

TOTAL FOREIGN SECURITIES AS AT 31/12/2017 [EUR MN] **4506,6**

F. DOMESTIC LOANS

Creditor	Issue year	Interest (in %)(2)	Maturity year	Currency of issue	Remaining maturity (in years)	Balance (in EUR mn)
Central Bank of Cyprus	2002	3,00	2032	EUR	14,5	510,9
Cyprus Coop. Bank	2007	6mE+1,50	2032	EUR	14,5	347,3
						858,2

G. FOREIGN LOANS

Creditor (3)	Issue year (6)	Interest rate (in %)	Maturity year	Currency of issue/reserve asset	Remaining maturity (in years)	Balance (in EUR mn)
CEDB	2004	6mE+0,28	2018	EUR	0,9	2,4
EIB	2004	5,35	2019	EUR	1,9	15,9
Govern. of the RF	2011	2,50	2021	EUR	3,7	2500,0
EIB	2004	1	2022	EUR	4,9	0,2
EIB	2004	1	2022	EUR	4,9	0,6
CEDB	2004	6mE+0,30	2023	EUR	6	8,7
CEDB	2003	6mE+0,30	2023	EUR	6	20,0
EIB	2004	1	2025	EUR	7,5	1,0
CEDB	2010	3mE+0,60	2025	EUR	7,9	38,0
IMF(4)	2013	BLR+1,00	2026	SDR	8,1	676,4
EIB	2004	1	2026	EUR	8,6	0,4
EIB	2014	3mE+0,70	2026	EUR	8,8	20,0
CEDB	2006	6mE+0,15	2026	EUR	9	51,4
CEDB	2007	6mE+0,09	2027	EUR	9,5	11,0
CEDB	2008	3,7	2028	EUR	11	32,3
EIB	2004	4,45	2029	EUR	11,5	31,0
CEDB	2017	6mE+0,217	2029	EUR	8,8	21,2
EIB	2009	3mE+0,48	2029	EUR	12	12,2
CEDB	2009	3mE+0,48	2029	EUR	12	7,5
CEDB	2014	1,46	2029	EUR	12	25,0
CEDB	2010	3mE+0,55	2030	EUR	12,6	4,7
ESM	2013	BLR+0,10	2031	EUR	13,8	6300,0
CEDB	2017	1,08	2032	EUR	14,5	16,0
CEDB	2013	6mE+0,81	2033	EUR	16	8,0
EIB	2004	VSFR	2033	EUR	16	138,6
EIB	2005	VSFR	2035	EUR	18	66,3
EIB	2007	6mE+0,06	2035	EUR	18	75,3
EIB	2004	VSFR	2035	EUR	18	44,3
EIB	2017	1,514	2037	EUR	19,5	40,0
EIB	2017	1,563	2037	EUR	19,7	14,0

EIB	2012	12mE+1,37	2037	EUR	19,6	200,0
EIB	2017	1,634	2037	EUR	19,6	30,0
EIB	2011	12mE+0,28	2038	EUR	20,5	56,0
EIB	2011	12mE+0,50	2039	EUR	21.9	53,0
EIB	2011	6mE+0,44	2040	EUR	23	76,0
EIB	2015	1,766	2040	EUR	23	40,0
EFSF(5)	2011			EUR		228,9
						10866,3

TOTAL LOANS AS AT 31/12/2017 [EUR MN] ***11724,5***

TOTAL DEBT OF CENTRAL GOVERNMENT AS AT 31/12/2017 [EUR MN] ***18315,3***

Notes:
(1) Definition: Debt of the budgetary central government (BCG) excluding debt of Social Security Investments,
state-owned entreprises categorised within the central government and the debt of local authorities.
BCG is approximately 98% of the general government debt (as at 31/12/2017)
(2) E= Euribor rate; BLR=Basic Lending Rate; VSFR = other variable interest rate;m=months
(3)EIB=European Investment Bank, CEDB= Council of Europe Development Bank, EFSF=European Financial Stability Facility,
RF=Russian Federation, IMF=International Monetary Fund,
ESM=European Stability Mechanism
(4) Loan balance in EUR using the relevant exchange rate as at 29/12/2017
(5) Debt issued by the EFSF for Greece, Ireland and Portugal
(6) It refers to the first disbursement
(7) Excluding liabilities due to the issuance of Euro coin
(8) There may be slight discrepancies between the totals shown and the sum of constituent items because of rounding.

Table 6: Outstanding Central Government debt as at the end of 2017

	Foreign-law securities		Domestic-law securities		IMF - ESM loans		Other loans		Total
2018	0		303		0		738		1048
2019	199		379		0		749		1333
2020	458		79		37		743		1323
2021	0		300		164		747		1217
2022	1000		329		149		122		1606
2023	1000		301		149		122		1578
2024	850		301		105		118		1379
2025	1000		92		411		116		1624
2026	0		0		1010		111		1120
2027	0		0		1000		177		1181
2028	0		0		1000		177		1181
2029	0		0		1050		171		1225
2030	0		0		900		167		1071
2031	0		0		1000		163		1167
2032	0		0		0		165		164
2033	0		0		0		45		42
2034	0		0		0		41		37
2035+	0		0		0		156		91
TOTAL	4506		2084		6976		4827		18387

Notes

1/ = Preliminary data
2/= Excluding debt for EFSF Loans
3/= Foreign currency debt valued according to exchange rate as at 29/12/2017
4/ = Excluding debt to Social Security Fund and liabilities due to the issuance of Euro coins
5/ = A flat redemption profile is assumed for loans granted to local authorities and State-Owed Enterprises.
6/= There may be slight discrepancies between the totals shown and the sum of constituent items because of rounding.

Table 7: Government debt[1/] by instrument and lender at the end of 2017 (in EUR mn)

A. Domestic Debt			**3340,1**
I. Long-term debt		**3140,1**	
1. Domestic bonds	**1259,6**		
- Monetary Financial Institutions	1058,4		
- Private Sector	201,2		
2. Retail securities	**624,5**		
3. Loans	**1127,4**		
- Central Bank of Cyprus	510,9		
- Local Authorities loans	222,2		
- Cyprus Cooperative Bank[2/]	347,3		
- Semi-government organisations loans	47,0		
4. Liabilities to issuance of euro coins	**128,6**		
II. Short-term debt		**200,0**	
1. Treasury Bills	**200,0**		
- Monetary Financial Institutions	198,2		
- Private Sector	1,8		
B. Foreign debt		**15384,7**	**15384,7**
I. Long-term debt			
1. Long term loans	**10649,1**		
-ESM and IMF[3/]	6976,4		
-Bilateral governments	2500,0		
-EIB and CEDB	1159,8		
2. Euro Medium Term Notes	**4506,6**		
3. EFSF loans	**229,0**		
II. Short-term debt		**0,0**	
Euro Commercial Papers	0,0		
C. Gross General Government Debt[4/]			**18724,8**

Note:
1/ = Preliminary data
2/ = Loans provided by the CCB for school committees.
3/ = Foreign currency debt valued according to exchange rates as at 29/12/2017.
4/ = Debt is reported in consolidated form and therefore any obligations among subsectors of the general government are omitted.

Table 8: Investments[1/] of the Social Security Fund with the central government as at the end of 2017

		Amount in EUR mn
1	**Deposits with the Central Government**	**7797,6**
	Social Insurance Fund	7119,7
	Unemployment Benefits Account	12,2
	Termination of Employment Fund	389,6
	Central Holiday Fund	70,7
	Insolvency Fund	205,4
2	**Investment in Cyprus EMTN bond 4,625% mat. 3/2/2020**	204,1
3	**Investment in Cyprus Domestic bond 6,00% mat. 9/6/2021**	10.0
		8011,7

Note

1/ = Investments in the form of deposits in financial institutions of EUR 84 are not included.

Table 9: Historical debt servicing in 2010-2016

	2010	2011	2012	2013	2014	2015	2016
				EUR mn			
Interest payments (IP)	380	402	564	696	570	646	582
General Government Debt (GGD)	10862	12966	15527	18615	18922	19072	19418
Tax revenue (TR)	4574	4686	4627	4349	4405	4362	4488
Total government revenue (TGR)	7203	7233	7085	6664	7008	6970	7081
				in %			
Interest payments to GDP	2,0	2,0	2,9	3,8	3,2	3,6	3,2
Interest payments to GGD	3,5	3,1	3,6	3,7	3,0	3,4	3,0
Interest payments to TR	8,3	8,6	12,2	16,0	12,9	14,8	13,0
Interest payments to TGR	5,3	5,6	8,0	10,4	8,1	9,3	8,2

Note:

1/ =Interest payments exclude intragovernmental interest payments to the Social Security Fund

Announcement 1

REPUBLIC OF CYPRUS
MINISTRY OF FINANCE
PUBLIC DEBT MANAGEMENT OFFICE

ANNOUNCEMENT
SIX YEAR GOVERMENT BONDS FOR NATURAL PERSONS
INTEREST RATE
REDUCTION 2018 SERIES

The Public Debt Management Office announces the reduction of interest rates under the terms of issuance on six-year government bonds for natural persons.

The aforementioned reduction on interest rates will enter into force on the issuance of the 1st Series of 2018 with value date on the 2nd of January 2018. Applications can be submitted between the 1st to the 20nd of December 2017. More specifically the reduction relates to the coupon paid to investors over the holding period of the bond. The table below exhibits the reduced coupon level of the six-year government bond as of the 1st series of 2018.

Holding period of the bond	**Annual coupon per holding period**
Up to 24 months	2,25%
Over 24 months and up to 48 months	2,50%
Over 48 months and up to 60 months	2,75%
Over 60 months and up to 72 months	3,00%

Bonds which were already issued will remain unaffected from all the above changes.

Additionally, it is noted that for the upcoming series of 2017 (11th and 12th series) with value dates on the 1st November and the 1st December 2017 respectively, the existing interest rates will apply. Applications for these series, can be submitted between the 2-20 October 2017 and 1-20 November 2017, respectively.

Further information can be found at: Debt Management Office (PDMO) Website: http://www.mof.gov.cy/pdmo

PUBLIC DEBT MANAGEMENT OFFICE

MINISTRY OF FINANCE

6 October 2017

Disclaimer:

IMPORTANT CLARIFICATION: This document does not constitute or form part of, and should not be construed as, an offer to sell or issue or the solicitation of an offer to buy or acquire securities of the Republic of Cyprus (Issuer) in any jurisdiction or an inducement to enter into investment activity in any jurisdiction. Neither this document nor any part thereof, nor the fact of its publication, shall form the basis of, or be relied on in connection with, any contract or commitment or investment decision whatsoever. Interested investors are encouraged to perform an independent review of the financial situation of the Issuer and the main characteristics/risks of the bonds. For this purpose, advice may be sought from a registered/licensed expert (eg. Investment Firms) as to whether this investment is suitable for them before taking any final decision as regards the Bonds.

Table 10: Stock of outstanding government guarantees as at the end of 2017

No	Principal debtors	Loan contracts	Stock of outstanding guarantees
		in number	EUR mn
1	**Corporate**	**42**	**329.364.323**
	Other Companies	1	10.508
	SMEs	8	3.946.849
	Banks and Other Credit Institutions	33	325.406.967
2	**Entities with Public Interest**	**70**	**1.001.875.970**
	Other Entities with Public Interest	1	23.896.501
	Public Organizations[1/]	13	355.090.467
	Sewerage Boards	56	622.889.002
3	**Local Authorities[2/]**	**152**	**300.233.080**
	Municipalities	103	293.977.822
	Community Boards	49	6.255.258
4	**Individuals / Retail**	**3773**	**140.299.635**
	Agricultural	1	31.713
	Small Business	1124	37.596.428
	Housing	2627	101.589.403
	Individuals / retail	21	1.082.092
5	**Total outstanding GG for loans excluding the issue of debt instruments (1+2+3+4)**	**4037**	1.771.773.008
6	**Issues of debt instruments**	**1**	**162.089.222**
	European Financial Stability Facility (EFSF)	1	162.089.222
7	**Grand Total outstanding GG (5+6)**	**4038**	**1.933.862.230**

Source: Treasury

(PDMO calculations)

1/ = An amount of EUR 13 mn concerns loans granted to Cyprus Theatrical Organisation and Cyprus Sport Organisation which are included in the public debt

2/ = These entities are included in the General Government sector and therefore their loans are part of the General Government Debt

Table 11: Central government liquid assets and cash/debt ratios in 2012-2017

Date	Cash at the CBC	Cash at MFIs	Total	Debt that falls due	Cash/debt[2]
31.12.2012	148,8	69,5	218,3	3202,0	6,8
31.12.2013	760,9	6,5	767,4	1748,0	43,9
31.12.2014	1015,9	6,5	1022,4	1978,0	51,7
31.12.2015	666,8	6,5	673,3	1131,0	59,5
31.12.2016	564,2	430,0	994,2	748,0	132,9
31.12.2017	284,0	380,0	664,0	1048,0	63,4

1/= The amount of debt that falls due within next year based on the statistical information at the end of the reference year
2/= % of cash over debt that falls due within one year

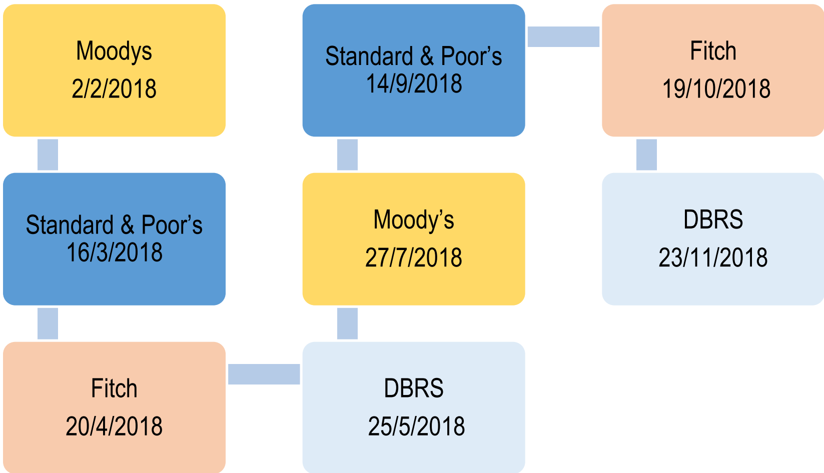
Table 12: Historical credit ratings[1/] 1989 – 2017 (Long term-short term rating)

Fitch		Moody's		S&P		DBRS	
BB	20/10/2017	Ba3	28/7/2017	BB+	17/3/2017	BB(L)	2/6/2017
BB-	21/10/2016	B1	11/11/2016	BB	16/9/2016	B	2/12/2016
B+	23/10/2015	B1	13/11/2015	BB-	25/9/2015	B	4/12/2015
B-	25/4/2014	B3	14/11/2014	B+	24/10/2014	BL	27/6/2014
CCC	5/7/2013	Caa3	10/1/2013	B	25/4/2014	CCC	12/7/2013
RD	28/6/2013	B3	8/10/2012	B-	29/11/2013		
CCC	3/6/2013	Ba3	13/6/2012	CCC+	3/7/2013		
B	25/1/2013	Ba1	12/3/2012	SD	28/6/2013		
BB-	21/11/2012	Ba3	4/11/2011	CCC	21/3/2013		
BB+	25/6/2012	Baa1	27/7/2011	CCC+	20/12/2012		
BBB-	27/1/2012	A2	24/2/2011	B	17/10/2012		
BBB	10/8/2011	Aa3	3/1/2008	BB	1/8/2012		
A-	31/5/2011	A1	10/7/2007	BB+	13/1/2012		
AA-	12/7/2007	A2	19/7/1999	BBB	27/10/2011		
AA	4/2/2002			BBB+	29/7/2011		
				A-	30/3/2011		
				A	16/11/2010		
				A+	24/4/2008		
				A	1/12/2004		
				A+	12/8/2003		
				AA-	3/12/1999		
				AA	9/11/1998		

				AA+	16/7/1996		
Short term rating							
B	3/6/2013	NP	13/3/2012	B	29/11/2013		
B	26/3/2013	P-3	4/11/2011	C	20/12/2012	R-4	12/4/2015
B	25/6/2012	P-2	27/7/2011	B	13/1/2012	R-5	12/7/2013
F3	27/1/2012	P-1	16/5/2011	A-3	5/12/2011		
F3	16/12/2011	P-1	6/11/1989	A-3	27/10/2011		
F3	10/8/2011			A-2	12/8/2011		
F1	31/5/2011			A-2	30/3/2011		
F1+	12/7/2007			A-1	12/8/2003		
F1	4/2/2002			A-1+	16/7/1996		

1/ = A credit upgrade/downgrade/affirmation is indicated in green/red/black color.

Figure 2: Sovereign Rating Review Calendar for the Republic of Cyprus in 2018



Note: CRAs are able to announce other evaluation dates outside the above official planned evaluations if required by economic conditions. They have not the obligation to issue a credit assessment decision at all of the above evaluation dates.

Table 13: Participation of PDMO officers to seminars, EU committees and other events during the year 2017

Description	March	April	May	June	July	Sept.	October	Nov.	Dec.
EFS Sub-Committee on EU Sovereign debt markets (Belgium)	Brussels (1/3)			Brussels (14/6)				Brussels (8/11)	
National Asset Liability Management Europe conference (United Kingdom)	London (22-24/3)								
Cyprus Institute of Internal Auditor (CIIA) seminar on (a) Credit risk-effective control and management, (b) Continuous auditing vs continuous monitoring	(a) Nicosia (15/3)	(b_1) Nicosia (3/4)	(b_2) Nicosia (25/5)						
IMF meetings (USA)		Washington (20-23/4)					Washington (4-11/10)		
USA investors roadshow		Philadelphia, New York, Boston (24-26/4)							
European Bank for Reconstruction and Development meeting and Business Forum			Nicosia (9-11/5)						
European investors roadshow (France-Switzerland-Germany) Note: The Director of the PDMO together with other Directors of the MoF participated in an another roadshow in London and Frankfurt.			Paris/Zurich/Munich (22-24/5)						
Commonwealth of Independent States and Baltic Bond Congress (Cyprus)				Limassol (8-9/6)					

Description	March	April	May	June	July	Sept.	October	Nov.	Dec.
ESM seminar on Debt sustainability analysis framework (Cyprus)				Nicosia (29-30/6)					
Seminar for General data protection regulation 2016/679					Maastricht (3-7/7)	Brussels (18-22/9)			Maastricht (18-20/12)
Goldman Sachs Interest Rate Derivatives Intensive Course (United Kingdom)						London (10-14/9)	London (16-19/10)		
ESM Shareholdings' Day								Luxembourg (8-9/11)	
11th UNCTAD Debt management Conference in Switzerland								Geneva (13-15/11)	
Commonwealth pilot program for a new Public Debt management system (Republic of India)								Pune (13-24/11)	

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