



Macroeconomic Environment:

- In the 2nd quarter of 2014, GDP (in seasonally adjusted terms) contracted by -2.5% compared with -3.9% in the 1st quarter of 2014 on an annual basis. The 4th annual review of the Macroeconomic Adjustment Programme includes the assumption that the annual contraction of the economy for 2014 will be 4.2%.
- The business operating environment remains constrained, given that lending to non-financial corporations is subdued and interest rates are still relative to economic conditions high. We maintain our view that growth in 2014 will remain negative, not exceeding 3%, and we assume a rebound in 2015 with a gradual restoration of lending at affordable rates.
- Exports of goods decreased by 6.2% in January-July 2014 compared to the corresponding period in 2013.
- In January-August 2014 tourist arrivals increased by 5.9% compared to the corresponding period in 2013. An increase of 1.3% was recorded in arrivals from the United Kingdom, a 6.5% decrease in arrivals from Greece and a 16.9% increase in arrivals from Russia.
- Inflation, as measured by the HICP, stood at 0.8% in August 2014 compared to 0.9% in July 2014 and for 2014 so far it stands at -0.3%.
- Labour Force Survey (LFS) unemployment, in monthly seasonally adjusted figures, decreased from 16.1% in July 2013 to 14.9% in July 2014 (15% in June 2014). The most affected segment of the population is youth. Particularly worrying is also the rapid increase in long-term unemployed.
- Compensation per employee in the 1st half of 2014 declined by around 5.1% compared to the 1st half of 2013, contributing to a decline of nominal unit labour costs and improving cost competitiveness further.
- The upcoming banking stress tests in October and the resolution of the issue of the foreclosure legislation will be the major drivers for the bond market yields in the coming months. External factors (the Ukrainian and Middle East crises) are expected to have an effect too.

Banking Sector:

- The authorities continue to focus in addressing rising NPL's through the introduction of various measures that will have an impact over the medium term such as the implementation of an arrears management directive, adopting a functioning foreclosure law while protecting vulnerable groups and modernizing the insolvency framework. We expect to have the relevant regulatory framework in place by the end of the year.
- Bank of Cyprus has completed successfully at end of August 2014 a capital increase exercise, and is continuing with the implementation of its restructuring plan.

- Deposits of domestic residents held with MFIs (private sector) exhibited a contraction presenting an annual decline of 3.1% in July 2014 vis-à-vis July 2013. From March 2014, a deceleration in the contraction of deposits was observed.
- Large banks (BoC, Coops, Hellenic Bank, RCB) are participating in the on-going Comprehensive Asset Quality Review and stress test of the ECB, due to be completed by the end of Oct-2014.
- The authorities intend to adapt the Road map in examining the external restrictive measures, aiming towards their gradual relaxation and eventual abolition, while ensuring consistency with financial stability.

Cooperative Credit Institutions:

- Publication of the consolidated audited accounts for 2013.
(<http://www.coopbank.com.cy/content/The%20Bank/COOPconsolFS2013.pdf>)
- The Cooperative Central Bank submitted in September 2014 the second quarterly report describing the progress with the implementation of the restructuring plan.
- Continuing enhancement of the operational capacity of the central NPL Management Division that was set up in the Cooperative Central Bank to handle the sector's most problematic clients and all terminated accounts. The main pillars of the Division is the Arrears Management & Restructuring Unit, the Debt Recovery Unit and the Property Management Unit.

Fiscal Developments:

- Developments in public finances continue to exceed expectations.
- General government budget balance (GGBB) was in surplus during the first 8 (eight) months of 2014, of the order of €126 mn (0.8% of GDP) compared to a deficit of €263 mn (-1.7% of GDP) during the same period of the previous year.
- General government primary balance (GGPB) was in surplus during the first 8 (eight) months of 2014, of the order of €457 mn (2.9% of GDP) compared to a surplus of €135 mn (0.8% of GDP) during the same period of the previous year.
- Total revenue exhibited a positive rate of growth of about 6.7%, reaching €4,449 mn during the first 8 (eight) months of 2014, compared to €4,170 mn during the same period of the year before.
- Total expenditure exhibited a negative rate of growth of about 2.5%, reaching €4,323 mn during the first 8 (eight) months of 2014, compared to €4,433 mn during the same period of the year before.
- In accordance with the macroeconomic scenario agreed during the 5th review, the budget balance is estimated to exhibit an improvement with the deficit falling to 4.7% of GDP in 2014 compared to a deficit of 5.4% the year before.

Public debt and financing:

- The General Government Debt at the end of September 2014 (preliminary data) stood at €18.4 bln. This indicator has not changed since December 2013.
- Short term yields have continued to drop with three month primary market yields dropping to 3.9% in August (no new issuances took place in September).
- Long term bond yields exhibited a significant drop in August and early September as the effects of the ECB's monetary decisions were taken in by the markets but have risen again following the general trend in the European periphery. Yields remain below the 5% mark.
- The 6th Programme tranche was not disbursed in September 2014 (€433 mln) due to non-compliance in introducing legislation on foreclosure as demanded by the Programme partners.

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Links:

Macroeconomic monitor:

[http://www.mof.gov.cy/mof/mof.nsf/All/8C7C516205417C67C2257D5B0025E398/\\$file/Macro%20Monitor%20August%202014.pdf?OpenElement](http://www.mof.gov.cy/mof/mof.nsf/All/8C7C516205417C67C2257D5B0025E398/$file/Macro%20Monitor%20August%202014.pdf?OpenElement)

Public Debt Quarterly Bulletin:

[http://www.mof.gov.cy/mof/pdmo/pdmo.nsf/All/F0C650FEBD5E4C11C225788D00208D2A/\\$file/CY%20Qrt%20Bulletin%20Q2_2014.pdf](http://www.mof.gov.cy/mof/pdmo/pdmo.nsf/All/F0C650FEBD5E4C11C225788D00208D2A/$file/CY%20Qrt%20Bulletin%20Q2_2014.pdf)

Roadmap on relaxation of capital controls:

[http://www.mof.gov.cy/mof/mof.nsf/All/3766C4D62B9EDE71C2257BC2002E22E9/\\$file/Roadmap%20PresentationLHM07%2008%202012ENG%20Compatibility%20Model.pdf](http://www.mof.gov.cy/mof/mof.nsf/All/3766C4D62B9EDE71C2257BC2002E22E9/$file/Roadmap%20PresentationLHM07%2008%202012ENG%20Compatibility%20Model.pdf)

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The information has been compiled and verified to the best of our knowledge. The possibility of a factual mistake can not, however, be excluded.