

# Cyprus

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## IN A NUTSHELL

- GDP growth recovered to 5.5%.
- Recovery and resilience facility expected to boost investment levels.
- House prices have continued to rise from the low post recession levels.
- Bank liquidity remains good.

## MACROECONOMIC OVERVIEW

The economy recovered swiftly, GDP increased by 5.5% to pre-pandemic levels, after dropping 5% in 2020. This was driven by all sectors including tourism, industry and construction. Unemployment dropped marginally to 7.5% from 7.6%. The harmonised index of consumer prices increased by 2.3% on average having accelerated in the second half of the year to an annualised rate of 3.9%. Cyprus will benefit from the EU's recovery and resilience facility and has already received pre-financing of EUR 157 mn in September 2021, following approval of the national recovery plan in July. The plan consists of EUR 1.2 bn, of which 41% funds green investments and 23% digital investments.

In the banking sector, non-performing loans continued to fall, the ratio to gross loans was 11.1% at year end.

The recovery in 2021 provided a significant increase in government revenue and drop in spending. The budget deficit narrowed to 1.7% of GDP from 5.8% in 2020, and the public debt to GDP ratio fell to 104% from 115% and remains on a downward trajectory.

Cyprus is affected by the Ukraine war and sanctions against Russia. Cyprus is a small and very open economy with a large services exports sector including tourism, shipping, and financial services. Russia was a significant tourism market for Cyprus and accounted for 20% of total arrivals in 2019, before the pandemic outbreak.

Cyprus' real GDP surprised for the upside, expanding by 6% in the first half of the year, and will likely exceed the European Commission's summer forecasts for 3.2% growth.

## HOUSING MARKET

Home ownership has been declining since the financial crisis of 2012-14 reflecting the deep recession, high non-performing loans, and tighter credit conditions. Ownership declined the most between 2013 and 2019, dropping by 6.1 pps to 67.9%. This is lower than the EU average of 69.8% and was the lowest among the peer group of southern European countries. In 2020 ownership rose to 68.6%.

New building construction, dropped from EUR 3.0 bn in 2008 to EUR 920 mn in 2014. Since then, it has to EUR 2.0 bn in 2018 and EUR 2.5 bn in 2019.

The construction sector started to recover in 2016. The share of the sector's value-added rose from 4.0% of GDP in 2015 to 6.3% in 2019 in nominal terms, dropped to 6.1% in 2020 and increased only marginally in 2021. In value terms gross output returned to about its 2019 level in 2021.

The recovery in the construction sector reflects the demand for housing and property prices. On a yearly basis, new sales peaked in 2007 at 21,245 but dropped by 82% by 2013. New sales rose steadily almost tripling (275%) by 2019 compared to 2013, but still less than half of the peak level. Sales dropped in 2020 and recovered in 2021 to their 2019 levels.

Prices, as measured by the Central Bank's residential property index, rose in 2017-21 by a cumulative 7.7% following a decline of 30.6% between 2008 and 2016. The increase in the period 2017-20 was driven by apartments (up 17.2% as opposed to houses which rose by 4.0%). Residential property price increases were greater in Limassol (up 14.0%) followed by Famagusta (up 7.9%), Larnaca (up 8.5%), Nicosia (up 3.8%) and Paphos (up 2.9%). In 2020, residential property prices increased by 1.5% on average, and in 2021 by 1.3%.

Regional differences reflect differences in the composition of demand. In Limassol there is higher demand from non-residents related to the city's international business orientation. There is a high proportion of vacation and second homes in the Larnaca, Paphos and Famagusta regions where prices have been more volatile in both the contraction and the recovery. Nicosia is the largest region by population and the country's capital and featured demand from locals, diplomats, and students.

The number of completed new dwellings in 2019 (latest available data) was 4,420 compared with 3,866 the year before and a peak of 18,195 in 2008. The total stock of dwellings at the end of 2019 was 460,000 having risen by 16.8% since 2008.

## MORTGAGE MARKET

### MARKET DYNAMICS

The mortgage market has been shrinking since the financial crisis of 2012-14, in absolute terms and relative to GDP. This follows years of restructuring and deleveraging in the banking sector. Total outstanding loans for house purchase at the end of 2021 were EUR 8.4 bn, 35.8% of GDP. This compares with EUR 12.7 bn, 65% of GDP in 2012. Loans for house purchase increased as a share of loans to residents (excluding the government) to 36% (from 24% in 2012) and as a share of all households loans to 72.8% (53.1% in 2012). This indicates a higher degree of deleveraging in the period in non-mortgage loans.

New mortgage loans have been rising since 2015. Total new mortgage loans reached EUR 1.3 bn in 2021 compared with EUR 947 mn in the previous year.

Excluding renegotiated amounts, net new mortgage loans reached EUR 1.1 bn, 4.5% of GDP in 2021 from EUR 783 mn or 4.3% of GDP in 2020. New mortgage loans were also higher than in 2019 (EUR 972 mn, EUR 874 mn excluding renegotiated amounts).

Mortgage rates for new loans have been declining since 2008-09. The floating rate for up to one year for house purchase dropped from a yearly average of 5.97% in 2008 to 2.10% in 2020 before rising to 2.17% in 2021.

Loan performance of households and non-financial corporations deteriorated markedly in the aftermath of the recession from 2011 to 2014. Nonperforming exposures, as defined by the European Banking Authority, rose sharply in the period, and dropped significantly in its aftermath. The resolution of Cyprus Cooperative Bank and the sale of a package of loans by Bank of Cyprus in the second half of 2018, led to a steep decline in bank non-performing exposures. Bank of Cyprus has sold three additional packages of problem loans since 2019 in difficult market conditions and Hellenic Bank announced a significant transaction in April 2022. Whilst there are no separate statistics for the performance of mortgages themselves, the performance of household loans, more than half of which are mortgages, is indicative.

Non-performing exposures of the household sector have been declining steadily. At the end of 2021 they were EUR 1.6 bn (or 14.8% of gross loans) compared with EUR 2.8 bn (23.7%) in 2020 and EUR 13.1 bn (52.3%) at the peak in early 2015. Mitigating this is a relatively high provisioning ratio of 36.3% at the end of 2021 and a high ratio of restructured facilities with the non-performing exposures of 41.9%.

### NON-MARKET LED INITIATIVES

The property market in Cyprus is being affected by tax and legislative changes. Property tax payable was abolished in 2017. A 19% VAT on building land and on the leasing of commercial property for business purposes was introduced in 2018.

In 2014, to attract foreign investors, the Council of Ministers established the 'Scheme for Naturalisation of Investors in Cyprus by Exception' which remained in place until November 2020 when it was abolished under the weight of implementation problems which exposed flawed procedures.

To aid low-income households with non-performing loans and primary homes as collateral, the government introduced a subsidy programme subject to specific income criteria, in July 2019. Applicants whose applications to participate in the scheme have been approved will continue to benefit from the scheme in accordance with the restructuring of the relevant loan that had been agreed.

In March 2020, in response to the pandemic, the government introduced a series of measures including a moratorium on loan repayments including mortgages and an interest subsidy for eligible mortgage loans from March 1, 2020. The programme expires at the end of the year and provides for an interest subsidy of 150 bps for the first four years of the loan.

### MORTGAGE FUNDING

Bank funding in Cyprus is primarily from customer deposits. Funding conditions are comfortable as reflected in the gross loans (not including provisions), to deposits ratio at 58% at the end of 2021, from 65.9% at the end of 2020. Cypriot banks have access to ECB funding. The securitisation legislation which has been

enacted in July 2018 provides an additional tool for banks to obtain funding.

### GREEN FUNDING

Cyprus will receive EUR 1.0 bn in grants and EUR 227 mn in loans, from the Next Generation EU funds in the period 2020-26. Cyprus' Recovery and Resilience Plan submitted to the European Commission consists of 134 measures structured around 13 components and grouped in five policy areas. Policies and projects to green the economy will comprise 41% of the recovery funds, and digital transition will comprise 23%. Key investments include improving the energy efficiency of buildings and incentives to use renewables.

	CYPRUS 2020	CYPRUS 2021	EU 27 2021
<b>MACROECONOMIC VARIABLES</b>			
Real GDP growth (%) (1)	-5.0	5.5	5.4
Unemployment Rate (LSF), annual average (%) (1)	7.6	7.5	7.0
HICP inflation (%) (1)	-1.1	2.3	3.0
<b>HOUSING MARKET</b>			
Owner occupation rate (%) (1)	68.6	68.6	70.0
Gross Fixed Investment in Housing (annual change)(1)	-5.9	-2.6	6.6
Building Permits (2015=100) (2)	140.1	162.8	134.0
House Price Index – country (2015=100) (2)	102.6	102.7	145.2*
House Price Index – capital (2015=100) (2)	102.7	102.2	146.1*
Nominal house price growth (%) (2)	0.7	0.0	10.3*
<b>MORTGAGE MARKET</b>			
Outstanding Residential Loans (mn EUR) (2)	8,649	8,385	6,508,621
Outstanding Residential Loans per capita over 18 (EUR) (2)	12,055	11,573	17,782
Outstanding Residential Loans to disposable income ratio (%) (2)	58.4	55.2	62.8*
Gross residential lending, annual growth (%) (2)	-10.4	43.1	12.2
Typical mortgage rate, annual average (%) (2)	2.1	2.2	2.0

\* Please note that this value is the simple average of the available values in 2021.

Sources:

(1) Eurostat

(2) European Mortgage Federation - Hyostat 2022, Statistical Tables.



## CYPRUS FACT TABLE

<b>Which entities can issue mortgage loans in your country?</b>	Financial institutions (banks and the Housing Finance Corporation HFC).
<b>What is the market share of new mortgage issuances between these entities?</b>	100%
<b>Which entities hold what proportion of outstanding mortgage loans in your country?</b>	Banks: 97% and HFC: 3%
<b>What is the typical LTV ratio on residential mortgage loans in your country?</b>	70%-80%
<b>How is the distinction made between loans for residential and non-residential purposes in your country?</b>	Depending on the use of the house, then the loan is classified as residential or not i.e. residential is for primary home or holiday use
<b>What is/are the most common mortgage product(s) in your country?</b>	Euro-denominated loans. Most of the loans are floating rates i.e. ECB base rate + spread. Fixed rate housing loans are also offered.
<b>What is the typical/average maturity for a mortgage in your country?</b>	The average maturity is 22 years.
<b>What is/are the most common ways to fund mortgage lending in your country?</b>	Customer deposits.
<b>What is the level of costs associated with house purchase in your country (taxes and other transaction costs)?</b>	The costs associated with house purchase include VAT or a transfer fee (for property sales for which VAT has to be paid, no transfer fees will be applied); a mortgage fee and stamp duty (in case of mortgage loan)- and, lastly, the costs of title deeds.
<b>What is the level (if any) of government subsidies for house purchases in your country?</b>	Due to the pandemic, the government subsidised mortgage loans for 4 years if the purpose of the house is for own use. This program has ceased as of 31/12/2021