

# Cyprus

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## IN A NUTSHELL

- GDP growth recovered to 5.6%.
- House prices have continued to rise from the low post recession levels.
- Housing demand and residential construction remained strong.
- Bank liquidity remains good.

## MACROECONOMIC OVERVIEW

The economy rebounded strongly in 2021-22 growing by 6.6% and 5.6% respectively after a 4.4% contraction in 2020 due to Covid disruptions. Growth was driven by strong performances in services sectors, particularly information, communications, and professional and financial services. Tourist activity continued to rebound strongly in 2022.

Economic growth is expected to continue in 2023-24 but at a slower pace, mainly due to an expected deterioration of external demand and slower domestic demand caused by higher interest rates and high consumer price inflation. According to the European Commission's spring forecasts, GDP is expected to grow by 2.3% in 2023 and 2.7% in 2024. GDP growth will be materially supported by EU funding in the form of grants and loans from the Recovery and Resilience Facility (RRF).

Inflation measured by the HICP, was 8.1% on average compared with 8.4% in the Euro area. Inflation peaked in July at 10.6% and has been decelerating since. It is forecast to drop to 3.8% in 2023, according to the European Commission.

The general government budget turned into a surplus of 2.1% of GDP and the public debt dropped to 86.5% of GDP from 101% in 2021. According to the European Commission, the budget will remain in surplus in 2023 by 1.8% of GDP and public debt will continue to decline dropping to 80.4% of GDP.

In the banking sector, total non-performing exposures at the end of April 2023 was EUR 2.2 bn, or 9.0% of gross loans and the coverage ratio was 53.7%. Respectively, total non-performing exposures were EUR 3 bn at the end of April 2022, 11.4% of gross loans with a coverage ratio of 50.5%. Private debt measured by bank loans to residents excluding the government, stood at 77% of nominal GDP at the end of June 2023.

## 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. Home ownership peaked in 2013 at 74% and dropped to a low of 67.9% in 2019. Since then, it has increased to 69.6% in 2022 (EU average 69.1%).

New building construction, dropped from EUR 3.0 bn in 2008 to EUR 0.92 bn in 2014. Since then, it has recovered to EUR 2.9 bn in 2021, the latest available

data. Construction of residential buildings rose from a low of EUR 0.4 bn in 2014 to EUR 1.8 bn in 2021 or 111% of 2008 values.

The long term performance of the construction sector lags the total economy. Average annual growth in construction in the period 1995-2022, was 2.2% compared with 2.9% in the economy. The volatility of the growth rate is much higher in construction. Construction activity dropped sharply in 2007-15 by a cumulative 61%, then recovered strongly in 2016-19. Real gross value added is still 25% lower than at the peak in 2007. The share of the sector's value-added in real terms dropped from 9.9% in 2007, to 4% in 2015 and then recovered to 5.8% in 2022.

Property sales fell by 82.3% in the period 2007-2013, then rose sharply in the period to 2022 at an average annual pace of 16.7%.

Prices, as measured by the Central Bank's residential property index, rose by a cumulative 17.7% in 2016-22, on an end-period basis, following a cumulative decline of 30% between 2008 and 2016. This increase was driven by apartments, up 32.6%, as opposed to houses which rose by 11.2%. Price increases in this period were greater in Limassol (28.6%) followed by Paphos (15.6%), Famagusta (15.2%), Larnaca (14.3%), and Nicosia (9%). In 2021, residential property prices increased by 2.6% on an end-year basis, and in 2022 by 6.6%.

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 features demand from locals, diplomats, and students.

The number of completed new dwellings in 2021 (latest available) was 7,357 compared with a low of 2,390 in 2015, and a peak of 18,195 in 2008. New dwellings were rising by 21% on average in 2015-2021. The total stock of dwellings at the end of 2021 was 473,000 having risen by 20% 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 as the banking sector restructures and deleverages. Total outstanding loans for house purchase at the end of 2022 were EUR 8.4 bn, 31.1% 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 38.6% (from 24% in 2012) and as a share of all household loans to 76.5% (53.1% in 2012). This indicates a higher degree of deleveraging in the period in non-mortgage loans.

New mortgage loans net of renegotiated amounts, have been rising since 2015, reaching EUR 1.2 bn in 2022 or 41.4% of total new loans net of renegotiated amounts, from EUR 0.3 bn or 16% of total in 2015.

Mortgage rates for new loans were declining since 2008 then started to rise since the second quarter of 2022, in anticipation of a tightening cycle by the ECB. The variable interest rate (up to one year initial rate fixation) for house purchase dropped from 6.5% at the end of December 2008 to 2.1% at the end of December 2019 to 3.3% at the end of December 2022 and 4.2% at the end of May 2023.

Loan performance of households and non-financial corporations deteriorated markedly in the aftermath of the recession from 2012 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. The sale of additional packages of problem loans since 2019, by the two largest banks, Bank of Cyprus and Hellenic Bank, continued to put downward pressure on the ratio of non-performing exposures.

Whilst there are no separate statistics for the performance of mortgages themselves, the performance of household loans, more than three quarters of which were mortgages at the end of December 2022, is indicative.

Non-performing exposures of the household sector have been declining steadily. At the end of December 2022, they were EUR 1.3 bn, or 12.1% of corresponding gross loans, compared with EUR 1.6 bn or 14.8% of gross loans at the end of December 2021. At their peak in early 2015, non-performing exposures of households EUR 13.1 bn or 52.3% of gross loans. There is a provisioning ratio of 35.4% and a high ratio of restructured facilities with the non-performing exposures of 38.9% at the end of December 2022.

### NON-MARKET LED INITIATIVES

The property market in Cyprus is being affected by tax and legislative changes. Property tax 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 help 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 have been approved will continue to benefit from the scheme in accordance with the restructuring 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 government, in the context of its policies of social supporting has been working with the national parliament and the European Commission for a programme of reduced VAT to 5%, for the acquisition of a primary home subject to conditions. The final proposal has been approved by parliament in June 2023.

### MORTGAGE FUNDING

Bank funding is primarily from customer deposits. Funding conditions are comfortable as reflected in the gross loans (not including provisions), to deposit ratio of 50.1% at the end of 2022, from 58% at the end of 2021. The loans to deposits ratio was higher than 100% in 2017. At the same time Cypriot banks have access to ECB funding. The securitisation legislation which has been enacted in July 2018 provides an additional funding tool.

### 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 received the payment, of EUR 157 million in September 2021 following the approval of the national recovery plan the previous July. Cyprus received its first disbursement in December 2022, of EUR 85 million, following the passage of conditional legislation in parliament, and after approval from the European Commission.

	CYPRUS 2021	CYPRUS 2022	EU 27 2022
<b>MACROECONOMIC VARIABLES</b>			
Real GDP growth (%) (1)	6.6	5.6	3.5
Unemployment Rate (LSF), annual average (%) (1)	7.5	6.8	6.2
HICP inflation (%) (1)	2.3	8.1	9.2
<b>HOUSING MARKET</b>			
Owner occupation rate (%) (1)	69.8	69.6	69.1
Gross Fixed Investment in Housing (annual change)(1)	-2.6	6.0	1.5
Building Permits (2015=100) (2)	162.8	151.7	125.8
House Price Index – country (2015=100) (2)	102.7	106.7	164.6*
House Price Index – capital (2015=100) (2)	102.2	105.2	163.8*
Nominal house price growth (%) (2)	0.0	3.9	10.6*
<b>MORTGAGE MARKET</b>			
Outstanding Residential Loans (mn EUR) (2)	8,385	8,386	6,743,197
Outstanding Residential Loans per capita over 18 (EUR) (2)	11,573	11,461	18,433
Outstanding Residential Loans to disposable income ratio (%) (2)	55.2	48.8	71.5
Gross residential lending, annual growth (%) (2)	43.1	5.1	-6.5
Typical mortgage rate, annual average (%) (2)	2.2	2.6	3.1

\* Please note that this value is the simple average of the available values in 2022.

Sources:

(1) Eurostat

(2) European Mortgage Federation – Hypostat 2023, Statistical Tables.



## CYPRUS FACT TABLE

**Which entities can issue mortgage loans in your country?** Financial institutions (banks and the Housing Finance Corporation HFC).

**What is the market share of new mortgage issuances between these entities?** 100%

**Which entities hold what proportion of outstanding mortgage loans in your country?** Banks: 97% and HFC: 3%

**What is the typical LTV ratio on residential mortgage loans in your country?** 70%-80%.

**How is the distinction made between loans for residential and non-residential purposes in your country?** 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.

**What is/are the most common mortgage product(s) in your country?** Euro-denominated loans. Most of the loans are floating rates i.e. ECB base rate + spread. Fixed rate housing loans are also offered.

**What is the typical/average maturity for a mortgage in your country?** The average maturity is 22 years.

**What is/are the most common ways to fund mortgage lending in your country?** Customer deposits.

**What is the level of costs associated with house purchase in your country (taxes and other transaction costs)?** 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.

**What is the level (if any) of government subsidies for house purchases in your country?** 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. The Cypriot parliament has approved a government proposal for a programme of reduced VAT to 5%, for the acquisition of a primary home subject to conditions. The programme requires the final approval of the European Commission.