

# CYPRUS: A SUCCESS STORY

**V**INCENZO GUZZO, THE RESIDENT REPRESENTATIVE FOR CYPRUS OF THE INTERNATIONAL MONETARY FUND, DESCRIBED CYPRUS AS “A SUCCESS STORY”, EXPLAINING THAT THE ECONOMIC ADJUSTMENT PROGRAMME HAS DELIVERED AN IMPRESSIVE TURNAROUND OF THE ECONOMY DURING THE PAST THREE YEARS, HAVING RETURNED TO POSITIVE GROWTH IN 2015 AND ACCELERATED FURTHER IN 2016, BEYOND EXPECTATIONS. HE NOTED THAT THE BANKING SYSTEM IS NOW ON A MUCH MORE SOLID FOOTING AND WORKOUTS OF NONPERFORMING LOANS ARE ACCELERATING, OPENING SPACE FOR NEW PRODUCTIVE LENDING. MOREOVER, THE COUNTRY’S FISCAL POSITION HAS BEEN RESTORED TO A SUSTAINABLE PATH, AND PUBLIC DEBT IS NOW FIRMLY ON A DOWNWARD TRAJECTORY.

The IMF Representative told the Summit that the economic recovery is broad-based and expansion is expected to continue. He then focused on what he sees as the three challenges facing Cyprus:

#### CHALLENGE 1: NON-PERFORMING LOANS

At around €26 billion, non-performing exposures are still close to 150% of GDP and the NPE ratio for the total banking system is 49%. On a positive note, over €14 billion of loans have been restructured, €6.8 billion of which from early 2015. Banks have set up loan restructuring operations and refining policies and practices, a legal framework for foreclosure and insolvency has been established and is starting to operate and a law allowing banks to sell their loans has been adopted. The Central Bank of Cyprus, said Vincenzo Guzzo, is taking an increasingly active role in encouraging and monitoring progress with reducing NPLs. He noted that dealing with the NPL problem effectively not only has an impact on the balance sheet and the capital of the banks, but it also has broader implications for the economy. By lowering NPLs, banks can increasingly extend new (target-

ed) credit to families and corporations on better terms, thus supporting investment and jobs. Banks’ improved lending capacity especially affects SMEs that are more dependent on bank financing.

#### CHALLENGE 2: PUBLIC SECTOR DEBT

At nearly 109% of GDP in 2015, public sector debt is still high, while the primary surplus will have to be kept at around 3% of GDP to maintain public debt on a sustained downward path. So far, fiscal performance has consistently exceeded targets and the Government has accessed the market four times, using part of the proceeds to build cash buffers, while bank government-guaranteed bonds issued during the crisis were cancelled, reducing the stock of government guarantees by nearly a third. Ensuring sustainable public debt allows adequate fiscal space for productive public investment spending, which in turn supports long-lasting growth.

“Controlling the growth of the public sector wage bill and increasing the efficiency of the public sector through promotions and mobility across the civil service is a critical step in this direction,” Guzzo said.

#### CHALLENGE 3: IMPROVING THE BUSINESS ENVIRONMENT

Cyprus’ ranking in the *World Bank Doing Business* Index has moved to 47 in 2016 from 60 a year earlier. An ambitious reform agenda is being developed and implemented, and an extensive action plan for growth, aimed at improving the business environment, has been developed. Steps already taken include adopting the legal framework for Fiscal Responsibility and Budget Systems, integrating the Inland Revenue and VAT Departments, enacting amendments to the foreclosure law, reforming the insolvency framework and privatising the commercial

activities of Limassol port. Guzzo noted that the legal unbundling of the Electricity Authority into two separate companies will become effective in December. A more business-friendly environment implies more investment, the IMF Representative said. “The privatisation of state-owned enterprises allows better and less expensive services for the population and attracts foreign direct investment, which can bring jobs and increase liquidity in the economy.” He went on to note that the development of an investment fund industry will help channel capital towards productive investment and reduce over-reliance on bank credit, while measures such as reducing labour market redundancy costs, opening up closed professions, removing barriers to competition, reducing red tape, strengthening the legal system and fostering innovation will all have a significant impact on medium-term growth.



So far, fiscal performance has consistently exceeded **TARGETS**