



CENTRAL BANK OF CYPRUS
ECONOMIC RESEARCH DEPARTMENT

MONETARY POLICY REPORT

JULY 2006



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The Monetary Policy Report (MPR) is drafted by the Central Bank's Economic Research Department in preparation for the meetings of the Monetary Policy Committee (MPC), and summarises current economic developments in Cyprus. The MPR appears about eight times a year. Of these eight issues, four are more extensive and comprehensive than the others.

The Greek version of the MPR as well as the English version of the statistical tables are available on the Bank's website on the same day as the MPC meeting. The entire English version of the MPR is posted on the Bank's website during the following month. The English edition of the more extensive version is also available in printed form.

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ECONOMIC RESEARCH DEPARTMENT

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Symbols, conventions and abbreviations

1. The following symbols are used:

-	no figures to be expected	CYP and £	Cyprus pound
n.y.a.	not yet available	€	euro
0	nil or negligible	\$	US dollar
Q	quarter	ST£	pound sterling
p	provisional	¥	Japanese yen

2. Thousands, millions and billions are separated by a dot (.) and decimals are separated by a comma (,). In some cases the totals in the tables may not add up due to rounding.

3. CCIs	Co-operative Credit Institutions
CSE	Cyprus Stock Exchange
Cystat	Statistical Service of the Republic of Cyprus
ECB	European Central Bank
Eurostat	Statistical Office of the European Communities
HICP	Harmonised Index of Consumer Prices

1. INTRODUCTION

The world economy continues to expand at a subdued pace as a result of restrained growth in the US and the euro area. Inflationary pressures emanating from the second round effects of the rise in oil prices have already taken effect and the major central banks are maintaining their vigilance in order to prevent further escalation of inflationary expectations. In this environment, both the ECB and the US Federal Reserve raised their interest rates at their latest meetings¹ while analysts expect both monetary authorities to continue a further tightening during the summer months. Interest rates are expected to rise in Japan soon, despite the fact that the Bank of Japan has not as yet set a time schedule for this.

Inflation rose to 3,13% in May 2006, compared with 2,96% in the previous month. The small increase reflects mainly the acceleration of the increase in the prices of petroleum and domestic industrial products. Inflationary pressures are also supported by the continuing growth of money supply and credit to the private sector. M2 is still growing at more than three times the respective rate recorded in May 2005. Specifically, M2 grew by 13,9% in the year to May 2006, compared with 4,2% in the same period of the previous year. However, it is noted that last year's low rate was partly due to the tax amnesty scheme. The annual growth of credit accelerated to 11,1% in May, compared with 4% in the same month of 2005. More specifically, lending in foreign currency was still at high levels compared with the previous year, accounting for more than 50% of the total amount of credit generated in the 12 months to May 2006.

At the same time, during May and June surplus liquidity conditions prevailed in the money market. This is an additional cause of concern regarding inflationary pressures.

As far as external transactions are concerned, the number of tourists visiting Cyprus in the first five months of 2006 was down by 2,5% compared with an increase of 5,6% recorded in the corresponding period of 2005. Revenue from tourism recorded an increase of 2,5% in the first four months of 2006, compared with a 4,7% decrease in the corresponding period of 2005.

Provisional data published by Cystat recorded a 13,5% increase in receipts from total imports in the first four months of 2006, compared with a marginal increase of 0,3% in the corresponding period of 2005. The significant increase is partly the result of the increase in the international price of oil. Total exports increased by 5,7% in the first four months of the year, compared with an increase of 31,2% in the corresponding period of 2005. As a result the trade deficit increased to £799,9 million in the first four months of 2006, compared with £690,3 million in the corresponding period of 2005.

The turnover index of retail trade rose by 5,5% in the first two months of 2006 compared with 5,3% in the corresponding period of the previous year. In the labour market, unemployment as a percentage of the economically active population rose to 3,8% in the first five months of 2006, compared with the corresponding period of 2005. However, the fall in unemployment is due to a change in

¹ On 8 and 29 June 2006, respectively.

methodology for measuring seasonal unemployment and not the result of a change in economic fundamentals. In the secondary sector, there was a deceleration in the sales of cement and the volume of building permits in the first quarter of 2006. At the same time, manufacturing displayed a decrease during the first quarter of the year.

As regards the preliminary consolidated accounts of the Ministry of Finance, which cover the central government and the social security funds for the period January-April 2006, total expenditure amounted to £897,2 million and total revenue to £873,3 million, thus recording a fiscal deficit of £24 million or 0,3% of GDP.

Compared with the corresponding four month period of 2005, revenue and expenditure increased by 2% and 7,1%, respectively. During the same period, public debt amounted to 69,4% of GDP compared with 69,6% in the corresponding period of 2005.

By excluding the receipts which emanated from temporary measures and which correspond to the first four months of 2005, the fiscal balance has improved by 0,7 percentage points. As regards the general government data for the first six months of 2006, it is anticipated that they will be published around mid-August of 2006.

2. ECONOMIC DEVELOPMENTS

2.1 INTERNATIONAL DEVELOPMENTS AND EXCHANGE RATES

International Economic Developments

In the **US** GDP grew at an annual rate of 3,6% during the first quarter of 2006. This was driven by consumption and investment expenditures. At the same time, analysts continue to express concern about the size of the US current account deficit, which is considered as unsustainable. Imports continue to rise rapidly and cause pressure on the dollar. Market expectations are that in the short term the US economy will continue to expand less rapidly due to the slowdown in consumption and higher interest rates. The US Federal Reserve has already hinted that more interest rate hikes may follow if this is considered necessary. Inflation was 4,2% in May, compared with 2,8% in the same month of the previous year, while unemployment was 4,6% in May 2006, compared with 5,1% in May 2005.

In the **euro area** GDP rose at an annual rate of 1,9% in the first quarter of 2006, mainly due to domestic demand. Evidence from surveys on consumption and industrial confidence confirm the continuation of this trend for the second quarter. The ECB believes that the euro area is close to its potential growth rate, despite the problems caused by high oil prices. The revised projections of the ECB on GDP growth and inflation in the euro area are slightly lower than the projections in March. In particular, the ECB believes that real GDP growth will be between 1,8% and 2,4% in 2006 and between 1,3% and 2,3% in 2007. In March, ECB projections for GDP growth were 1,7%-2,5% for 2006 and 1,5%-2,5% for 2007.

Inflation is anticipated to fluctuate between 2,1% and 2,5% in 2006 and between 1,6% and 2,8% in 2007. In March, ECB projections were 1,9%-2,5% for 2006 and the same as those of June for 2007. High oil prices still create upside risks for inflationary pressures and long-term downside risks for GDP growth.

In the **UK** GDP growth continues close to potential, mainly based on investment expenditures and the build-up of company inventories. Analysts believe that the economy will continue to expand, supported by private consumption and exports. During the period February – April, unemployment reached 5,3%, compared with 4,7% in the same period of the preceding year. Inflation rose to 2,2% in May, compared with 1,9% in the same month of the previous year.

In **Japan** domestic demand continues to be the main engine of GDP growth. Economic prospects are positive and although interest rates will remain at zero levels for the time being, analysts believe that the first rise in interest rates is very close. At the same time some analysts believe that should the Governor of the Bank of Japan, Toshihiko Fukui, resign following the scandal surrounding his private investments, it could prove to be an obstacle to the restrictive monetary policy adopted in March. At this juncture, it is not clear whether Mr Fukui will indeed resign. The government has fully supported him while public opinion believes that his credibility has been damaged.

Following a positive trend, as a result of corporate profit announcements, all three main stock market indices (Chart 1) declined in May. The increased likelihood of interest rate rises in all three geographical areas (USA, euro area and Japan) led to a selling of stocks. More specifically, in May the S&P 500 index declined by 2,7%, the Dow Jones Eurostoxx index fell by 6% and the Nikkei 225 receded by 8,6%. During the last three months the aforementioned indices decreased by 1,6%, 4,1% and 3,1%, respectively.

In the **oil markets**, the average daily price of Brent crude reached \$69,63 per barrel in May, compared with \$69,49 per barrel in April. During June the average daily price decreased to \$67,8 per barrel. Towards the end of June, there was an increase in the supply of oil from Iraqi that had been disrupted for about a year due to the damaged pipeline between Turkey and Iraq.

Table 1
GDP projections⁽¹⁾
 (annual percentage change)

	The Economist Poll GDP forecasts ⁽²⁾			Lehman Brothers Weekly Outlook - GDP ⁽³⁾			International Monetary Fund World Economic Outlook ⁽⁴⁾			European Commission Economic Forecasts ⁽⁵⁾		
	2005	2006	2007	2005	2006	2007	2005	2006	2007	2005	2006	2007
World				2,6 (2,7)	2,9 (2,8)	2,2 (2,3)	4,8 (4,3)	4,9 (4,3)	4,7	4,6 (4,3)	4,6 (4,3)	4,3 (4,2)
Euro area	1,4	2,1	1,7	1,4	2,0 (1,7)	0,9 (0,8)	1,3 (1,2)	2,0 (1,8)	1,9	1,3	2,1 (1,9)	1,8 (2,1)
USA	3,6	3,4 (3,3)	2,8	3,5	3,5	2,8 (3,0)	3,5	3,4 (3,3)	3,3	3,5	3,2	2,7
Japan	2,6	2,9 (3,0)	2,4	2,6 (2,7)	3,1 (2,8)	2,9 (3,0)	2,7 (2,0)	2,8 (2,0)	2,1	2,7 (2,5)	2,8 (2,2)	2,4 (1,8)
UK	1,7	2,4 (2,3)	2,5 (2,4)	1,8	2,2	2,4	1,8 (1,9)	2,5 (2,2)	2,7	1,8 (1,6)	2,4 (2,3)	2,8

(1) Figures in parentheses indicate the corresponding projection in the previous Monetary Policy Report, in case of change. In the case of the International Monetary Fund and European Commission, the figures indicate the projections in September 2005 and November 2005, respectively.

(2) The Economist, 24 June 2006.

(3) Lehman Brothers Global Weekly Economic Monitor, 23 June 2006.

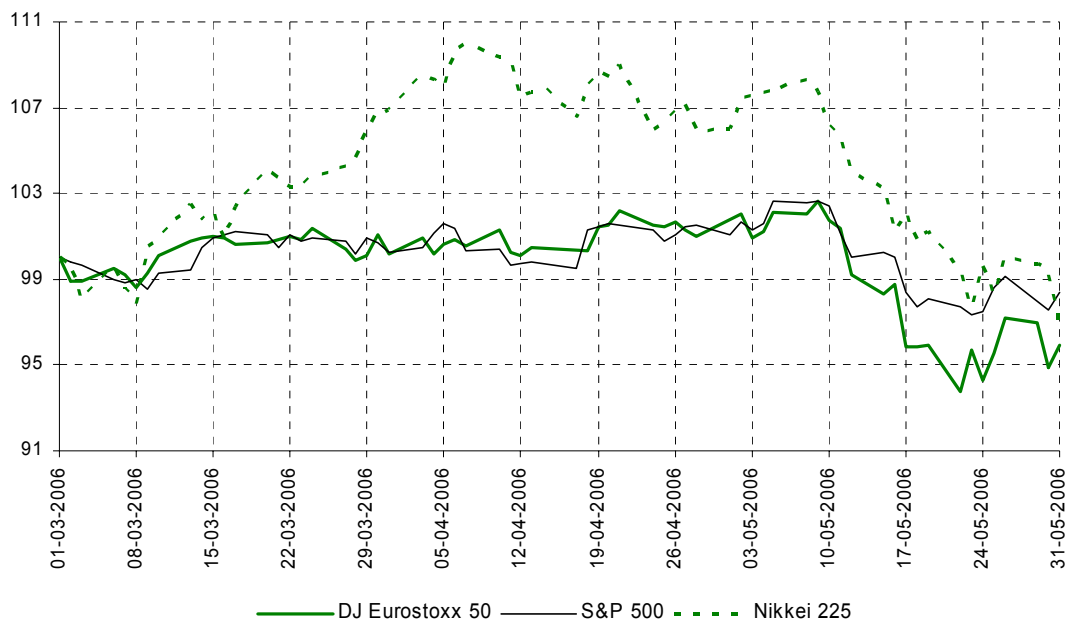
(4) International Monetary Fund, World Economic Outlook, April 2006.

(5) European Commission, Economic Forecasts, Spring 2006.

Chart 1

Selected international stock market indices

(1 March 2006 = 100, daily data)



Source: Bloomberg.

Table 2**Main economic indicators***(percentage change year-on-year)*

	GDP				Industrial production April (annual)	Retail sales April (annual)	Unemployment April (annual)	Inflation ⁽²⁾ May (annual)
	2005 (Q4)		2006 (Q1)					
	(quarterly) ⁽¹⁾	(annual)	(quarterly) ⁽¹⁾	(annual)				
UK	2,4	1,8	2,3	2,2	-1,0	4,0 ⁽³⁾	5,3 ⁽⁴⁾	2,2
Japan	5,4	4,0	3,1	3,8	3,6	-1,5	4,1	0,4 ⁽⁵⁾
USA	1,6	3,2	5,3	3,6	4,3 ⁽³⁾	4,6	4,6 ⁽³⁾	4,2
Euro area	1,0	1,7	2,4	1,9	1,9	2,8	8,0	2,5

Source: *The Economist*, 24 June 2006.⁽¹⁾ Percentage change on previous quarter at an annualised rate.⁽²⁾ Based on the consumer price index.⁽³⁾ May 2006.⁽⁴⁾ February - April 2006.⁽⁵⁾ April 2006.**International currencies**

In June 2006 the dollar strengthened reaching 125 cents per euro on 23 June, compared with 128 cents per euro on 1 June. The announcement of US economic indicators seems to have affected positively the course of the US dollar. However, it should be noted that the US Federal Reserve left the door open for further rate rises, something which is also expected by the markets.

The publication of economic indicators for the euro area countries, which presented a negative picture of several of their economies, has affected the course of the euro. At the same time, the 25 basis points increase in ECB interest rates did not have any positive effect on the euro since the markets expected a higher increase.

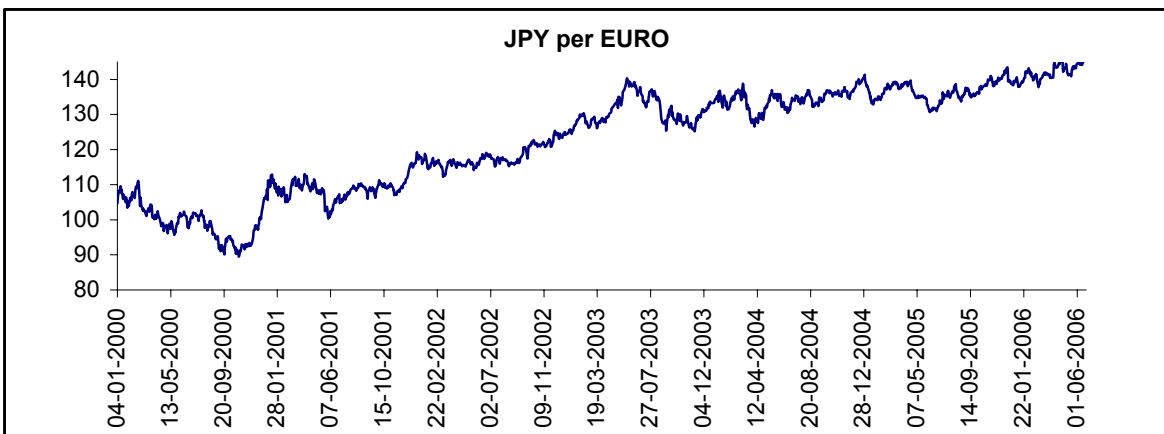
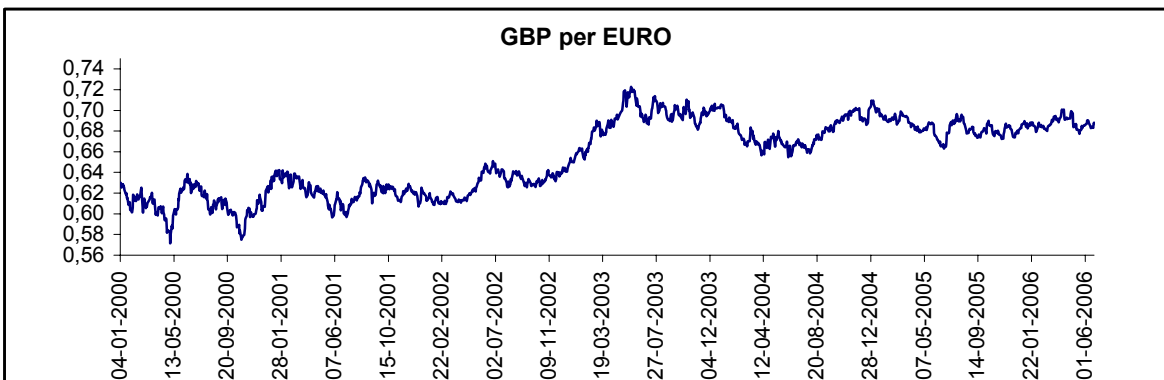
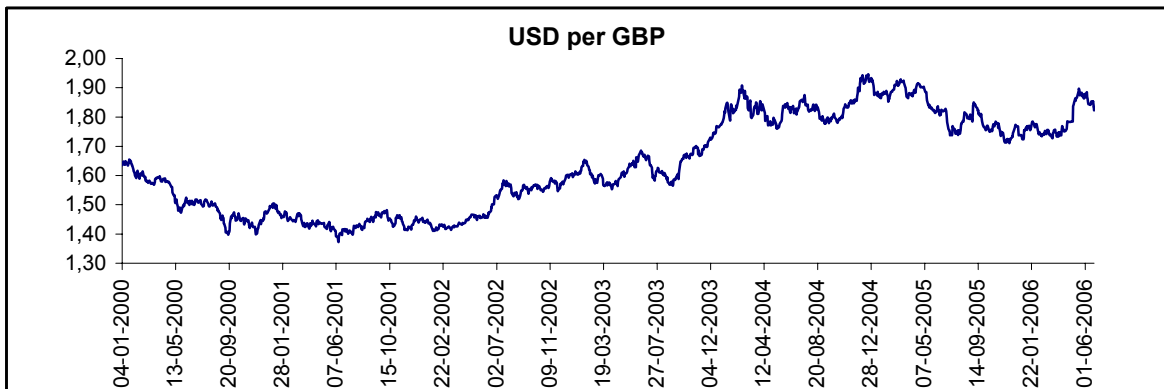
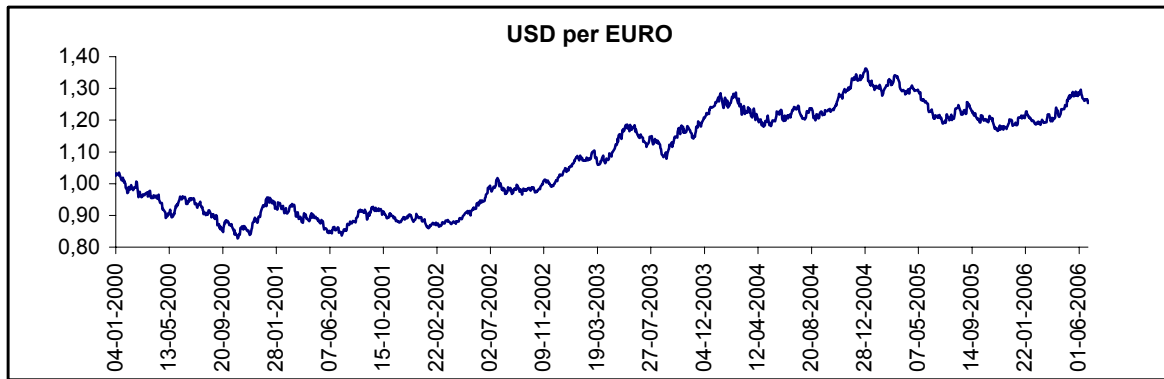
During the period under consideration, as well as the first half of 2006, sterling did not register significant fluctuations against the euro. On 23

June, sterling remained stable at 69 pence to the euro. Sterling was supported by the continued interest of foreign investors in British companies, as well as by expectations of interest rate increases by the Bank of England.

The Japanese yen did not record significant fluctuations during the period under review, reaching ¥145,94 per euro on 23 June, compared with ¥144,54 per euro on 1 June. The yen seems to have been affected by expectations for possible rate rises by the Bank of Japan.

The fluctuations of the aforementioned currencies over the last six years are shown in Chart 2.

Chart 2
Major international currencies
 (middle rate)



Source: Central Bank of Cyprus.

Cyprus pound

In the period 1 January - 23 June 2006, the Cyprus pound recorded a gradual but continuous marginal weakening relative to the euro. More specifically, during the period from 1 to 23 June the Cyprus pound remained stable of £0,5750 per euro. Reflecting the fluctuations of foreign currencies during the period under review, the Cyprus pound depreciated against the dollar, reaching \$2,1813 on 23 June, compared with \$ 2,2208 on 1 June.

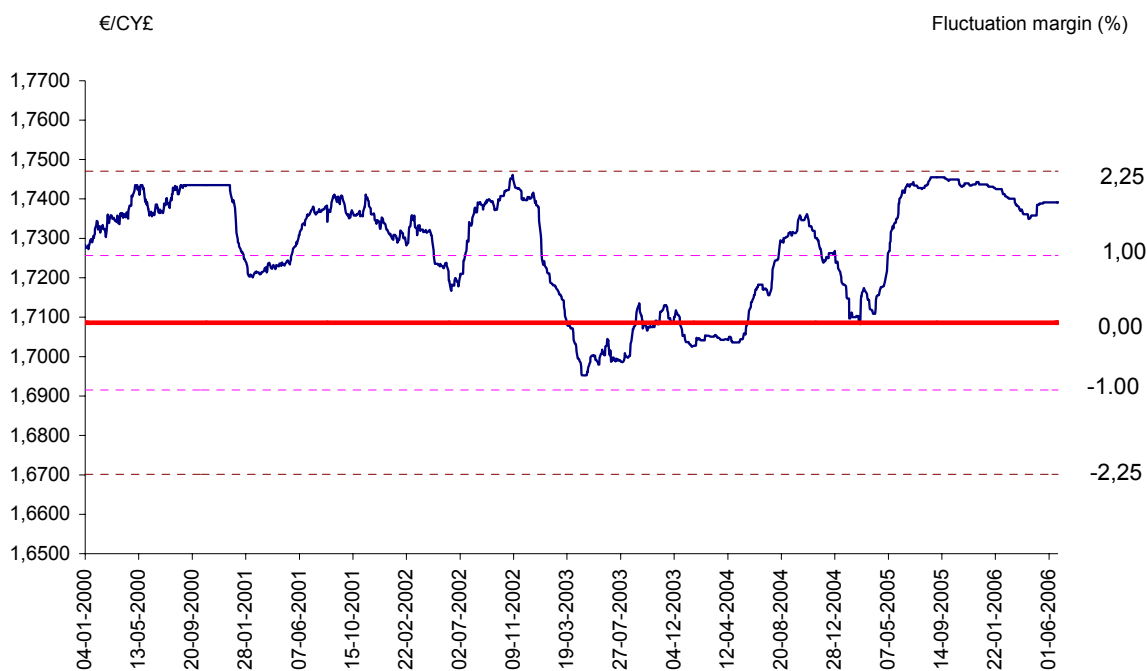
During the same period the Cyprus pound recorded marginal fluctuations relative to sterling, reaching ST£1,1968 on 23 June, compared with ST£1,1908 on 1 June.

Recent exchange rate fluctuations of the Cyprus pound relative to the euro, dollar, sterling and yen are shown in charts 3 and 4.

Chart 3

Exchange rate of the euro against the Cyprus pound

(middle price fixing)

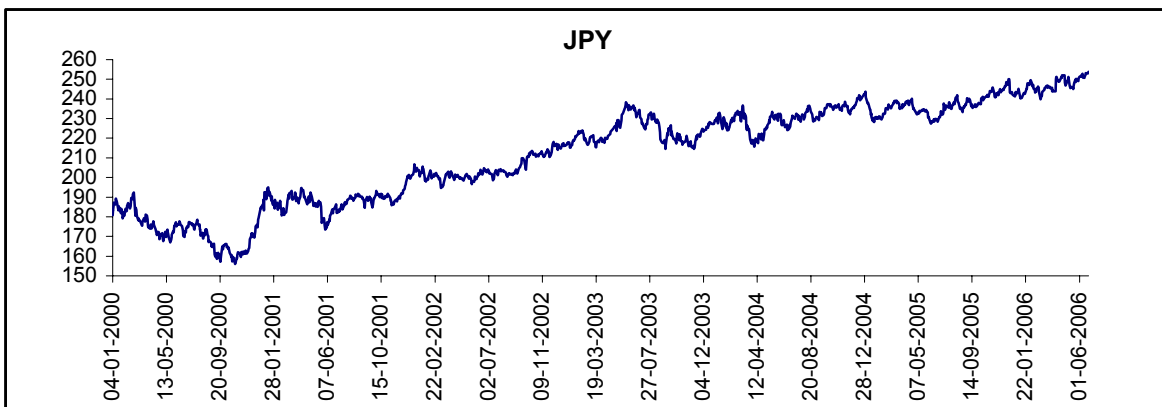
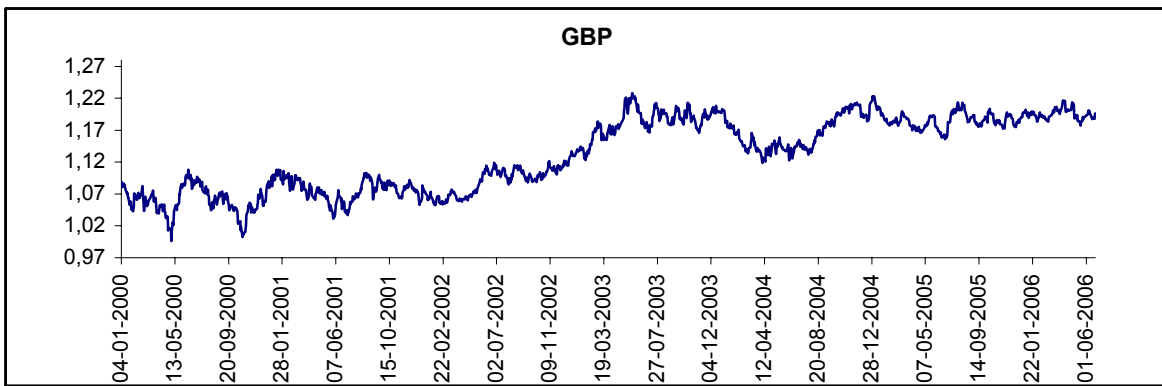
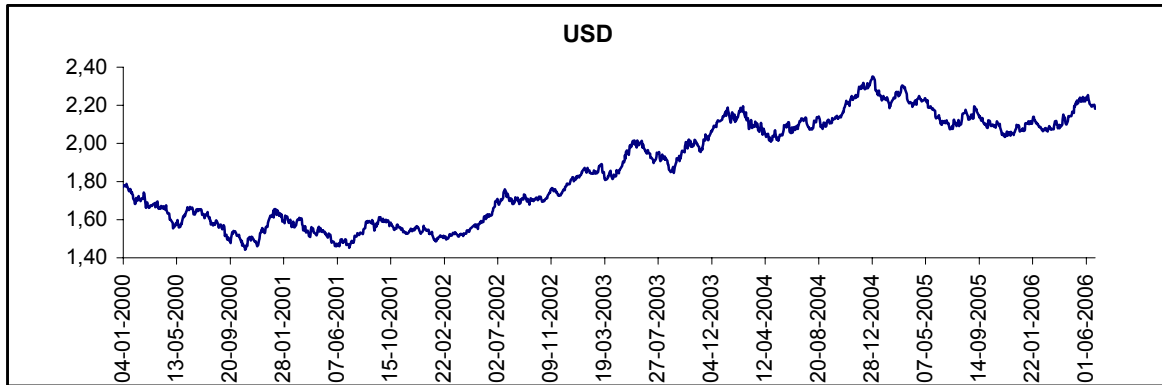


Source: Central Bank of Cyprus.

Note: The official fluctuation margins of the Cyprus pound against the euro are set equal to ±15%.

Chart 4

Cyprus pound against major international currencies
(middle rate)



Source: Central Bank of Cyprus.

BOX 1

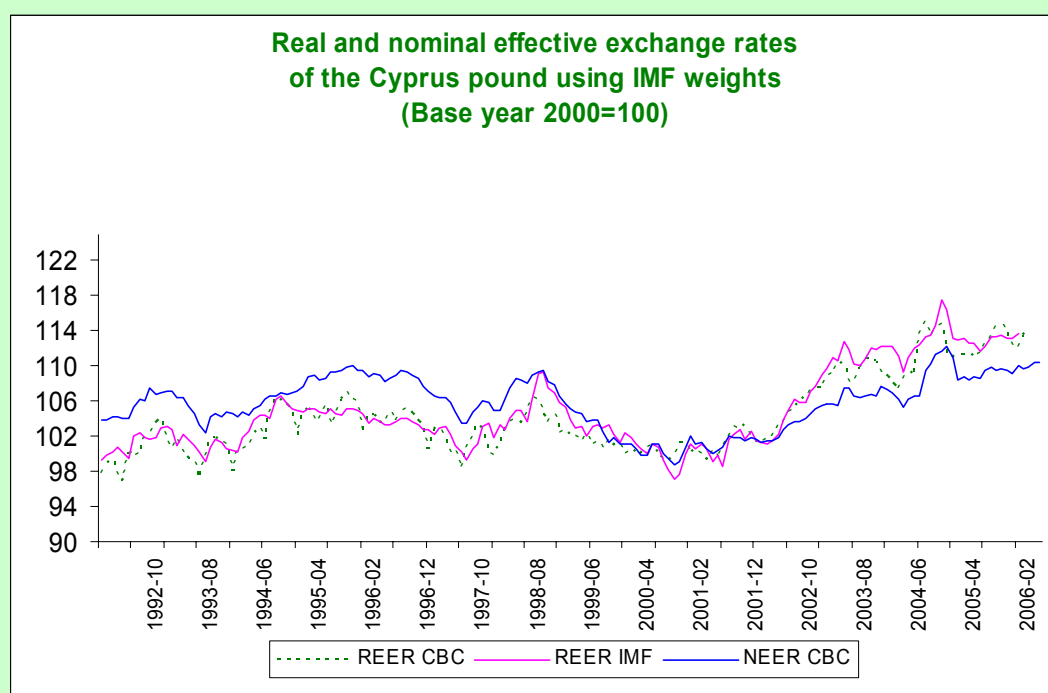
Effective exchange rate indices of the Cyprus pound

Effective exchange rate indices reflect the average fluctuation of a currency relative to the currencies of its trading partners. The effective exchange rate expressed in real terms represents the deflated value of the corresponding nominal effective exchange rate, where the deflator can be either the consumer price index or any other price or cost variable such as unit labour cost.

The chart below illustrates the monthly nominal and real effective exchange rates of the Cyprus pound from January 1992 to April and May 2006, respectively. An upward trend of the overall index reflects an appreciation of the domestic currency in real or nominal terms, thus indicating weakening of the competitiveness for exported products.

The real effective exchange rate of the Cyprus pound, REER IMF, shown in the chart below is calculated by the International Monetary Fund (IMF) and is a third country competition weighted index, taking into account 19 countries. The weights are estimated using data on trade and tourism for the years 1988 – 1991 (for the data until 1994) and 1999 - 2001 (for the data from 1995 onwards) and the consumer price index is used to deflate the series. Using 2000=100 as the base year, REER IMF reached 113,73 units in January 2006. Due to the time lag in reporting, the Central Bank of Cyprus calculates its own index based on the IMF index, using 8 instead of 19 countries. The Central Bank of Cyprus index, REER CBC, shown in the chart follows the IMF index very closely. The most recent available data for this index, with the base year 2000=100, are for April 2006 in real terms and May 2006 in nominal terms. The REER CBC index averaged 114,4 units in April 2006 whereas the index in nominal terms reached 110,4 units in May 2006.

The outlook indicated by the nominal index differs from the one indicated by the real index. The sharper appreciation observed in real terms is primarily attributable to the higher inflation recorded in Cyprus compared with other European countries, largely as a result of the progressive increase in VAT from 10% to 15% during 2002 and 2003 as well as increases in other consumption taxes (particularly those on petroleum products). More recent data pertaining to May 2006 place the index at 110,4 units. For the whole of 2005 the average level of the index was close to 109,5 units.



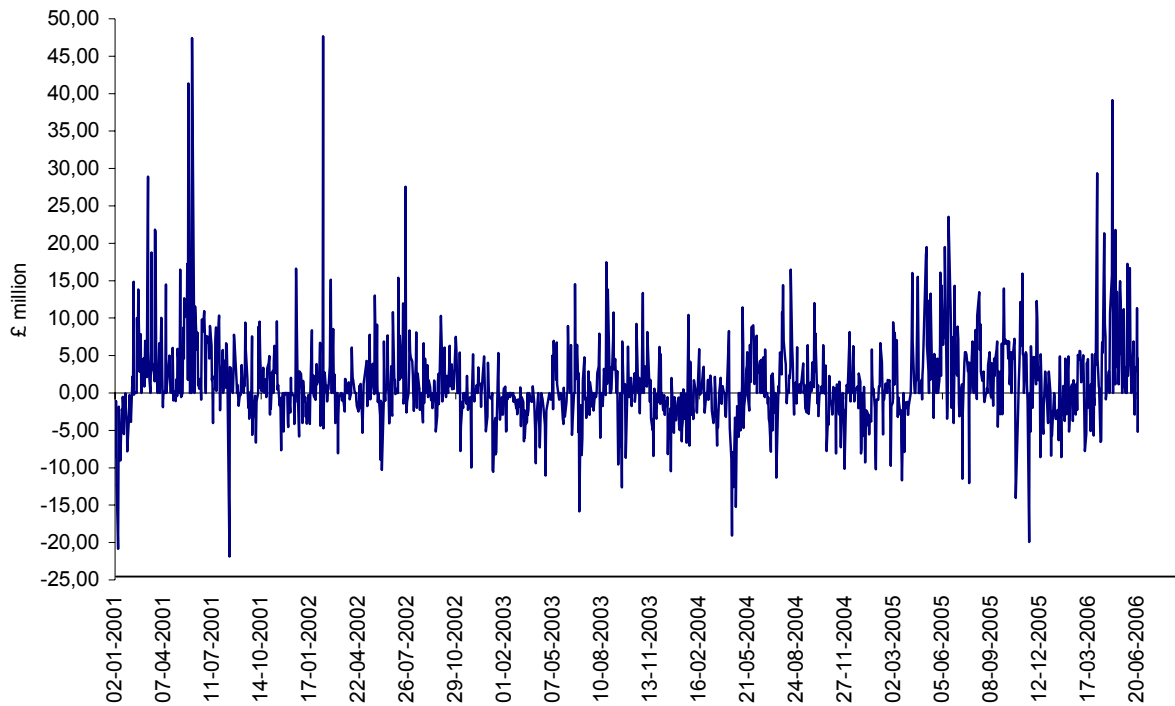
Sources: Central Bank of Cyprus and International Monetary Fund.

Table 3 illustrates the Central Bank’s foreign currency transactions until 23 June 2006 on the basis of their transaction date. The corresponding daily total transactions in foreign currency by the Central Bank with the local banks since 2001 are illustrated in Chart 5. During the first 23 days of June, net inflows of

£70,91 million were recorded compared with net inflows of £121,58 million during the corresponding period of 2005. For the period 1 January until 23 June 2006 net inflows of £304,63 million were recorded, compared with net inflows of £225,33 million in the corresponding period of 2005.

Chart 5

Daily purchases / sales of foreign exchange by the Central Bank of Cyprus from / to domestic banks



Source: Central Bank of Cyprus.

Note: Purchases of foreign exchange by the Central Bank of Cyprus are shown with a positive sign.

Table 3**Domestic foreign exchange market: purchases and sales by the Central Bank of Cyprus**

Period	Foreign currency per Cyprus pound (period average)			Purchases(+)/Sales(-) of foreign exchange by the Central Bank (based on transaction date)			
				In foreign currency (million)			In Cyprus pounds (million)
	Euro	USD	Sterling	Euro	USD	Sterling	
<u>Yearly</u>							
2001	1,7314	1,5602	1,0805	755,82	242,99	76,39	663,30
2002	1,7383	1,6445	1,0934	321,55	64,75	53,05	273,13
2003	1,7121	1,9378	1,1849	-259,75	5,16	19,50	-134,01
2004	1,7187	2,1357	1,1663	-91,40	15,75	25,70	-25,52
<u>Quarterly</u>							
2004 Q1	1,7060	2,1348	1,1604	-155,75	2,00	30,20	-64,23
2004 Q2	1,7099	2,0579	1,1401	-19,05	6,50	1,10	-7,49
2004 Q3	1,7271	2,1107	1,1612	199,60	4,95	-19,20	101,02
2004 Q4	1,7317	2,2394	1,2033	-116,2	2,3	13,6	-54,82
2005 Q1	1,7161	2,2496	1,1902	-161,1	10,5	30,1	-64,1
2005 Q2	1,7297	2,1785	1,1742	518,15	22,3	4,40	312,86
2005 Q3	1,7443	2,1278	1,1928	250,45	3,55	-0,10	141,83
2005 Q4	1,7440	2,0737	1,1861	292,05	0,5	2,90	170,09
2006 Q1	1,7407	2,093	1,1947	-85,05	1,70	0,60	-47,47
<u>2005</u>							
January	1,7189	2,2561	1,2009	-100,60	0,00	10,90	-49,46
February	1,7149	2,2324	1,1828	-18,00	0,00	12,30	-0,11
March	1,7145	2,2602	1,1868	-42,50	10,05	6,90	-14,53
April	1,7159	2,2208	1,1722	91,35	20,75	4,40	-66,32
May	1,7312	2,1958	1,1852	175,45	0,05	0,00	101,53
June	1,7419	2,1189	1,1653	251,35	1,50	0,00	145,01
July	1,7432	2,0992	1,1992	49,00	0,00	0,00	28,10
August	1,7453	2,1395	1,1831	134,05	-3,40	0,00	75,27
September	1,7445	2,1447	1,1960	67,40	-0,15	-0,10	38,46
October	1,7447	2,0961	1,1892	140,30	0,80	0,00	80,78
November	1,7437	2,0558	1,1845	95,15	-0,15	0,90	55,24
December	1,7438	2,0691	1,1845	56,60	-0,15	2,00	34,07
<u>2006</u>							
January	1,7429	2,1102	1,1960	-79,95	-0,30	0,00	-46,01
February	1,7411	2,0798	1,1896	-8,45	0,00	0,60	-4,34
March	1,7382	2,0894	1,1984	3,35	2,00	0,00	2,88
April	1,7356	2,1247	1,2059	159,45	-0,15	2,00	93,46
May	1,7388	2,2216	1,1881	326,40	0,00	0,00	187,73
June*	1,7392	2,2068	1,1924	123,20	0,15	0,00	70,91

*Figures until 23 June 2006.

Source: Central Bank of Cyprus.

2.2 MONETARY DEVELOPMENTS

The banking system in Cyprus consists of the domestic banks, the co-operative credit institutions (CCIs) and the international banking units (IBUs). Although there are updated figures for commercial banks, data for CCIs are available with a delay of approximately three months. For this reason, in the analysis that follows it is mainly commercial bank data that are described as they are readily available, whereas in the case of CCIs our comments are based on estimates or preliminary data. Regarding IBUs, a concise analysis is presented which is specific to the loans provided in foreign currency. Following the complete liberalisation of capital movements, IBUs are free to provide credit to Cypriots. It should be noted that since 1 January 2006 the term “International Banking Units” (IBUs) has ceased to be used. Upon introduction of the new monthly balance sheet for monetary and financial institutions (MFIs) the data from IBUs will be consolidated with the local MFIs.

Analysis of monetary aggregates

In the monetary sector the main development was the continued rise in M2 and credit to the private sector. At the same time large inflows of foreign exchange continued, consistent with the increase in foreign currency lending. As a

result, surplus liquidity prevailed in the money market. The aforementioned developments are a cause of concern for inflationary pressures.

The Central Bank of Cyprus has decided to temporarily halt the process of a gradual reduction of the minimum reserve requirement from the current 5%, in order to avoid a further increase in surplus liquidity.

According to provisional data, the annual growth rate of total money supply M2C², which includes deposits with banks and CCIs, reached 12,4% in May, compared with 12% in April 2006 and 5,8% in May 2005. The annual growth of total credit to the private sector accelerated to 10,5% in May 2006, compared with 5,9% in the same period of 2005.

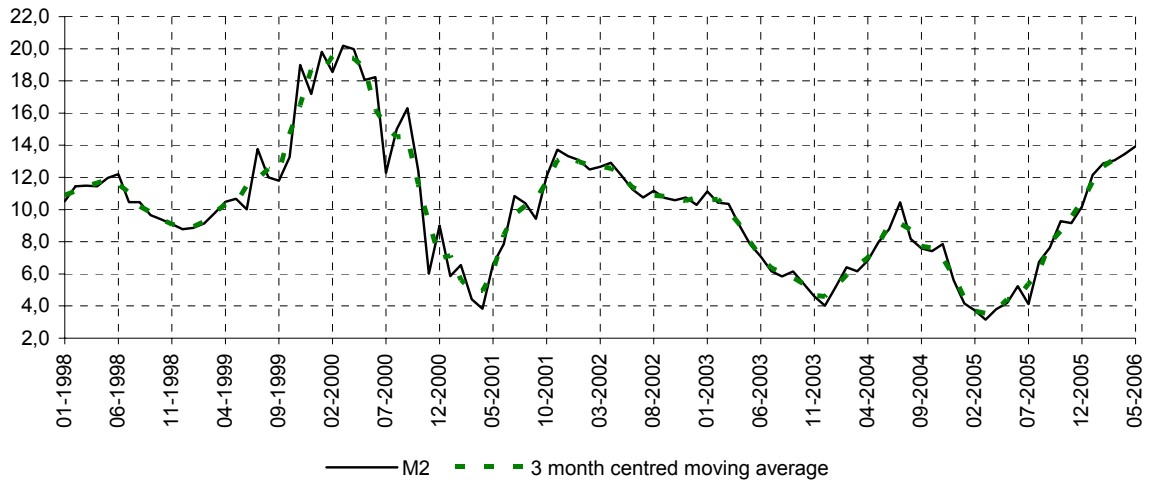
Based on domestic bank data, the rate of growth of both M2 and credit to the private sector accelerated in May compared with April. More specifically, M2 grew by 13,9% in May compared with 13,5% in April 2006 and 4,2% in May 2005. The three-month moving average of M2 accelerated to 13,5% in the period March – May, from 13,1% in the period February – April 2006.

2. The monetary aggregate M2C should be treated with caution since the co-operative credit institutions are not supervised by the Central Bank of Cyprus and, in addition, the automation undertaken by the Co-operative Computers Society (SEM) Ltd, does not yet cover all the co-operative credit institutions.

Chart 6

M2 growth

(annual percentage change, monthly data)

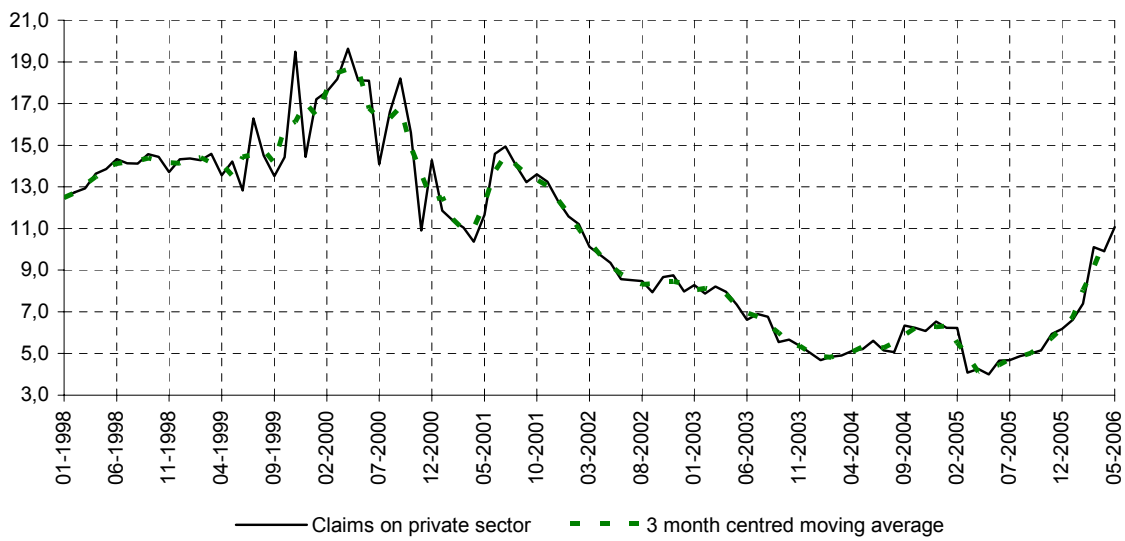


Source: Central Bank of Cyprus.

Chart 7

Growth of claims on private sector

(annual percentage change, monthly data)



Source: Central Bank of Cyprus.

Table 4 presents the annual percentage change of components and factors affecting total money supply. Regarding the components of M2, the narrow money aggregate M1 registered an annual increase of 26,9% in May, compared with 25,3% in April 2006 and 8,7% in May of the previous year. Quasi-money rose at an annual rate of 11,4% in May compared with 11,2% in April 2006 and 3,4% in May 2005. The marked difference between this year's and last year's growth rates is due to the substantial increase in time deposits in local currency in 2006. At the end of May quasi-money accounted for 81,6% of M2 while M1 accounted for 18,4%.

The annual rate of growth of residents' deposits in local currency rose by 12,1% in May 2006, compared with 1,7% in the same month of the previous year, partly due to the tax amnesty scheme in 2005. At the same time the annual growth rate of residents' foreign currency

deposits continued to be high. More specifically, the increase in residents' foreign currency deposits was 34,1% in the 12 months to May 2006, virtually unchanged from that exhibited during the same period of the previous year.

The acceleration in M2 growth was mainly due to the increase in net foreign assets and the rise in credit to the private sector. Credit to the private sector rose at an annual rate of 11,1% in May compared with 9,9% in April. In April and May 2005 the respective growth rates were 4,2% and 3,8%. The three-month moving average of credit growth was 10,4% in the period March – May compared with 9,1% in the period February – April. Credit to the public sector rose by 18,3% year-on-year to May 2006. In the year to May 2005 there was a decrease of 10,7%, reflecting the base effect as a result of the government's foreign borrowing via the eurobond (EMTN) issue in July 2004.

Table 4**Main monetary indicators**

	Outstanding amount as a percentage % of M2 ⁽¹⁾	Annual percentage change			
		2005 Apr.	2005 May	2006 Apr.	2006 May
Money supply (M1)	18,4	8,0	8,7	25,3	26,9
Currency in circulation	5,3	12,6	7,1	6,2	9,5
Demand deposits	13,1	5,6	9,5	35,8	35,6
Quasi-money	81,6	3,0	3,4	11,2	11,4
Total money supply (M2)	100,0	3,8	4,2	13,5	13,9
Claims on private sector		4,3	4,0	9,9	11,1
of which in foreign currency		20,0	17,7	41,1	52,0
Claims on public sector		-10,2	-10,7	20,2	18,3

Source: Central Bank of Cyprus.

(1) As at the end of the last month available.

The breakdown of bank credit by sector of economic activity (Table 5) shows that in the year to May personal/professional loans rose by 19,4% compared with 17,9% in April and 9,6% in May 2005. Credit to the construction sector rose at an annual rate of 16,6% in May, compared with 15,4% in April 2006 and 11,5% in May 2005.

It is noted that, via a circular to the banks dated 13 June 2006, the Governor of the Central Bank of Cyprus has drawn attention to the risks associated with the financing of real estate purchases. In addition, banks should take into account credible professional advice when evaluating property and compare different evaluations to see whether the amounts are

overstated. At the same time the circular emphasises that housing loans should not exceed 70% of the purchase value of the property and the land plot value on which the property will be constructed. Loans to first time buyers are exempted from this. In this case, financing can be extended up to 80% of the purchase value.

During the same period, there was a slight acceleration in the growth of credit to public corporations and institutions, including the government. Specifically, the aforementioned loans grew by 11,7%, compared with 11,5% in the 12 months to May 2006 and 4,1% in the 12 months to May 2005.

With the exception of tourism, the rest of the categories registered a fall. The largest share of total outstanding amounts at the end of May was maintained by personal/professional loans with

48,5%, followed by credit to the construction sector with 18,2% and foreign and domestic trade with 14,4%.

Table 5
Bank credit by sector⁽¹⁾

	Outstanding amount as a percentage % of total ⁽²⁾	Annual percentage change			
		2005 Apr.	2005 May	2006 Apr.	2006 May
Public institutions and corporations ⁽³⁾	3,06	5,8	4,1	11,5	11,7
Agriculture	1,00	0,4	-0,1	-8,4	-8,1
Mining	0,27	4,3	3,3	1,0	1,9
Manufacturing	5,09	0,1	0,5	-1,0	0,0
Transport and communications	0,94	-21,2	-18,7	-7,9	-5,9
Foreign and domestic trade	14,36	-4,8	-5,9	-2,9	-2,0
Building and construction	18,15	11,7	11,5	15,4	16,6
Tourism	8,55	2,4	1,3	1,7	3,1
Personal and professional loans	48,53	9,8	9,6	17,9	19,4
Bills discounted: local	0,03	-29,6	-15,7	24,1	-0,2
foreign	0,01	-22,9	-15,0	-44,6	-49,0
Total	100,00				

Source: Central Bank of Cyprus.

(1) This refers to loans in local and foreign currency, given to residents and non-residents of Cyprus.

(2) As at the end of the last month available.

(3) Including government loans.

Foreign currency lending to residents by domestic banks rose by £508,6 million in the 12 months to May 2006, compared with a rise of £147,5 million in the same period to May 2005. The share of new foreign currency loans to total new loans given out in the 12 months to May 2006 rose to 52,2%, compared with 43,6% in the same period of the preceding year. As a result, the share of new foreign currency loans to total loans outstanding at the end of May was 15,2%, compared with 11,1% at the end of May 2005 (Table 6). At the end of May 2006, 62,7% of foreign currency loans was accounted for by

euros, 28,4% by Swiss francs, 6% by dollars and 1,9% by yen, compared with 67,1%, 18,5%, 10,2% and 2,6%, respectively, at the end of May 2005. It is noted that the rise in lending in Swiss francs is due to the low interest rates in this currency. It appears that borrowers have been disregarding the exchange rate risk associated with such transactions, even though the exchange rate between the Swiss franc and the Cyprus pound has historically exhibited strong fluctuations.

Table 6
Claims on private sector ⁽¹⁾

	2003	2004	2005	2005 May	2006 Apr.	2006 May
<i>(outstanding amounts at end of period, CYP million)</i>						
Foreign currency loans to residents	799,0	909,9	1.205,8	978,7	1.379,9	1.487,3
Claims on private sector	8.302,0	8.844,2	9.390,8	8.800,2	9.696,3	9.773,9
Share %	9,6	10,3	12,8	11,1	14,2	15,2
<i>(12 month change, CYP million)</i>						
Foreign currency loans to residents	13,8	111,0	295,8	147,5	401,9	508,6
Claims on private sector	397,9	542,2	546,6	338,1	874,7	973,7
Share %	3,5	20,5	54,1	43,6	45,9	52,2

Source: Central Bank of Cyprus.

(1) From domestic banks.

According to data covering medium and long-term lending in foreign currency, during the period January – April 2006 64,6% of new loans was used for refinancing³, 12,9% for the purchase of fixed assets and 7,7% was used in the local construction sector. The respective figures for the same period of 2005 were 56,6%, 21,6% and 9,7%. Concerning the IBUs, during the period January – February loans to residents rose by £6,2 million, compared with net repayments of £15,3 million in the same period of the preceding year.

Domestic expenditure by holders of Cypriot credit cards rose at an annual rate of 26,8% in May 2006, compared with a mere 3% rise in the same month of 2005. During the first five

months of 2006 this type of expenditure rose by 16,2%, compared with 10,2% in the same period of the previous year. Expenditure by Cypriot cardholders abroad rose at an annual rate of 42,9% in May, compared with an increase of 18,1% in the same month of the previous year. During the period January – May 2006 this type of expenditure rose by 38,2%, compared with a rise of 19,1% in the same period of the previous year. Finally, foreign card holders' expenditure in Cyprus rose by 9,1% in May 2006, compared with a rise of 10,3% in the same month of the previous year. During the first five months of the current year this type of expenditure rose by 8% compared with an increase of 4,8% in the same period of 2005 (Table 7).

3. Refinancing refers to the repayment of existing loans in Cyprus pounds or the conversion of existing foreign currency loans into a different currency.

Table 7
Credit card transactions

	2004	2005	May		Jan.-May	
			2005	2006	2005	2006
Foreign cardholder spending in Cyprus						
Value (CYP thousand)	232.671	244.609	24.616	26.856	75.078	81.062
Annual % change	8,6	5,1	10,3	9,1	4,8	8,0
Local cardholder spending in Cyprus						
Value (CYP thousand)	591.912	659.486	47.741	60.543	243.872	283.296
Annual % change	12,3	11,4	3,0	26,8	10,2	16,2
Local cardholder spending abroad						
Value (CYP thousand)	195.009	244.131	18.126	25.894	89.433	123.606
Annual % change	9,3	25,2	18,1	42,9	19,1	38,2

Source: JCC Payment Systems.

Co-operative Credit Institutions (CCIs)⁴

During May local currency deposits with CCIs amounted to 37,9% of total deposits (in CCIs and banking institutions), compared with 37,4% in the same month of 2005. In May 2006 the share of CCI loans in local currency was estimated at around 29,9%, compared with 29,5% in the same month of 2005. Deposits with CCIs are estimated to have increased by 12% in the 12 months to May 2006, compared with 5,3% in the same period of the previous year. Regarding CCI loans, these are estimated to have risen by an annual rate of 8,4% in May 2006, compared with 10,8% in May 2005. The slowdown is mainly due to the fact that CCIs do not provide loans in foreign currency.

Money market

During May there was an increase in surplus bank liquidity⁵. The increase in the average daily value of net foreign assets and the decrease in net government deposits with the Central Bank, were the main factors that affected surplus liquidity positively (Table 8).

At the last auction for the acceptance of deposits held in June, £520 million was absorbed at an average interest rate of 2,78%.

4. The data for the CCIs are estimated by the Central Bank based on a sample of 210 CCIs, which make up about 96% of total deposits and loans.

5. The box on page 22 presents the liquidity conditions for the period 16 March – 21 June 2006. Any differences in the amounts are due to the different periods being analysed.

Table 8**Banking system's liquidity position***(CYP million, period averages of daily positions)*

	Liquidity - providing factors					Liquidity - absorbing factors						Credit institutions current accounts (MRA)	Base money (6+7+9+12) 13
	Net assets in gold and foreign currency (NFA)	Monetary policy operations				Deposit facility (overnight)	Other liquidity-absorbing operations (additional, special & S.M.E. dep.)	Rev-repos & depos	Currency in circulation	Central govern. deposits (net) ⁽¹⁾	Other factors (net)		
		Main refinancing operations (repos)	Long-term refinancing operations	Marginal lending facility (lombard)	Other liquidity providing operations (swap)								
	1	2	3	4	5	6	7	8	9	10	11	12	13
2004 May	1.038,5	0,0	0,0	6,0	0,2	8,0	79,3	0,0	509,8	-416,2	223,1	640,6	1.237,7
June	1.108,4	0,0	0,0	0,0	0,0	32,9	79,4	0,0	519,6	-374,9	214,7	636,8	1.268,6
July	1.340,1	0,0	0,0	0,0	0,0	42,1	79,5	61,2	533,4	-190,3	175,0	639,4	1.294,3
Aug.	1.499,7	0,0	0,0	0,0	0,0	44,5	79,4	151,6	536,1	-140,6	185,9	642,9	1.302,8
Sep.	1.429,8	0,0	0,0	2,0	0,0	31,9	79,3	162,7	531,1	-208,9	191,0	644,6	1.286,9
Oct.	1.393,1	0,0	0,0	0,0	0,0	24,3	79,4	121,1	529,0	-192,1	185,5	645,8	1.278,6
Nov.	1.376,0	0,0	0,0	0,0	0,0	15,8	79,3	82,2	516,3	-144,9	184,1	643,2	1.254,6
Dec.	1.441,6	0,0	0,0	10,0	0,0	12,9	79,3	0,0	543,5	-29,0	201,9	642,9	1.278,6
2005 Jan.	1.419,9	0,0	0,0	0,6	0,0	50,7	79,6	114,2	537,8	-142,3	139,9	640,8	1.308,8
Feb.	1.425,9	0,0	0,0	0,6	0,3	11,4	79,4	55,0	520,7	-36,0	149,0	647,3	1.258,8
Mar.	1.432,9	0,0	0,0	0,3	0,0	25,2	79,3	28,4	524,0	-48,4	178,9	646,2	1.274,8
Apr.	1.361,7	0,0	0,0	0,1	0,0	63,7	79,3	17,3	537,7	-191,8	208,2	647,7	1.328,1
May	1.395,2	0,0	0,0	0,0	0,0	33,4	79,3	72,9	554,6	-204,1	210,1	648,9	1.316,3
Jun.	1.510,9	0,0	0,0	6,2	0,1	36,2	79,7	68,3	568,4	-114,8	224,1	655,2	1.339,6
Jul.	1.571,9	0,0	0,0	0,4	0,0	31,9	79,6	88,1	586,5	-62,2	182,6	665,8	1.363,8
Aug.	1.596,2	0,0	0,0	0,0	0,0	37,7	79,4	93,5	587,6	-58,1	185,2	670,8	1.375,5
Sep.	1.638,9	0,0	0,0	0,0	0,0	87,5	79,4	198,7	579,4	-119,0	200,2	612,7	1.359,1
Oct.	1.712,1	0,0	0,0	7,3	0,0	55,1	79,3	168,1	579,7	-12,5	231,5	618,1	1.332,3
Nov.	1.772,0	0,0	0,0	0,0	0,0	181,7	79,3	173,7	566,4	-41,3	246,6	565,6	1.393,1
Dec.	1.830,5	0,0	0,0	0,0	0,0	198,5	79,3	227,7	594,8	-130,6	277,8	583,0	1.455,7
2006 Jan.	1.840,4	0,0	0,0	0,0	0,0	190,5	0,1	333,5	579,2	-148,0	223,8	661,1	1.430,9
Feb.	1.796,1	0,0	0,0	0,0	0,0	174,0	0,0	302,9	562,2	-154,2	236,9	674,3	1.410,5
Mar	1.792,1	0,0	0,0	0,9	0,0	238,8	0,1	256,1	564,8	-210,2	265,8	677,6	1.481,2
Apr.	1.845,7	0,0	0,0	0,0	0,0	183,3	0,0	138,7	594,7	-32,1	266,1	695,1	1.473,1
May	1.993,9	0,0	0,0	0,0	0,0	233,0	0,0	269,7	603,8	-78,0	271,3	694,2	1.531,0

Source: Central Bank of Cyprus.

(1) The negative sign of net central government deposits is due to the inclusion of the government loan amounting to £961,1 million. Following the prohibition of public sector financing by the Central Bank in July 2002, outstanding claims of the Central Bank on the government were converted into a loan with a maturity of 30 years, the repayment of which will commence in 2007.

As shown in Table 9, no auctions were held in government securities in May. During June, auctions were held in 13 and 52 week treasury bills as well as in five-year government bonds. The respective average yields were 2,46%, 2,79% and 3,87%.

The interbank overnight interest rate fell to 2,48% in May from 2,53% in April.

Table 9

Interest rates

(percent per annum, period averages)

	2003	2004	2005	2005 May	2006 Mar.	2006 Apr.	2006 May
Interbank (1 day)	3,35	3,92	3,27	3,47	2,52	2,53	2,48
Acceptance of deposits	3,45	3,89	3,28	3,71	2,64	2,40	2,34
Treasury bills (13 weeks)	3,51	4,21	4,26	-	-	-	-
Treasury bills (52 weeks)	3,70	4,77	4,29	-	2,92	-	-
Development stocks (2 years)	3,83	5,14	4,74	-	-	-	-
Development stocks (5 years)	4,49	5,92	5,68	-	3,72	-	-
Development stocks (10 years)	4,70	6,07	5,17	-	4,07	-	-
Development stocks (15 years)	4,81	6,31	5,61	-	-	-	-

Source: Central Bank of Cyprus.

BOX 2**Liquidity conditions and monetary policy operations**

This box reviews the Central Bank of Cyprus (CBC) liquidity management from 16 March to 21 June 2006. Figure 1 summarises the liquidity absorption and provision through monetary policy operations, while Figure 2 presents the developments in the main short-term interest rates.

Liquidity conditions in the banking system

The net liquidity impact of the autonomous factors, i.e. the factors not related to monetary policy operations, resulted in an increase in the liquidity position of the banking system.

Monetary policy operations and interest rates

The CBC conducted seven liquidity absorbing operations (LAOs) through auctions for the acceptance of deposits.

Open market operations

(CYP million; interest rates in percentages per annum)

Operation	Date of settlement	Date of maturity	Bids (amount)	Allotment (amount)	Bid-cover ratio	Weighted average allotment rate	Running for (...) days
LAO	16/03/2006	30/03/2006	508,5	280,0	1,82	2,69	14
LAO	30/03/2006	13/04/2006	260,5	110,0	2,37	2,43	14
LAO	13/04/2006	27/04/2006	366,0	140,0	2,61	2,39	14
LAO	27/04/2006	11/05/2006	434,5	220,0	1,98	2,36	14
LAO	11/05/2006	25/05/2006	536,0	280,0	1,91	2,35	14
LAO	25/05/2006	08/06/2006	691,0	320,0	2,16	2,32	14
LAO	08/06/2006	22/06/2006	627,5	400,0	1,57	2,31	14

Source: Central Bank of Cyprus.

The LAOs were carried out through variable rate tenders with a maximum bid rate of 3,25%. The absorbed liquidity ranged between £110 million and £400 million, whereas the weighted average allotment rate remained within the range of 2,31% and 2,69%. The ratio of the amount bid to the volume allotted, ranged between 1,57 and 2,61 with an average of 2,06, while the number of participating counterparties varied between 5 and 7.

Standing facilities

(period averages of daily recourse in CYP million)

Period	Deposit facility	Marginal lending facility
16/03 - 29/03/2006	277,1	0,0
30/03 - 12/04/2006	120,7	2,0
13/04 - 26/04/2006	216,5	0,0
27/04 - 10/05/2006	164,7	0,0
11/05 - 24/05/2006	240,6	0,0
25/05 - 07/06/2006	318,4	0,0
08/06 - 21/06/2006	286,0	0,0

Source: Central Bank of Cyprus.

In view of the aforementioned liquidity conditions during the above periods, averages of daily recourse to the deposit facility ranged between £120,7 million and £318,4 million. This is in contrast to the very limited recourse to the marginal lending facility for which the respective period averages ranged between zero and £2 million.

Figure 1. Monetary policy operations

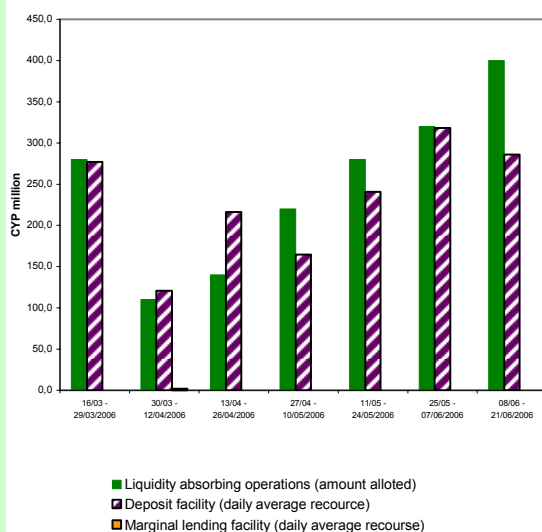
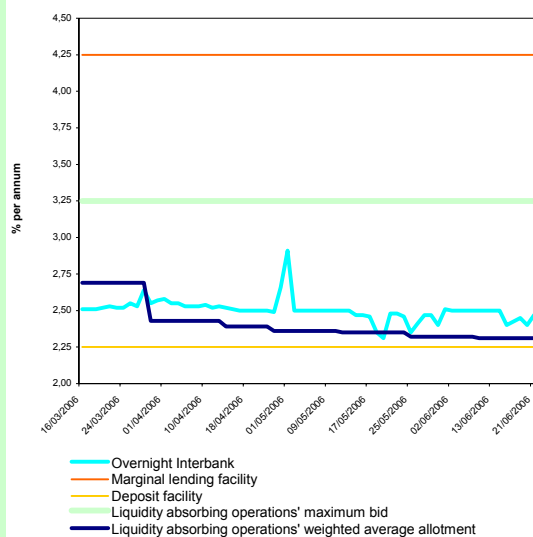


Figure 2. Interest rates



Overnight interbank interest rate

(percent per annum)

Period	Minimum rate	Maximum rate	Average rate
16/03 - 29/03/2006	2,51	2,64	2,53
30/03 - 12/04/2006	2,52	2,58	2,54
13/04 - 26/04/2006	2,50	2,52	2,50
27/04 - 10/05/2006	2,49	2,91	2,56
11/05 - 24/05/2006	2,31	2,50	2,45
25/05 - 07/06/2006	2,35	2,51	2,46
08/06 - 21/06/2006	2,40	2,50	2,47

Source: Central Bank of Cyprus.

During the period under review the overnight interbank interest rate ranged between 2,31% and 2,91%. The average rate stood at around 2,50%.

Table 10 provides a comparison between domestic and European long-term interest rates. The most recent data refer to the latest 12 month average until May 2006 and show

that domestic long-term real interest rates exceeded the corresponding euro area rates by 116 basis points, compared with 137 basis points in the previous 12 month period.

Table 10**Inflation and interest rates in Europe and Cyprus – May 2006***(latest 12-month average)*

	Inflation (HICP) (%)	Long-term interest rates (%)	Long-term real interest rates (%)
Austria	1,90	3,45	1,55
Belgium	2,60	3,48	0,88
Czech Republic	2,10	3,52	1,42
Denmark	2,00	3,43	1,43
Estonia ⁽¹⁾	4,20	3,94	-0,26
Finland ⁽¹⁾	1,10	3,33	2,23
France	2,00	3,46	1,46
Germany	2,10	3,41	1,31
Greece	3,40	3,68	0,28
Hungary	3,00	6,55	3,55
Ireland	2,50	3,40	0,90
Italy	2,30	3,66	1,36
Latvia	6,90	3,71	-3,19
Lithuania	2,90	3,69	0,79
Luxembourg	3,90	3,45	-0,45
Malta	2,80	4,39	1,59
Netherlands	1,60	3,44	1,84
Poland	1,30	4,95	3,65
Portugal ⁽¹⁾	2,40	3,54	1,14
Slovakia	3,50	3,64	0,14
Slovenia	2,40	3,74	1,34
Spain	3,70	3,44	-0,26
Sweden	1,20	3,35	2,15
United Kingdom	2,10	4,28	2,18
Eurozone	2,30	3,49	1,19
EU -25	2,30	3,71	1,41
Cyprus	2,00	4,35	2,35

Sources: Eurostat and European Central Bank.

(1) Data for April 2006.

International and domestic official interest rates

At their recent meetings the US Federal Reserve and the ECB raised their interest rates by 25 basis points. In contrast, the Bank of England maintained its interest rates unchanged. On 19

May the Central Bank of Cyprus also left its rates unaltered. As a result, the differential between domestic and European official interest rates decreased to 50 basis points (Table 11).

Table 11
Selected official interest rates

(percent per annum, changes in percentage points)

		change
European Central Bank		
<i>(8 June 2006)</i>		
Minimum bid rate on the main refinancing operations	2,75	+0,25
Interest rate on the marginal lending facility	3,75	+0,25
Interest rate on the deposit facility	1,75	+0,25
Bank of England		
<i>(8 June 2006)</i>		
Repo rate	4,50	-
Federal Reserve		
<i>(29 June 2006)</i>		
Federal funds rate	5,25	+0,25
Discount rate	6,25	+0,25
Central Bank of Cyprus		
<i>(19 May 2006)</i>		
Minimum bid rate on the main refinancing operations	3,25	-
Maximum bid rate on the liquidity absorbing operations	3,25	-
Interest rate on the marginal lending facility	4,25	-
Interest rate on the deposit facility	2,25	-

Sources: European Central Bank, Bank of England, Federal Reserve and Central Bank of Cyprus.

Cyprus Stock Exchange (CSE)

During most of May, the main and parallel market index of the CSE exhibited a downward trend mainly due to liquidations of shares in the banking sector (Chart 8). The index fluctuated between 2.432,6 and 3.017,5 reaching a monthly average of 2.749. During the first five months of the year the average value of the index was 2.375,8. The average daily value of transactions rose to £7,4 million, compared with £4,2 million in April. The average daily volume of transactions rose to 2.920 in May from 1.807 in the previous month. The companies with the

largest volume of transactions were Bank of Cyprus and Laiki Bank, accounting for 28,1% and 22,9% of the total volume, respectively.

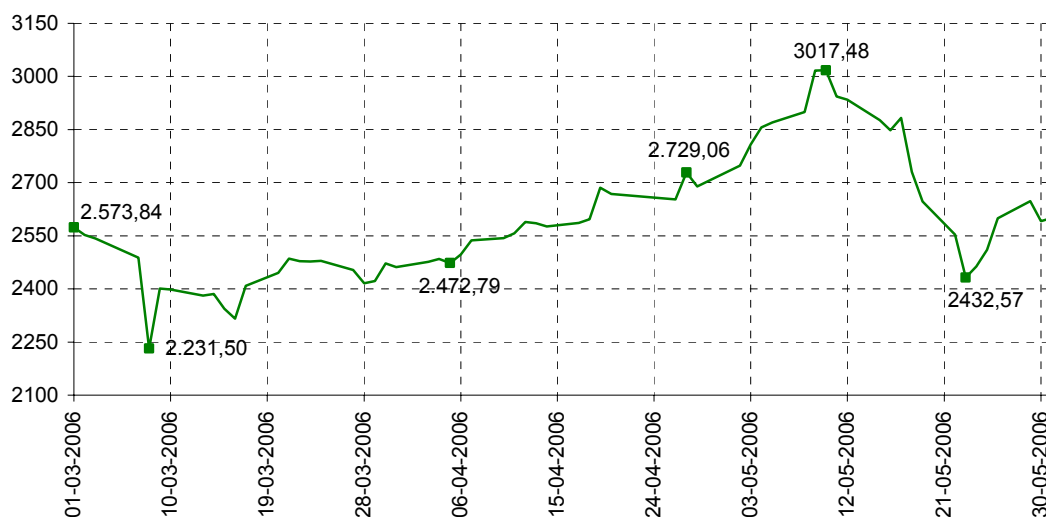
At the last meeting of the month, the main indices as well as the sectoral index of banks and hotels exhibited a fall compared with the previous month's closing.

An analysis of the purchases/sales of listed shares by non-residents is shown in the Annex (Table 13).

Chart 8

Cyprus Stock Exchange – main and parallel market index

(daily data, 3/9/2004=1000)



Source: Cyprus Stock Exchange.

2.3 INFLATION

The consumer price index recorded an increase of 3,13% in May 2006, compared with 2,96% in the previous month. Table 12 shows that the small increase in inflation in May, is mainly due to the acceleration in the prices of petroleum and domestic agricultural products. A small deceleration compared with the previous month was recorded in the prices of electricity and services. A further fall was recorded in the prices of non-petroleum imported products (including cars).

For the first five months of the year, inflation reached 2,84%. More specifically, domestic product prices rose by 4,77%, petroleum product prices rose by 14,03%, imported product prices fell by 1,29%, and services prices rose by 2,39%.

Table 12 shows that there was a deceleration in domestic product prices which rose by 20,7% in May 2006, compared with 24,25% in April 2006. In contrast, there was an acceleration in the prices of agricultural products, which rose by 9,68% in May, compared with 8,13% in the previous month.

Petroleum prices rose by 15,87% compared with 12,33% in April. Imported product prices (except petroleum products) declined by 1,63% in May, compared with a 1,4% decrease in April 2006. More specifically, the prices of motor vehicles declined by 0,23%, compared with 0,79% in April. At the same time, a further decline of 2,22% was recorded in the prices of other imported products. Finally, the prices of services rose by 2,63% in May compared with 2,68% in April 2006.

The Harmonised Index of Consumer Prices (HICP) recorded an increase of 2,5% in May, remaining unchanged from the previous month. The HICP 12 month moving average until May 2006 was 2,0%, which is lower than the 2,7% reference value of the Maastricht criteria for the specific month.

Table 12**Percentage change in the consumer price index by economic origin**

		2003	2004	2005	May 2005/ 2004	April 2006/ 2005	May 2006/ 2005	Jan.- May 2005/ 2004	Jan.- April 2006/ 2005	Jan.- May 2006/ 2005	Weights 1998=100 2005=100	
GENERAL INDEX		4,14	2,28	2,56	2,45	2,96	3,13	2,83	2,78	2,84	100,00	100,00
A	Imported products	7,30	5,03	3,90	3,10	5,23	5,39	3,83	4,61	4,77	36,69	28,60
A.1	Agricultural	4,54	3,32	1,34	-3,49	8,13	9,68	1,03	3,83	5,00	7,93	6,92
A.2	Industrial	6,46	3,36	1,14	1,24	2,01	2,12	1,79	2,49	2,41	22,91	19,24
A.3	Electricity	10,20	-3,13	11,51	10,17	24,25	20,70	3,57	25,86	24,83	1,52	2,44
B	Petroleum products	14,16	17,18	14,82	16,63	12,33	15,87	15,41	13,57	14,03	4,33	6,44
C	Imported products	-2,38	-5,55	-2,47	-1,89	-1,40	-1,63	-2,24	-1,20	-1,29	22,20	25,31
C1	Motor vehicles	-8,31	-13,50	-2,42	-1,99	0,79	-0,23	-1,96	0,47	0,33	9,43	6,15
C2	Other imported	1,81	-0,39	-2,49	-1,84	-2,21	-2,22	-2,39	-1,90	-1,97	12,77	19,16
D	Services	4,38	3,23	3,34	3,60	2,68	2,63	3,99	2,36	2,39	41,11	39,65
HICP		4,0	1,9	2,1	2,0	2,5	2,5	2,4	2,4	2,4		

Table 13

Inflation : Cyprus and other countries

(annual percentage change in consumer prices)

	Inflation rate	Month	Forecast for 2006 ⁽¹⁾
Austria	1,7	May	1,8
Belgium	2,2	May	2,0
Canada	2,4	Apr.	2,3
Cyprus	3,1	May	2,5 ⁽²⁾
Denmark	2,0	May	2,0
Euro area	2,5	May	2,1
France	2,1	May	1,8
Germany	1,9	May	1,7
Italy	2,2	May	2,1
Japan	0,4	Apr.	0,5
Spain	4,0	May	3,5
Sweden	1,6	May	1,3
Switzerland	1,4	May	1,2
UK	2,2	May	2,0
USA	4,2	May	3,3

(1) Source: *The Economist*, 17 June 2006

(2) Source: Central Bank of Cyprus.

For purposes of comparison, Table 13 shows the final monthly data and prospects for 2006 for inflation in Cyprus, the eurozone and other industrial countries. As explained in more detail in the section concerning the economy, inflation in 2006 is expected to move at the same levels as in 2005.

2.4 PRODUCTION, DEMAND AND THE LABOUR MARKET

The growth rate of real GDP reached 3,3% in the first three months of 2006 compared with 3,9% in the same period of 2005. More specifically, private consumption exhibited an increase of 4,4% compared with 5,6% the same period of 2005. Public consumption rose by 11,9% compared with 0,6% in the same period of the previous year. At the same time investment in fixed assets as well as exports and imports of goods and services, rose by 0,4%, 1,4% and 2,4%, respectively, compared with 10,7%, 1,9% and 7,8%, respectively, during the same period of 2005. Registered unemployment, as a percentage of the economic active population, rose to 3,8% in the first five months of 2006, compared with 4,1% in the same period of 2005.

Production

In the services sector, tourist arrivals registered an increase of 2,5% in the first five months of 2006, compared with an increase of 5,6% in the same period of 2005. Receipts from tourism rose by 2,5% in the first four months, compared with a fall of 4,7% in the corresponding period of 2005. In the secondary sectors, the manufacturing production index fell by 1,9% in the first three months of 2006, compared with a decrease of 2,9% in the corresponding period of 2005.

At the same time, in the construction sector the volume index of building permits fell by 0,7% in the first three months of 2006, compared with an increase of 17,8% in the same period of 2005. Cement sales fell by 6,8% in the first four months of 2006, compared with an increase of 15,4% in the same period of 2005.

Table 14

Manufacturing production volume index

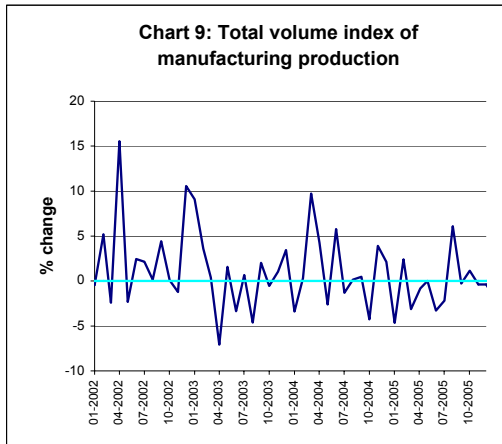
(percentage change by category)

	March 05/04	March 06/05	Jan-Mar 05/04	Jan.-Mar. 06/05
General index	-3,3	-2,7	-2,9	-1,9
Food products, beverages & tobacco	-1,8	-14,2	-0,3	0,3
Textiles & textile products	-15,0	-7,1	-17,8	21,6
Leather & leather products	-71,2	12,7	-55,9	-6,7
Wood & wood products	5,7	2,5	-0,2	0,2
Paper, paper products, publishing & printing	-2,4	4,5	-4,3	4,5
Refined petroleum products	-96,7	-8,0	-96,9	-1,4
Chemicals, chemical products & man-made fibres	1,8	10,6	1,7	-1,6
Rubber & plastic products	-9,6	0,2	-9,6	10,6
Other non-metallic mineral products	1,3	-0,8	8,8	-8,1
Basic metals & fabricated metal products	-8,9	2,1	-10,7	11,9
Machinery & equipment n.e.c.	6,7	2,0	7,6	-7,1
Electrical & optical equipment	6,8	17,2	2,8	-2,7
Transport equipment	1,2	-4,2	-4,5	4,7
Manufacturing n.e.c.	-4,5	1,2	-5,7	6,1

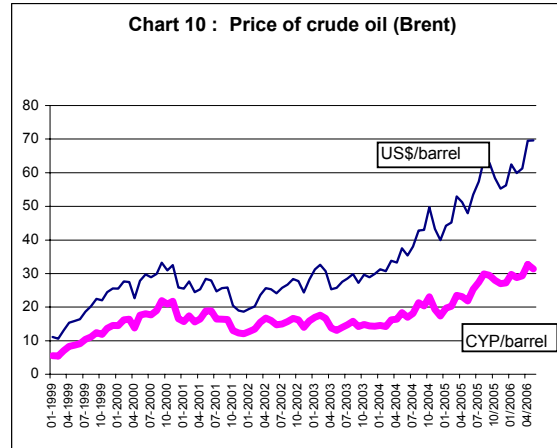
Source: Cystat.

Charts 9 - 12

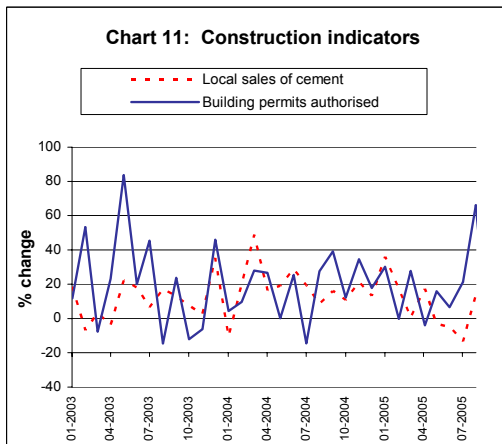
Selected economic indicators



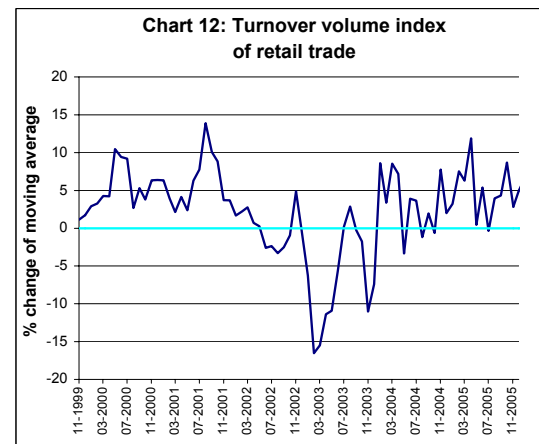
Source: Cystat.



Source: Reuters.



Source: Cystat.



Source: Cystat.

Consumption

The turnover volume index of retail trade, from which the sales of motor vehicles are excluded, exhibited a rise of 6,6% and 4,3% in the first and second month of 2006

respectively. For the first two months of the year, this index rose by 5,5% compared with 5,3% increase in the same period of 2005.

Table 15

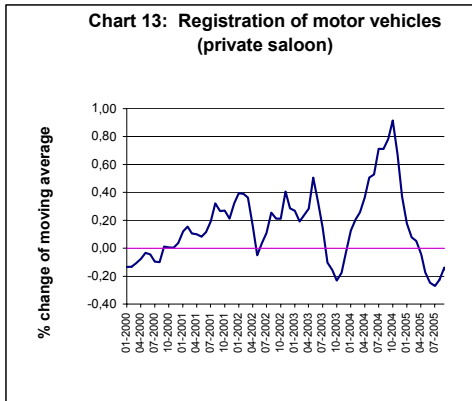
Turnover volume index of retail trade

(percentage change by category)

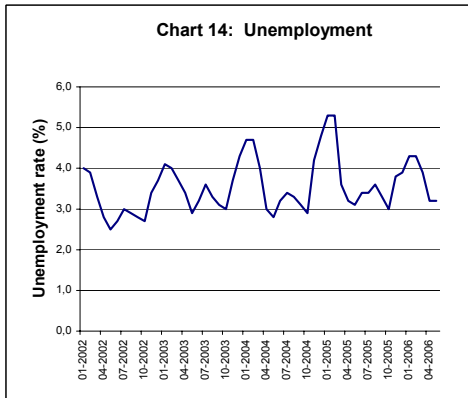
	February 05/04	February 06/05	Jan-Feb 05/04	Jan.-Feb. 06/05
General index	7,53	4,20	5,27	5,49
Retail sale in non-specialised stores with food, beverages or tobacco predominating	14,22	6,30	11,15	-10,03
Other retail sale in non-specialised stores	6,22	-2,20	3,07	-2,98
Retail sale of food, beverages and tobacco in specialised stores	0,32	4,70	4,05	-3,90
Retail sale of pharmaceutical and medical goods, cosmetics and toilet articles	5,85	25,00	15,18	-13,18
Retail sale of textiles, clothing, footwear and leather goods	0,86	1,90	2,22	-2,17
Retail sale of furniture, lighting equipment and household articles, electrical household appliances and radio and television goods hardware, paints and glass	13,36	5,00	9,26	-8,48
Retail sale of books, newspapers and stationery and other retail sale in specialised stores	-4,51	1,30	-4,27	4,46
Retail sale of second-hand goods in stores	-32,47	3,10	-30,37	43,62
Retail sale not in stores	23,26	2,80	-3,84	4,00

Source: Cystat.

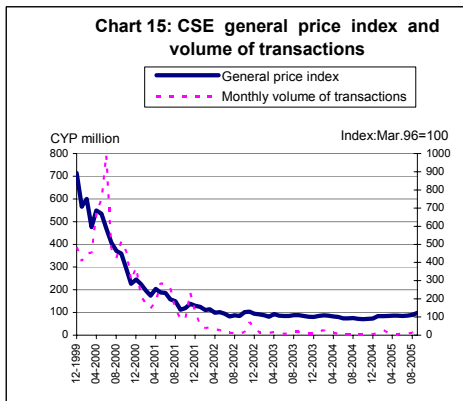
Charts 13 -15
Selected economic indicators



Source: Cystat.



Source: Cystat.



Source: Cystat.

Due to the base effect following the reduction in excise taxes that took place in November 2003, saloon car registrations exhibited a fall of the order of 17,2% in 2005, compared with an increase of 50,4% in the previous year. The reduction in car registrations continued in the first five months of 2006, and reached 6,5%. Despite the above decline in car registrations, private consumption in general, continued an upward trend during 2006.

As already mentioned, the consumption of Cypriots and foreigners using credit cards in Cyprus exhibited an acceleration and rose by 16,2% and 8% respectively, in the period January-May 2006 compared with an increase of 10,2% and 4,8% respectively in the same period of 2005.

Labour market

The most recent data concerning unemployment based on the Labour Force Survey cover the period until the end of 2005. According to the Survey, in 2005 unemployment exhibited a marginal increase of 4,8% compared with 4,7% in 2004. As far as the number of registered unemployment is concerned, a rise of 4,1% was recorded in May 2006 while the unemployment rate, as a percentage of the economically active population, fluctuated of 3,2% compared with 3,1% in May 2005.

In the first five months of 2006, the number of registered unemployed fell by 5,9% compared with an increase of 8,6% in the same period of 2005, while unemployment as a percentage of the economically active population, fluctuated at around 3,8% compared with 4,1% in the corresponding period of 2005.

The decrease in unemployment occurred due to the change in the methodology concerning the registration of the seasonally unemployed and as a result of a change in fundamentals. For example, those unemployed in the hotel industry are no longer obliged to be registered in order to be eligible for unemployment benefit.

Confidence indicators

The trends in the confidence indicators are to a certain extent consistent with the overall picture of the economy as presented in this report.

In the first five months of 2006, the construction confidence indicator exhibited a negative movement, which is consistent with the deceleration of the volume index of building permits and the cement sales.

The negative trend observed in the services confidence indicator, during the period January - May 2006, partly reflects the weak performance of the tourism sector in the first months of 2006.

In the first five months of 2006, the consumer confidence indicator and the retail sales confidence indicator remained negative. These negative indicators are not consistent with observed consumer spending.

The industrial confidence indicators exhibited a small increase in the period January – May 2005.

2.5 PUBLIC FINANCES

As regards public finance developments, the preliminary results of the consolidated accounts covering the central government and the social security funds for the first four months of 2006 have been released. If we exclude the £105 million of proceeds emanating from temporary measures, the fiscal balance has improved by around 0,7 percentage points compared with the corresponding period of 2005. In absolute numbers and excluding the 2005 revenue from the aforementioned temporary measures, a fiscal deficit of £24 million or 0,3% of GDP was recorded compared with a surplus of £53,8 million or 0,7% of GDP in the corresponding first four months of 2005. Public debt was contained at 69,4% of GDP compared with 69,6% in the corresponding period of 2005.

If we exclude the temporary receipts during the first four months of 2005, then total tax revenue increased by 13,2%. This includes revenue from direct taxes and non-tax revenue, which recorded increases of 28,2% and 48,4%, respectively. Including the temporary receipts, the above categories present reductions of the order of 2%, 1,1%, 17,2% and 9,4% respectively, as stipulated in Table 15 of the annex.

It is noted that the aforementioned increase in revenue from direct taxes includes almost a doubling of receipts from land and survey fees (£8,2 million compared with £4,7 million in the previous year). A large increase was also

observed in the dividends received from legal entities (£19,6 million compared with £3,9 million in 2005) as a result of legislation enacted in 2002 providing for the taxation of undistributed profits. The same category, however, includes a reduction by £2,7 million in the tax receipts emanating from international business companies, as well as a reduction of £3,7 million due to changes in the classification of road taxes for certain types of vehicles.

As regards indirect taxes, an increase of 6,7% was recorded, amounting to £403,7 million. This includes reduced income from import duties (-76,6%) and excise duties (-4,2%) as well as the 10,2% increase in VAT receipts, mainly as a result of the accelerated rate of growth of the economy and the broadening of the VAT tax base. Also, increased receipts emanating from land and survey fees enhanced indirect taxes by 77,4% (£16,5 million compared with £9,3 million in 2005).

As regards public expenditure, a total increase of 7,1% was recorded, which reflects the 8,8% rise in wages and salaries, mainly as a result of the incorporation of the 2,38% COLA increase as well as the granting of 2% contractual salary increases as from 1 January 2006 to public service employees. Payments towards goods and services also rose by 28,2% or £67,5 million and included ad hoc purchases, such as medication, medical services and water. Also, payments were effected towards road and public property maintenance. The broad category of

current transfers⁶ on the other hand, experienced changes leading to an increase of 9,2%, reaching £269,3 million compared with £246,7 million in the corresponding first four months of 2005. More specifically, payments towards pensions and gratuities fell by 5,2% as a result of the adoption of the gradual extension of the retirement age in the civil service, as from 1 July 2005. The contributions of the Cyprus government

towards the EU Budget reached £29,9 million and subsidies of £18,3 million were granted with respect to educational grants. Finally, it is noted that the preliminary data for the general government sector (which include the accounts of the general government and the semi-government organisations) covering the first six months of 2006, are expected to be published in mid-August 2006.

6. This includes: pensions and gratuities, social pensions, child and student allowances, public aid, grants to semi-governmental organizations and local authorities as well as contributions to the EU Budget.

2.6 EXTERNAL TRANSACTIONS

Goods

An overview of the trade balance for the period January-April 2006 is given in Table 17 which is based on preliminary data published by Cystat. Since May 2004, the collection of data on intra-EU trade has been undertaken using a new methodology introduced by Eurostat, for all European countries.

During the period January-April, the value of total imports of goods recorded a significant increase of 13,5%, compared with a marginal increase of 0,3% recorded in the corresponding period of 2005. The significant increase in the value of imports is partly the result of the significant increase in the international price of oil. Total exports of goods recorded a 5,7% increase during the period January - April compared with a 31,2% increase in the corresponding period of 2005.

As a result of the above, the trade balance deteriorated, registering a deficit of £799,9 million during the period January – April compared with a deficit of £690,3 million in the corresponding period of 2005.

Tourism

Tourist arrivals, shown in Table 18, decreased by 2,5% in the period January - May 2006, compared with a 5,6% increase in the corresponding period of 2005.

Revenue from tourism increased by 2,5% in the period January - May 2006, compared with a 4,7% decrease in the corresponding period of 2005, indicating an increase in per capita expenditure.

Table 16**Trade balance data**

(CYP million)

Period	TOTAL TRADE		EXTRA-EU TRADE		INTRA-EU TRADE	
	Total Imports/ Arrivals (cif)	Total Exports/ Dispatches (fob)	Total Imports (cif)	Total Exports (fob)	Arrivals (cif)	Dispatches (fob)
2000	2.402,0	591,9	1.140,9	364,5	1.261,1	227,4
2001	2.528,7	627,9	1.208,8	376,5	1.320,0	251,4
2002	2.486,6	511,3	1.140,9	240,9	1.345,8	270,4
2003	2.304,1	476,8	992,8	198,3	1.311,3	278,5
2004	2.679,3	548,0	921,7	202,5	1.757,6	345,5
2005	2.966,8	719,2	952,9	224,3	1.965,4	447,8
2005						
January	195,2	42,4	62,9	14,6	132,3	27,8
February	214,9	46,8	76,5	18,6	138,5	28,2
March	256,5	57,9	74,0	22,5	182,5	35,4
April	230,7	59,8	78,1	18,6	152,6	41,3
May	239,0	56,1	74,5	16,0	164,5	40,1
June	234,7	56,7	85,3	18,9	149,4	37,8
July	239,5	58,7	78,6	18,9	160,9	39,8
August	221,0	52,8	64,5	17,3	156,2	35,5
September	270,5	69,9	94,8	15,4	175,7	54,5
October	283,5	72,5	93,9	16,2	189,6	56,3
November	307,9	88,5	115,1	27,7	192,8	60,9
December	273,3	56,9	74,6	17,0	198,8	40,0
2006						
January	247,3	52,0	80,8	13,8	166,5	38,2
February	237,1	49,1	83,3	17,1	153,6	31,9
March (p)	260,3	56,7	91,1	22,5	169,2	34,2
Jan. - Apr. 2003	740,6	153,2	318,2	61,6	422,4	91,7
Jan. - Apr. 2004	894,8	157,7	382,7	57,9	512,1	99,9
Jan. - Apr. 2005	897,3	207,0	291,4	74,3	605,8	132,7
Jan - Apr. 2006 (p)	1.018,6	218,7	341,7	74,5	676,8	144,3
% change Jan. - Apr. 2004/2003	20,8	2,9	20,3	-6,0	21,2	9,0
% change Jan. - Apr. 2005/2004	0,3	31,2	-23,8	28,3	18,3	32,9
% change Jan. - Apr. 2006/2005 (p)	13,5	5,7	17,2	0,3	11,7	8,7

Source :Cystat

Note: Care should be taken when comparing data for May 2004 onwards with pre-May 2004 data due to methodological changes resulting from accession to the EU. Figures are not strictly comparable since data prior to May 2004 for intra-EU and extra-EU trade on arrivals/imports are recorded by country of origin while for dispatches/exports by country of final destination, whereas data for May 2004 onwards for intra-EU trade on arrivals are recorded by country of consignment and for dispatches by country of dispatch. Intra-EU trade refers to trade with EU 25 Member States, while extra-EU trade refers to trade with third countries. "Arrivals" denote goods within the European Union which enter the statistical territory of Cyprus and "Dispatches" denote goods which leave the statistical territory of Cyprus in order to enter another Member State. Data on countries and territories not specified and stores and provisions prior to May 2004 are included in extra-EU trade.

Balance of payments

Table 14 of the Annex presents preliminary data regarding the balance of payments for 2005. This data, which was compiled by the Central Bank, reveals a worsening of the current account deficit in 2005 compared with the deficit recorded in 2004.

The current account deficit in 2005, based on preliminary data, reached £453 million compared with £416,3 million in 2004.

As far as the income account is concerned, a net deficit of £258,5 million was recorded in 2005 compared with a £285,2 million deficit in 2004. This was the result of an improvement in the subcategories of “compensation of employees” and “investment income”.

The services surplus, excluding tourism, reached £1.109,6 million in 2005, compared with £1.008,7 million in 2004. A positive performance was recorded by the “transportation” and “financial services” sectors, while a somewhat weaker performance was recorded by “other business services”

The surplus in the travel account reached £684,9 million in 2005 compared with £676,2 million in 2004. Nevertheless, the increase in overseas travel by Cypriots as well as the significant increase in their expenditures are considered to be substantial.

Table 17**Tourist arrivals⁽¹⁾***(number of persons)*

	2000	2001	2002	2003	2004	2005	2006	% change 2003/2002	% change 2004/2003	% change 2005/2004	% change 2006/2005
January	63.553	64.214	54.067	59.529	56.504	58.894	54.875	10,1	-5,1	4,2	-6,8
February	87.243	83.569	71.950	77.972	75.705	72.600	66.151	8,4	-2,9	-4,1	-8,9
March	135.487	137.578	138.625	91.634	111.946	137.075	107.071	-33,9	22,2	22,4	-21,9
April	221.785	237.228	180.481	169.891	191.251	183.561	206.548	-5,9	12,6	-4,0	12,5
May	299.355	324.901	279.070	231.527	261.646	284.132	283.513	-17,0	13,0	8,6	
June	302.011	322.835	293.192	262.100	264.799	282.652		-10,6	1,0	6,7	
July	362.299	373.385	327.404	318.143	305.978	338.972		-2,8	-3,8	10,8	
August	356.686	371.536	301.724	325.390	305.926	336.587		7,8	-6,0	10,0	
September	329.964	329.400	306.731	287.358	303.506	302.833		-6,3	5,6	-0,2	
October	300.597	269.744	275.840	271.980	278.976	292.273		-1,4	2,6	4,8	
November	133.500	107.454	111.327	123.800	114.048	104.822		11,2	-7,9	-8,1	
December	93.722	74.887	77.822	83.919	78.723	75.656		7,8	-6,2	-3,9	
Jan. - Dec.	2.686.202	2.696.731	2.418.233	2.303.243	2.349.008	2.470.057		-4,8	2,0	5,2	
Jan-May	807.423	847.490	724.193	630.553	697.052	736.262	718.158	-12,9	10,5	5,6	-2,5

Source: Cystat.

*(1) Arrivals of same-day visitors are not included.***Table 18****Receipts from tourism⁽¹⁾***(CYP million)*

	2000	2001	2002	2003	2004	2005	2006	% change 2004/2003	% change 2005/2004	% change 2006/2005
January	-	24,9	21,6	25,6	21,8	20,7	21,2	-15,0	-5,0	2,4
February	-	29,1	28,9	31,4	25,4	23,5	23,1	-19,1	-7,5	-1,7
March	-	49,7	59,2	37,8	42,1	47,6	38,9	11,2	13,2	-18,3
April	-	89,9	77,0	67,1	72,1	62,0	74,5	7,4	-14,0	20,2
May	-	139,1	119,5	92,5	99,5	105,4		7,6	5,9	
June	122,9	157,4	139,3	114,8	109,3	113,3		-4,8	3,7	
July	162,7	192,0	160,7	152,4	135,1	140,1		-11,4	3,7	
August	173,7	205,0	153,8	165,3	148,1	161,3		-10,4	8,9	
September	161,9	176,3	157,4	134,1	141,2	137,9		5,3	-2,3	
October	135,1	130,2	128,0	112,4	115,9	120,5		3,1	4,0	
November	54,1	48,8	51,4	48,7	43,1	43,1		-11,5	0,0	
December	36,2	29,2	35,6	32,9	28,8	30,3		-12,4	5,2	
Jan. - Dec.	-	1.271,6	1.132,4	1.015,0	982,3	1.005,7		-3,2	2,4	
Jan. - Apr.	-	193,6	186,6	162,0	161,3	153,8	157,7	-0,4	-4,7	2,5

Source: Cystat.

(1) Receipts from same-day visitors are not included.

2.7 PROSPECTS FOR 2006

In 2006 GDP is expected to grow at about 3,8%, the same as in 2005. However, if the price of oil remains at the currently high levels, the growth rate will be slightly restrained. In 2006 domestic demand is expected to play a major role due to the anticipated improvement in the international environment, as confirmed by recent forecasts published by the European Commission. As regards the labour market, the rise of real GDP is expected to lead to stabilization of the registered unemployed, provided that the increase of foreign workers in Cyprus remains at the same levels.

Inflation during 2006 is expected to reach the same levels as 2005. Any fluctuations in the oil prices will lead to fluctuations in inflation. The continuation of competition in the retail trade sector, following Cyprus's accession to the EU, as well as monetary developments will have a significant impact on the inflation rate.

Even with the optimistic scenario the oil remaining at around \$70 per barrel, the HICP is expected to remain below the reference value of the Maastricht criteria. This estimation is compatible with the recent assessment of the European Commission .

Up until May 2006, 12 month moving average HICP was around 2,0% compared with the relevant Maastricht criterion of 2,7% for May 2006.

In 2006 the balance of payments deficit is expected to rise slightly compared with 2005, mainly as a result of recent revised estimates for oil prices.

In accordance with the Ministry of Finance forecasts, the fiscal deficit during 2006 is expected to fluctuate at around 2% of GDP, whereas the public debt is expected to be around 67% of GDP. An important development is the anticipated abrogation of Cyprus from the excessive deficit procedure on the basis of the fiscal indicators as well as the overall positive economic developments. The government forecasts and evaluations are analysed in the Convergence Programme 2005-2009 and are generally in line with those of the European Commission.

3. ANNEX

Table 1
Monetary aggregates and counterparts

(outstanding amounts at end of period, CYP thousand)

	2005 Apr.	2005 May	2006 Apr.	2006 May
Money supply (M1)	1.454.135	1.501.530	1.822.076	1.904.705
Currency in circulation	516.019	502.865	548.131	550.535
Demand deposits	852.770	902.014	1.164.326	1.231.260
Deposits in foreign currency	85.346	96.651	109.619	122.910
Quasi-money	7.533.750	7.599.463	8.375.301	8.464.345
Saving deposits	320.111	320.094	374.727	383.045
Time deposits	6.539.846	6.572.396	7.069.796	7.126.907
Deposits in foreign currency	673.793	706.973	930.778	954.393
Total money supply (M2)	8.987.885	9.100.993	10.197.377	10.369.050
Net foreign assets	1.053.069	1.129.188	1.807.220	1.872.012
Claims on private sector	8.821.559	8.800.184	9.696.255	9.773.912
of which in foreign currency	977.952	978.731	1.379.852	1.487.334
Claims on public sector	1.871.356	1.906.128	2.248.694	2.255.018
Unclassified items	-2.758.099	-2.734.507	-3.554.792	-3.531.892

Source: Central Bank of Cyprus.

Table 2
Bank credit by sector⁽¹⁾

(outstanding amounts at end of period, CYP thousand)

	2005 Apr.	2005 May	2006 Apr.	2006 May
Public institutions and corporations ⁽²⁾	287.670	285.460	320.754	318.925
Agriculture	114.136	113.020	104.584	103.888
Mining	28.153	27.689	28.429	28.212
Manufacturing	538.169	530.344	532.912	530.430
Transport and communications	105.701	104.242	97.301	98.069
Foreign and domestic trade	1.554.296	1.525.978	1.509.138	1.495.514
Building and construction	1.602.143	1.620.978	1.848.506	1.890.654
Tourism	881.485	863.729	896.777	890.169
Personal and professional loans	4.223.413	4.235.225	4.979.553	5.054.910
Bills discounted: local	2.909	3.342	3.610	3.335
foreign	2.161	2.476	1.198	1.263
Total	9.340.236	9.312.483	10.322.762	10.415.369

Source: Central Bank of Cyprus.

(1) This refers to loans in local and foreign currency, given to residents and non-residents of Cyprus.

(2) Including government loans.

Table 3
Official interest rates
(percent per annum)

Date of monetary policy decision	Deposit facility	Open market operations			Marginal lending facility	
		Main refinancing operations	Liquidity absorbing operations			
		Repo operations	Reverse repo operations	Acceptance of deposits operations ⁽¹⁾		
		Minimum bid rate	Maximum bid rate	Maximum bid rate		
2001	10 Aug.	3,50	5,00	5,00	-	6,50
	18 Sep.	3,00	4,50	4,50	-	6,00
	02 Nov.	2,50	4,00	4,00	4,00	5,50
2002	13 Dec.	2,50	3,75	3,75	3,75	5,00
2003	04 Apr.	2,50	3,50	3,50	3,50	4,50
2004	30 Apr.	3,50	4,50	4,50	4,50	5,50
2005	25 Feb.	3,25	4,25	4,25	4,25	5,25
	20 May	2,75	3,75	3,75	3,75	4,75
	09 Jun.	2,25	3,25	3,25	3,25	4,25

Source: Central Bank of Cyprus.

(1) The first operation for the acceptance of deposits was conducted on 9 October 2001 with a maximum bid rate of 4,50%.

Table 4
Open market operations allotted through tenders - liquidity absorbing operations ⁽¹⁾
(CYP million, interest rates in percent per annum)

Date of settlement	Bids (amount)	Allotment (amount)	Variable rate tenders				Running for (...) days	
			Maximum bid rate	Weighted average allotment rate	Minimum allotment rate	Maximum allotment rate		
2005	10 Nov.	417,5	250,0	3,25	2,91	2,48	3,12	14
	24 Nov.	396,5	180,0	3,25	2,53	2,50	2,54	14
	08 Dec.	411,0	200,0	3,25	2,48	2,48	2,49	14
	22 Dec.	455,5	300,0	3,25	2,54	2,43	3,25	14
2006	05 Jan.	533,5	300,0	3,25	2,46	2,44	2,49	14
	19 Jan.	604,0	380,0	3,25	2,41	2,39	2,43	14
	02 Feb.	544,0	300,0	3,25	2,37	2,36	2,37	14
	16 Feb.	477,0	300,0	3,25	2,71	2,32	3,25	14
	02 Mar.	414,0	250,0	3,25	2,58	2,46	2,69	14
	16 Mar.	508,5	280,0	3,25	2,69	2,46	3,00	14
	30 Mar.	260,5	110,0	3,25	2,43	2,43	2,44	14
	13 Apr.	366,0	140,0	3,25	2,39	2,38	2,41	14
	27 Apr.	434,5	220,0	3,25	2,36	2,34	2,37	14
	11 May	536,0	280,0	3,25	2,35	2,33	2,35	14
	25 May	691,0	320,0	3,25	2,32	2,26	2,33	14
	08 Jun.	627,5	400,0	3,25	2,31	2,29	2,32	14
22 Jun.	622,5	520,0	3,25	2,78	2,30	3,22	14	

Source: Central Bank of Cyprus.

(1) Since 9 October 2001, open market operations for the absorption of liquidity have been conducted through auctions for the acceptance of deposits (depos).

Table 5
Money market interest rates

(percent per annum, period averages)

	Cyprus					Euro area				
	Overnight deposits	2-7 days deposits	1-month deposits	1-6 months deposits	6-12 months deposits	Overnight deposits (EONIA)	1-month deposits (EURIBOR)	3-month deposits (EURIBOR)	6-month deposits (EURIBOR)	12-month deposits (EURIBOR)
2005 Apr.	3,83	4,14	4,55	-	5,15	2,08	2,10	2,14	2,17	2,27
May	3,47	4,10	-	4,30	5,10	2,07	2,10	2,13	2,14	2,19
June	3,11	3,49	3,31	3,75	-	2,06	2,10	2,11	2,11	2,10
July	2,70	3,12	2,85	3,44	-	2,07	2,11	2,12	2,13	2,17
Aug.	2,75	3,01	2,90	-	4,10	2,06	2,11	2,13	2,16	2,22
Sep.	2,55	2,91	2,83	-	-	2,09	2,12	2,14	2,17	2,22
Oct.	2,85	2,99	2,87	3,98	-	2,07	2,12	2,20	2,27	2,41
Nov.	2,62	2,84	2,90	5,75	-	2,09	2,22	2,36	2,50	2,68
Dec.	2,51	2,85	2,95	3,31	-	2,28	2,41	2,47	2,60	2,78
2006 Jan.	2,51	3,07	3,12	3,07	-	2,33	2,39	2,51	2,65	2,83
Feb.	2,48	2,90	2,98	4,33	3,38	2,35	2,46	2,60	2,72	2,91
Mar.	2,52	2,84	3,02	2,97	3,35	2,52	2,63	2,72	2,87	3,11
Apr.	2,53	2,80	2,95	3,64	3,35	2,63	2,65	2,79	2,95	3,22
May	2,48	3,23	3,22	3,44	3,55					

Sources: Central Bank of Cyprus and European Central Bank.

Table 6**Interest rates of commercial banks^(1,2)***(percent per annum)*

	Lending rates					Deposit rates		
	Enterprises: overdraft within limits	Enterprises: secured loans	Personal: secured loans	Housing: loans secured by assignment of life policy	Credit cards	Current accounts	3 month notice - over CYP5.000	1 year fixed deposits - over CYP5.000
2004 Apr.	6,92	6,90	7,53	6,30	10,50	0,42	3,35	3,40
May	7,92	7,90	8,53	7,30	11,50	0,69	4,41	3,88
June	7,92	7,90	8,53	7,30	11,50	0,66	4,42	4,04
July	7,92	7,90	8,53	7,30	11,50	0,66	4,43	4,08
Aug.	7,92	7,90	8,53	7,30	11,50	0,67	4,61	4,11
Sep.	7,92	7,92	8,55	7,30	11,50	0,66	4,44	4,14
Oct.	7,92	7,92	8,55	7,30	11,50	0,66	4,44	4,18
Nov.	7,92	7,92	8,55	7,30	11,50	0,64	4,44	4,21
Dec.	7,92	7,92	8,55	7,30	11,50	0,63	4,44	4,21
2005 Jan.	7,92	7,92	8,55	7,30	11,50	0,66	4,47	4,32
Feb.	7,90	7,91	8,60	7,30	11,67	0,67	4,39	4,36
Mar.	7,61	7,63	8,38	6,76	11,83	0,65	4,37	4,38
Apr.	7,61	7,63	8,38	6,76	11,75	0,64	4,30	4,38
May	7,18	7,20	7,97	6,33	11,83	0,55	4,04	4,07
June	6,69	6,70	7,58	5,76	12,00	0,39	3,47	3,88
July	6,69	6,70	7,47	5,76	12,00	0,42	3,47	3,85
Aug.	6,70	6,69	7,49	5,74	12,00	0,45	3,47	3,82
Sep.	6,69	6,69	7,49	5,74	12,00	0,46	3,47	3,79
Oct.	6,69	6,68	7,29	5,74	12,00	0,47	3,47	3,75
Nov.	6,69	6,68	7,29	5,72	12,00	0,46	3,48	3,72
Dec.	6,69	6,68	7,28	5,71	12,00	0,45	3,47	3,68
2006 Jan.	6,67	6,67	7,28	5,71	12,00	0,46	3,48	3,63
Feb.	6,65	6,65	7,27	5,71	12,00	0,45	3,48	3,59
Mar.	6,64	6,65	7,27	5,69	12,00	0,47	3,48	3,57
Apr.	6,64	6,64	7,28	5,69	12,00	0,48	3,48	3,55
May	6,64	6,63	7,28	5,68	12,00	0,47	3,48	3,52

Source: Commercial banks.

(1) Reported as at end of month.

(2) Data refer to the average of the representative interest rates as defined by the three largest banks.

Table 7
Interest rates - European monetary financial institutions

(percent per annum, outstanding amounts as at end-of-period)

1. Interest rates on euro-denominated deposits by euro area residents

	Deposits from households					Deposits from non-financial corporations		
	Overnight	With agreed maturity		Redeemable at notice ⁽¹⁾		Overnight	With agreed maturity	
		Up to 2 years	Over 2 years	Up to 3 months	Over 3 months		Up to 2 years	Over 2 years
2005 Mar.	0,74	1,92	3,22	1,96	2,47	0,94	2,09	3,71
Apr.	0,74	1,93	3,22	1,95	2,45	0,95	2,10	3,57
May	0,75	1,92	3,19	1,97	2,43	0,95	2,11	3,51
June	0,69	1,92	3,22	2,17	2,38	0,91	2,10	3,55
July	0,68	1,91	3,18	2,15	2,34	0,94	2,11	3,50
Aug.	0,69	1,92	3,18	2,03	2,31	0,96	2,10	3,52
Sep.	0,69	1,91	3,19	2,02	2,29	0,96	2,12	3,50
Oct.	0,69	1,93	3,17	1,96	2,27	0,97	2,12	3,45
Nov.	0,70	1,96	3,15	1,99	2,27	0,99	2,16	3,43
Dec.	0,71	2,01	3,15	1,98	2,30	1,02	2,30	3,41
2006 Jan.	0,73	2,05	3,10	1,99	2,32	1,04	2,32	3,48
Feb.	0,74	2,09	3,19	1,99	2,34	1,07	2,38	3,36

2. Interest rates on euro-denominated loans by euro area residents

	Loans to households						Loans to non-financial corporations		
	Lending for house purchase, with maturity			Consumer credit and other loans, with maturity			With maturity		
	Up to 1 year	Over 1 and up to 5 years	Over 5 years	Up to 1 year	Over 1 and up to 5 years	Over 5 years	Up to 1 year	Over 1 and up to 5 years	Over 5 years
2005 Mar.	4,75	4,41	4,78	8,07	6,97	5,77	4,38	3,91	4,40
Apr.	4,69	4,38	4,74	8,02	6,94	5,76	4,34	3,86	4,37
May	4,63	4,36	4,71	8,00	6,87	5,74	4,33	3,85	4,35
June	4,62	4,33	4,67	7,92	6,93	5,72	4,32	3,85	4,35
July	4,57	4,29	4,63	7,89	6,86	5,70	4,30	3,82	4,29
Aug.	4,54	4,24	4,60	7,96	6,86	5,73	4,25	3,80	4,28
Sep.	4,51	4,23	4,59	7,94	6,85	5,71	4,25	3,78	4,26
Oct.	4,49	4,19	4,58	7,95	6,80	5,70	4,24	3,77	4,25
Nov.	4,51	4,17	4,53	7,88	6,77	5,70	4,29	3,79	4,25
Dec.	4,54	4,14	4,52	7,93	6,78	5,67	4,35	3,84	4,24
2006 Jan.	4,63	4,14	4,50	8,00	6,78	5,66	4,42	3,88	4,26
Feb.	4,62	4,16	4,54	7,97	6,79	5,69	4,49	3,95	4,31

Source: European Central Bank.

(1) For this instrument category, households and non-financial corporations are merged and allocated to the household sector, since the outstanding amounts of non-financial corporations are negligible compared with those of the household sector in all participating Member States combined.

Table 8**Interest rate announcements in 2006**

	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sep.	Oct.	Nov.	Dec.
European Central Bank ⁽¹⁾	12 2,25	2 2,25	2 2,50	6 2,50	4 2,50	8 2,75	6	3	14	5	2	7
Bank of England ⁽²⁾	12 4,50	9 4,50	9 4,50	6 4,50	4 4,50	8 4,50	6	3	7	5	9	7
Federal Reserve ⁽³⁾	31 4,50		28 4,75		10 5,00	28/29 5,25		8	20	24		12
Central Bank of Cyprus ⁽⁴⁾	13 4,25	24 4,25		7 4,25	19 4,25		7		1	20		1

(1) Minimum bid rate on the main refinancing operations.

(2) Repo rate.

(3) Federal funds rate.

(4) Interest rate on the marginal lending facility.

Table 9
Percentage change in the consumer price index by economic origin (%)

	2003	2004	2005	May 2005/ 2004	April 2006/ 2005	May 2006/ 2005	Jan.- May 2005/ 2004	Jan.- April 2006/ 2005	Jan.- May 2006/ 2005	Weights	
										1998=100	2005=100
GENERAL INDEX	4,14	2,28	2,56	2,45	2,96	3,13	2,83	2,78	2,84	100,00	100,00
A Imported products	7,30	5,03	3,90	3,10	5,23	5,39	3,83	4,61	4,77	36,69	28,60
A.1 Agricultural	4,54	3,32	1,34	-3,49	8,13	9,68	1,03	3,83	5,00	7,93	6,92
A.2 Industrial	6,46	3,36	1,14	1,24	2,01	2,12	1,79	2,49	2,41	22,91	19,24
A.3 Electricity	10,20	-3,13	11,51	10,17	24,25	20,70	3,57	25,86	24,83	1,52	2,44
B Petroleum Products	14,16	17,18	14,82	16,63	12,33	15,87	15,41	13,57	14,03	4,33	6,44
C Imported products	-2,38	-5,55	-2,47	-1,89	-1,40	-1,63	-2,24	-1,20	-1,29	22,20	25,31
C1 Motor Vehicles	-8,31	-13,50	-2,42	-1,99	0,79	-0,23	-1,96	0,47	0,33	9,43	6,15
C2 Other Imported	1,81	-0,39	-2,49	-1,84	-2,21	-2,22	-2,39	-1,90	-1,97	12,77	19,16
D Services	4,38	3,23	3,34	3,60	2,68	2,63	3,99	2,36	2,39	41,11	39,65
HICP	4,0	1,9	2,1	2,0	2,5	2,5	2,4	2,4	2,4		

Table 10**Weighted contribution to the total change in the consumer price index by economic origin (%)**

		2003	2004	2005	May 2005/ 2004	April 2006/ 2005	May 2006/ 2005	Jan.- May 2005/ 2004	Jan.- April 2006/ 2005	Jan.- May 2006/ 2005	Weights	
											1998=100	2005=100
GENERAL INDEX		4,14	2,28	2,56	2,45	2,96	3,13	2,83	2,78	2,84	100,00	100,00
A	Imported products	2,79	1,98	1,58	1,25	1,48	1,52	1,53	1,31	1,35	36,69	28,60
A.1	Agricultural	0,37	0,27	0,11	-0,29	0,55	0,63	0,09	0,26	0,34	7,93	6,92
A.2	Industrial	1,47	0,78	0,27	0,30	0,39	0,41	0,42	0,48	0,46	22,91	19,24
A.3	Electricity	0,20	-0,07	0,23	0,19	0,54	0,48	0,07	0,57	0,55	1,52	2,44
B	Petroleum products	0,74	0,99	0,97	1,05	0,78	1,00	0,96	0,82	0,86	4,33	6,44
C	Imported products	-0,48	-1,04	-0,43	-0,33	-0,36	-0,42	-0,40	-0,31	-0,33	22,20	25,31
C1	Motor vehicles	-0,69	-1,00	-0,15	-0,12	0,05	-0,01	-0,12	0,03	0,02	9,43	6,15
C2	Other imported	0,21	-0,04	-0,28	-0,21	-0,42	-0,42	-0,27	-0,36	-0,37	12,77	19,16
D	Services	1,83	1,35	1,41	1,51	1,06	1,04	1,69	0,94	0,95	41,11	39,65

Table 11
Percentage change in the consumer price index by category of goods and services(%)

	Years			May 2005/ 2004	April 2006/ 2005	May 2006/ 2005	Jan.- May 2005/ 2004	Jan.- April 2006/ 2005	Jan.- May 2006/ 2005	Weights	
	2003	2004	2005							2005=100	1998=100
GENERAL INDEX	4,14	2,28	2,56	2,45	2,96	3,13	2,83	2,78	2,84	100,00	100,00
Food & non-alcoholic beverages	5,11	3,97	1,59	-0,45	5,55	6,28	1,74	3,63	4,16	17,50	18,20
Alcoholic beverages & tobacco	24,22	10,57	0,23	-0,09	-1,11	-1,07	1,16	-0,16	-0,34	2,21	1,78
Clothing & footwear	1,19	-0,79	-2,24	-0,96	-2,50	-2,84	-1,65	1,31	0,48	8,93	8,22
Housing, water, electricity & gas	5,04	4,19	5,41	5,59	7,01	6,40	5,05	7,25	7,08	15,87	21,27
Furnishings, household equipment & supplies	3,59	-0,45	0,58	0,49	0,04	-0,24	0,29	0,66	0,48	6,78	7,08
Health	5,66	3,72	0,36	0,83	1,85	1,66	1,47	-2,48	-1,65	5,03	4,92
Transport	0,35	-3,06	3,79	4,08	4,54	5,56	3,86	4,85	4,99	15,99	17,42
Communications	-7,16	-8,48	-10,34	-9,57	-0,11	0,97	-9,73	-2,41	-1,74	3,94	1,79
Recreation & culture	3,55	2,26	1,06	2,77	-1,06	-1,01	2,47	-1,26	-1,21	6,33	5,88
Education	4,02	3,96	5,21	5,60	4,55	4,55	5,60	4,55	4,55	2,87	2,33
Restaurants & hotels	5,31	4,69	3,30	3,33	2,43	2,41	4,57	1,88	1,99	7,57	6,07
Miscellaneous goods & services	5,50	5,16	3,83	4,09	1,51	1,71	4,45	1,97	1,92	6,98	5,04

Table 12**Weighted contribution to the total change in the consumer price index by category of goods and services (%)**

	Years			May 2005/ 2004	April 2006/ 2005	May 2006/ 2005	Jan.- May 2005/ 2004	Jan.- April 2006/ 2005	Jan.- May 2006/ 2005	Weights	
	2003	2004	2005							2005=100	1998=100
GENERAL INDEX	4,14	2,28	2,56	2,45	2,96	3,13	2,83	2,78	2,84	100,00	100,00
Food & non-alcoholic beverages	0,97	0,76	0,31	-0,09	0,96	1,07	0,34	0,64	0,72	17,50	18,20
Alcoholic beverages & tobacco	0,54	0,28	0,01	0,00	-0,02	-0,02	0,03	0,00	-0,01	2,21	1,78
Clothing & footwear	0,08	-0,05	-0,14	-0,07	-0,24	-0,27	-0,10	0,10	0,03	8,93	8,22
Housing, water, electricity & gas	1,10	0,93	1,22	1,25	1,10	1,01	1,13	1,13	1,11	15,87	21,27
Furnishings, household equipment & supplies	0,23	-0,03	0,04	0,03	0,00	-0,02	0,02	0,05	0,03	6,78	7,08
Health	0,30	0,20	0,02	0,05	0,09	0,08	0,08	-0,14	-0,09	5,03	4,92
Transport	0,06	-0,51	0,59	0,63	0,72	0,89	0,59	0,77	0,79	15,99	17,42
Communications	-0,09	-0,10	-0,11	-0,10	0,00	0,04	-0,10	-0,10	-0,08	3,94	1,79
Recreation & culture	0,19	0,12	0,06	0,15	-0,07	-0,06	0,13	-0,08	-0,08	6,33	5,88
Education	0,10	0,10	0,13	0,14	0,13	0,13	0,14	0,13	0,13	2,87	2,33
Restaurants & hotels	0,35	0,31	0,23	0,23	0,18	0,18	0,31	0,14	0,15	7,57	6,07
Miscellaneous goods & services	0,29	0,28	0,21	0,22	0,11	0,12	0,24	0,14	0,13	6,98	5,04

Table 13
Cyprus Stock Exchange: purchase and sale of listed shares by non-residents⁽¹⁾

(CYP thousand)

Geographic origin of non-resident investors	Purchase of listed shares by non-residents							Sale of listed shares by non-residents						
	2004	2005	2006					2004	2005	2006				
			Jan.	Feb.	Mar.	Apr.	May			Jan.	Feb.	Mar.	Apr.	May
EUROPE	7.416,2	7.395,9	2.118,1	1.386,5	2.214,9	3.603,4	6.436,9	1.199,3	3.461,1	872,1	1.312,8	1.765,8	1.604,9	2.220,6
EU-25	6.064,4	6.805,2	1.951,1	1.072,6	2.053,5	1.385,2	3.367,4	3.710,1	2.980,4	692,5	856,6	1.655,3	1.555,9	1.688,2
Greece	5.519,5	5.667,5	1.633,9	821,4	1.545,2	1.082,9	2.294,2	3.328,1	2.269,5	629,2	791,8	1.359,8	674,4	1.229,9
United Kingdom	265,2	238,2	40,3	70,2	231,8	132,0	295,8	182,5	390,6	46,5	26,8	132,4	178,5	316,6
Other European countries	1.351,8	590,7	167,0	313,9	161,4	2.218,2	3.069,5	228,6	480,7	179,6	456,1	110,5	49,0	532,3
Russian Federation	1.131,5	405,4	64,2	252,3	105,2	3,1	49,3	59,3	279,7	159,5	264,8	9,2	9,1	51,2
AFRICA	415,8	51,4	0,0	14,4	59,5	3,7	21,3	295,7	90,1	36,1	19,3	0,0	7,9	28,4
North African countries	0,9	0,0	0,0	0,0	0,0	0,0	0,0	0,0	1,8	0,0	0,0	0,0	0,0	0,0
Other African countries	414,9	51,4	0,0	14,4	59,5	3,7	21,3	295,7	88,3	36,1	19,3	0,0	7,9	28,4
South Africa	56,7	0,0	0,0	6,3	0,0	1,8	7,9	0,0	7,6	0,3	6,0	0,0	7,9	0,0
AMERICA	888,6	429,3	269,9	219,7	487,8	409,6	1.180,1	1.643,7	1.232,7	70,7	355,5	449,0	414,5	942,7
North American countries	635,6	84,1	190,0	42,1	75,3	4,2	24,6	80,0	33,2	1,1	84,2	48,8	61,4	10,8
United States of America	634,9	81,9	189,4	41,8	75,3	4,2	10,5	28,7	33,2	0,9	84,2	48,8	52,5	10,8
Canada	0,7	2,2	0,6	0,3	0,0	0,0	14,1	51,3	0,0	0,2	0,0	0,0	8,9	0,0
Central American countries	253,0	345,2	79,9	177,5	412,5	405,5	1.155,5	1.563,7	1.199,4	69,6	271,3	400,2	353,0	931,9
South American countries	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0
ASIA	61,7	267,3	1,3	16,0	8,5	0,0	11,2	12,2	229,2	4,1	71,0	1,0	1,1	88,2
West Asia	17,0	204,7	1,3	13,7	8,4	0,0	11,2	12,2	168,9	4,1	71,0	1,0	1,1	43,1
Other Asian countries	44,8	62,6	0,0	2,3	0,1	0,0	0,0	0,0	60,3	0,0	0,0	0,0	0,1	45,1
OCEANIA	18,5	0,0	0,0	0,0	0,0	0,0	0,0	8,2	0,0	0,0	0,0	0,0	0,0	0,0
Total	8.800,8	8.143,9	2.389,3	1.636,5	2.770,7	4.016,7	7.649,5	5.898,5	5.013,0	983,0	1.758,7	2.215,8	2.028,4	3.279,8

Source: Cyprus Stock Exchange.

(1) Purchase of shares included in the central securities depository as well as shares not included in the central securities depository.

Table 14
Balance of payments
(CYP million)

CATEGORIES	2004 (Annual) (Prov.)			2005 (Annual) (Prov.)		
	CREDIT	DEBIT	NET	CREDIT	DEBIT	NET
CURRENT ACCOUNT	4.038,1	4.454,4	-416,3	4.340,8	4.793,8	-453,0
Goods, services and income	3.760,1	4.259,7	-499,6	4.048,4	4.543,7	-495,4
Goods and services	3.458,6	3.673,0	-214,4	3.691,1	3.927,9	-236,9
Goods	541,0	2.440,3	-1.899,3	675,7	2.671,0	-1.995,3
Services	2.917,6	1.232,7	1.684,9	3.015,3	1.256,9	1.758,4
Transport	676,6	523,1	153,5	714,3	500,6	213,7
Travel	1.054,4	378,2	676,2	1.081,7	432,8	648,9
Communications services	16,5	36,6	-20,1	15,6	44,0	-28,4
Construction services	68,4	6,9	61,5	75,6	4,9	70,7
Insurance services	20,9	33,3	-12,4	26,3	30,0	-3,7
Financial services	104,6	46,8	57,8	127,6	43,7	83,9
Computer and information services	112,4	11,7	100,7	98,7	16,0	82,7
Royalties and licence fees	8,3	25,0	-16,7	6,9	21,2	-14,3
Other business services	687,5	105,5	582,0	699,1	94,6	604,5
Personal, cultural and recreational services	11,6	22,7	-11,1	19,2	26,0	-6,9
Government services, n.i.e.	156,3	42,8	113,5	150,4	43,1	107,4
Income	301,5	586,7	-285,2	357,3	615,8	-258,5
Compensation of employees	14,3	79,2	-64,9	24,2	85,8	-61,6
Investment income	287,2	507,6	-220,3	333,1	530,0	-196,9
Current transfers	278,0	194,7	83,3	292,5	250,1	42,4
General government	85,9	61,3	24,6	108,2	97,3	10,9
Other sectors	192,1	133,4	58,8	184,3	152,8	31,5
Capital and financial account			434,5			518,5
Capital account	86,1	27,1	59,0	60,9	20,6	40,3
Financial account			375,5			478,2
Direct investment			215,8			340,8
Abroad			-289,9			-200,4
In Cyprus			505,7			541,2
Portfolio investment			551,8			-62,0
Assets			-839,9			-755,9
Liabilities			1.391,7			693,9
Financial derivatives			-21,2			-6,8
Other investment			-191,6			540,0
Assets			-1.383,9			-3.384,1
Liabilities			1.192,3			3.924,1
Reserve assets			-179,3			-333,8
NET ERRORS AND OMISSIONS			-18,2			-65,6

Sources: Central Bank of Cyprus and Cystat.

Table 15**Accounts of general government (analysis of expenditure and revenue)**

	Jan-April 2005	Jan-April 2006	April 2006/2005
	CYP million		% change
Total revenue and grants	891,5	873,3	-2,0
Direct taxes	277,0	229,4	-17,2
Income tax	91,9	124,1	35,0
Other direct taxes	185,1	105,3	-43,1
Indirect taxes	378,2	403,7	6,7
Value added tax	211,9	233,5	10,2
Excise taxes	112,7	107,9	-4,3
Import duty	11,0	2,6	-76,4
Social security contributions	117,9	131,3	11,4
Non-tax revenue	89,7	81,2	-9,5
Foreign grants	28,7	27,7	-3,5
Total expenditure and net lending	837,6	897,2	7,1
Current expenditure	793,6	853,2	7,5
Goods and services	52,7	67,5	28,1
Wages and salaries	246,6	268,4	8,8
Pensions and gratuities	54,2	51,4	-5,2
Social pensions	9,1	9,3	2,2
Other current transfers ⁽²⁾	183,4	208,6	13,7
Unallocable expenses ⁽³⁾	5,4	1,9	-64,8
Social security funds payments	128,9	136,7	6,1
Subsidies	3,6	3,5	-2,8
Interest	109,7	106,0	-3,4
Capital expenditure	44,1	44,0	-0,2
Investment	44,1	44,0	-0,2
Capital transfers	0,0	0,0	0,0
Net lending	0,0	0,0	0,0
Fiscal surplus (+)/deficit(-)	97,9	20,0	-79,6
<i>As % of GDP</i>	<i>0,70</i>	<i>-0,30</i>	<i>-142,9</i>

(1) The figures are prepared on a cash basis methodology. Therefore, they are not identical with the figures submitted officially by Cystat to Eurostat as these refer to general government finances and are compiled on an accrual basis.

(2) Includes transfers to semi-governmental organisations, local authorities, pensioners and students.

(3) Includes only expenditure on military equipment.