CENTRAL BANK OF CYPRUS
EUROSYSTEM

REVIEW OF EXTERNAL STATISTICS

2013-2014

INTRODUCTION

The purpose of this report is to provide a comprehensive overview of the main developments in the external statistics of Cyprus, with an emphasis on developments in selected economic sectors[1].

The data analysed in this report derives from the time series 2008-2014 which have been compiled on the basis of the 6th edition of the Balance of Payments and International Investment Position manual of the IMF (BPM6), which was implemented in 2014. All publications and data releases prior to 2008 are, therefore, not comparable as they are based on the BPM5[2] methodology. The most important change concerns the incorporation and publication of data on "special purpose entities" (SPEs) registered in Cyprus. All presentational and methodological changes vis-à-vis BPM5 can be found in the Appendix.

1. CURRENT ACCOUNT

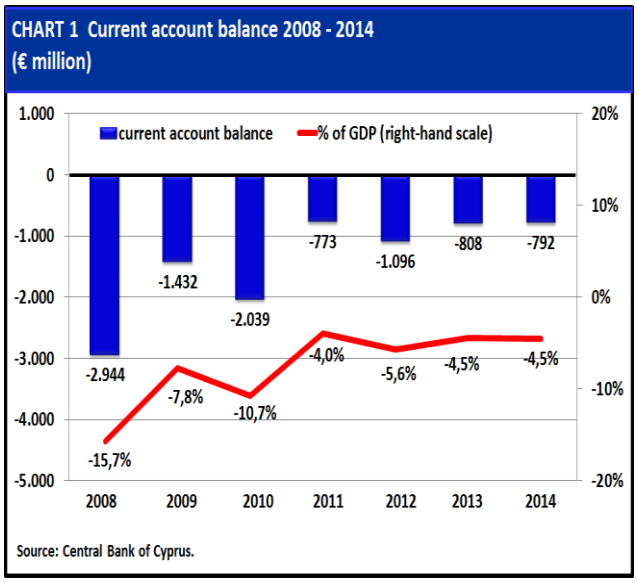
- **Cyprus's current account (CA) deficit for 2014 settled at €791,5 million.**
- **The current account deficit-to-GDP ratio remained at 4,6%.**
- **There was a €2.933,0 million surplus in services for 2014.**
- **The trade deficit in goods for 2014 was €2.812,2 million.**

Cyprus's CA deficit for 2014 settled at €791,5 million, following considerable fluctuations since 2008 when it reached a record high of €2.944,1 million (**Chart 1**). Expressed as a percentage of GDP, the CA deficit in 2014 remained stable at 4,6%, following a decrease from 5,6% in 2012 to 4,5% in 2013. The main cause of the reduction in the deficit was a decrease in imports of goods and income payable abroad during 2013.

The individual components of the current account are illustrated in **Chart 2**. The trade balance in goods remained negative (deficit) at €2.812,2 million in 2014, despite substantial improvements during the last four years. In contrast, there was a surplus in **services**, which in 2014 amounted to €2.933,0 million. The corresponding balance in 2013 and 2012 was €3.134,5 million and €3.297,2 million, respectively. The reduction in the services balance in 2014 was primarily due to a reduction in exports of "transport" services. The **primary and secondary income** accounts also recorded deficits in 2014 (€488,8 and €423,5 million, respectively). The deficit in the primary income account concerned mostly direct investment and "other" investment income.

[1] *External Statistics* – specifically balance of payments (BOP), international investment position (IIP) and external debt statistics – measure all economic transactions and all financial positions between residents and non-residents. In addition, they constitute part of the external statistics of the European Union and the euro area.

[2] Balance of Payments and International Investment Position manual of the IMF, 5th edition



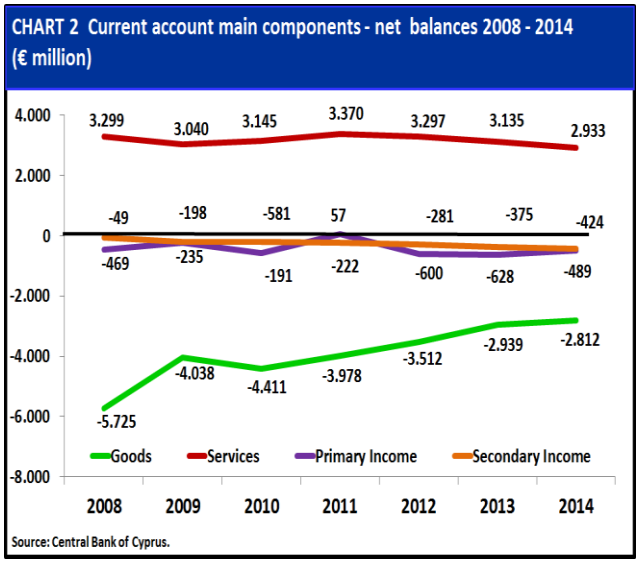
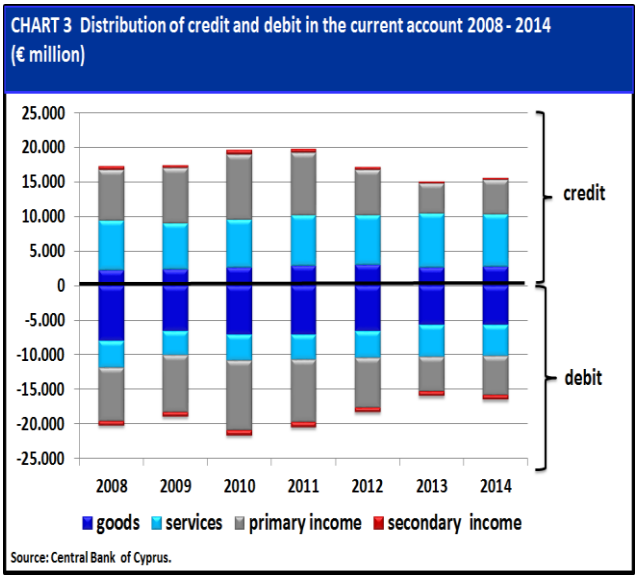


Chart 3 illustrates the year–on–year movement of CA debits (outward flows) and credits (inward flows). Both credits and debits increased marginally between 2013 and 2014.

- "Primary income" is the component with the highest recorded increase during 2014. In particular, "primary income" credits increased from €4.395,1 million in 2013 to €5.051,0 million in 2014 and "primary income" debits from €5.023,1 to €5.539,9 million during the same period.
- "Services" provide the highest share contribution in both debits and credits since 2012, while previously this was the case with "primary income".



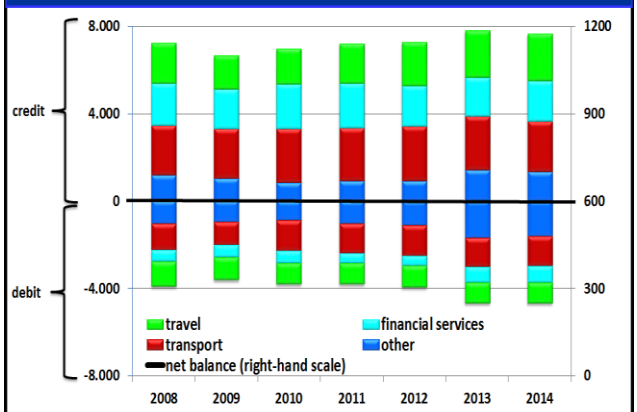
Services

The most important sectors under the "services" category are further analysed in **Chart 4**.

- Receipts from "services" (credits) totalled €7.629,8 million in 2014, down 2,3% from 2013 (€7.807,6 million).
- In contrast, "services" related payments (debits) increased marginally to €4.696,7 million in 2014 (up from €4.673,2 million recorded in 2013).
- Exports of "services" consisted mainly of "travel", "transport" and "financial" services. In 2014 exports of "transport" and "telecommunication, computer and information" services decreased.
- "Travel" and "transport" are also the main import (debits) sectors in "services". Since 2008, exports of "services" have been consistently higher than imports and in 2014 the net balance closed at

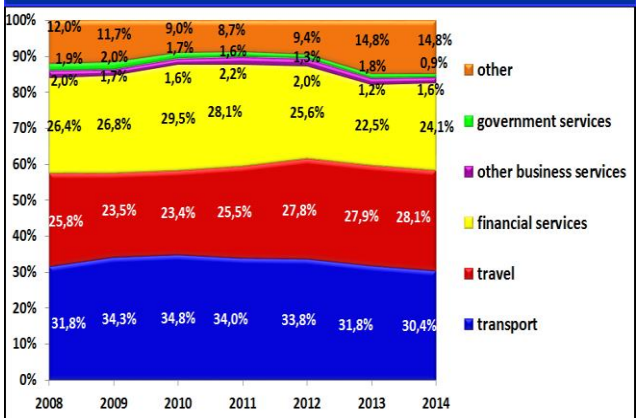
€2.933,0 million. Surpluses were realised in the "transport" (€957,7 million), , "financial services" (€1.060,2 million), and "travel" (€1.196,9 million) sectors of "services". The "financial services" sector consists mostly of financial companies, including monetary and financial institutions (MFIs) and the "transport" sector of shipping companies.

CHART 4 Current account - exports and imports of services 2008 - 2014 (€ million)



Source: Central Bank of Cyprus.

CHART 5 Services exports 2008 - 2014 (% shares)

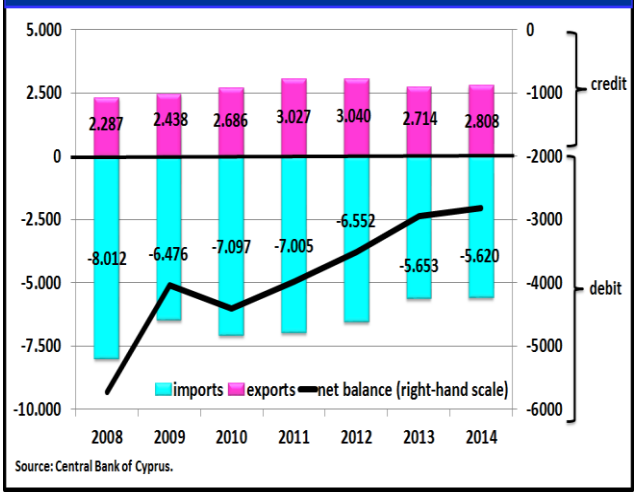


Source: Central Bank of Cyprus.

Chart 5 provides a percentage decomposition of "services" exports. This information enables the identification of the most important "service" sectors of the economy, where Cyprus has a competitive advantage. "Transport" and "financial services" contributed 30,4% and 24,1% of the total amount of "services" exported in 2014, respectively. Historically, there has been a significant contribution from "travel" services, which increased to 28,1% in 2014. The contribution by "other services" (includes all remaining services except legal, accounting, management services and triangular trade) closed at 14,8%, in 2013 and 2014, which is higher than the previous years.

Goods

CHART 6 Current account - exports and imports of goods 2008 - 2014 (€ million)



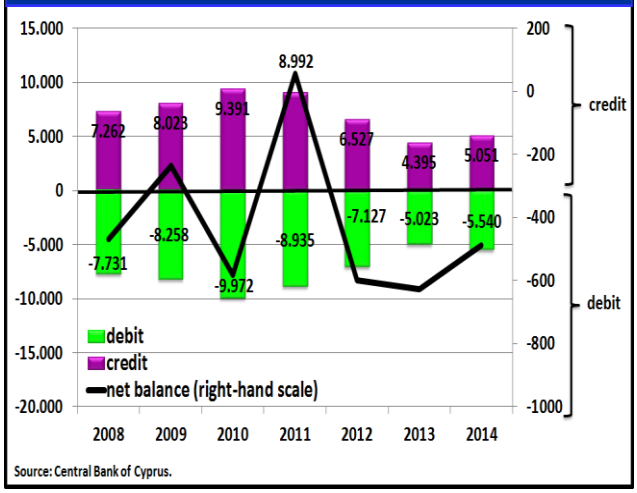
Source: Central Bank of Cyprus.

The year-on-year comparison of the trade deficit is demonstrated in **Chart 6**. Imports are consistently higher than exports. A significant reduction in the trade deficit was recorded in 2013 when imports of goods decreased from €6.551,9 miilion to €5.652,9 million. Imports of goods dropped further in 2014 to €5.620,0 million.

Primary income

Primary income account payments (debits) and receipts (credits) are analysed in **Chart 7**. Primary income receipts increased to €5.051,0 million in 2014, mainly due to increases in direct investment

income receipts. There was also a parallel increase in income payments during the same year, from €5.023,1 million in 2013 to €5.539,9 million. The net balance in the primary income account was particularly volatile prior to 2012 with occasional surpluses, as in 2009 and 2011. Since 2012, both primary income debits and credits declined in volume. However, debits remained higher than credits mainly due to large payments of direct investment income.



The income account also consists of secondary income, which refers to transfer payments between Cyprus and the rest of the world (e.g. workers' remittances). Total credits for 2014 were €232,1 million and total debits €655,6 million.

2. CAPITAL ACCOUNT, FINANCIAL ACCOUNT AND INVESTMENT POSITIONS

2.1 Capital account

The capital account is of relatively small importance to the CA financing when compared to the contribution of the financial account. Capital account credits reached €147,6 million and debits €1,2 million in 2014 (thus providing a net contribution of €146,4 million to the current account financing). In previous years, credits were: €257,0 million in 2013, €35,6 million in 2012, and €95,2 million in 2011. The increased surplus in 2013 was due to the revenues from the rights on the exploitation and exploration of the natural gas and oil reserves within the exclusive economic zone of Cyprus.

2.2. Financial account

Based on the principle of double-entry accounting, the balance of the financial account is, by definition, equal to the balance of the current and capital accounts. In practice, however, this correlation is weak since, firstly, transactions cannot always be correctly attributed to the respective periods and, secondly, there are gaps in the statistical coverage of almost all sub-accounts. All these discrepancies are reflected in the "net errors and omissions" account.

For the sake of a more comprehensive analysis, the remainder of **Section 2** presents the flows in the financial account together with the stock positions of each investment category. Stock positions are recorded in the IIP and are further analysed in **Section 3**.

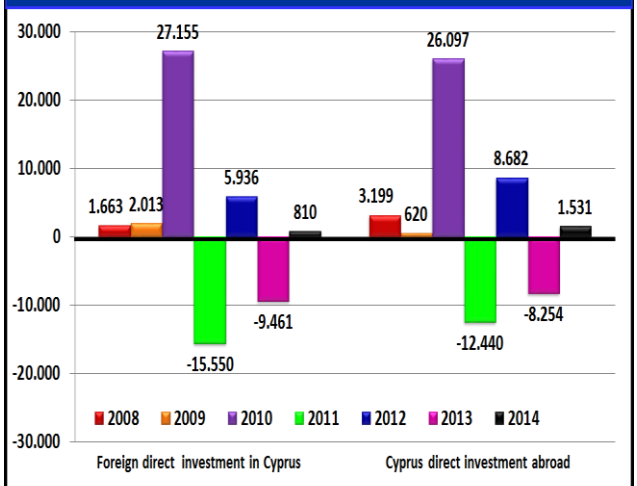
2.2.1. Foreign direct investment

- **Foreign direct investment flow liabilities increased by €810,1 million in 2014.**
- **Foreign direct investment flow assets increased by €1.531,3 million.**
- **Between 2013 and 2014, the total stock of foreign direct investment liabilities increased by 4%.**
- **Most direct investment in Cyprus concerns "financial & insurance activities".**

The inflow of foreign direct investment (FDI) constitutes a long-term strategic objective of the Cyprus business model. FDI flow liabilities increased by €810,1 million in 2014 (**Chart 8**), following a large

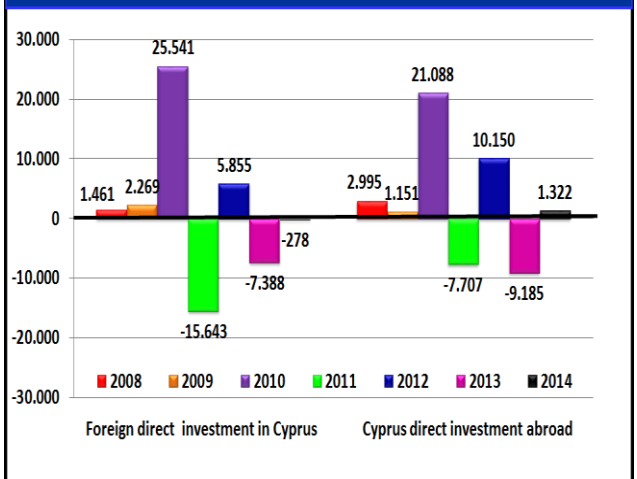
reduction of €9.461,2 million in the previous year. Similarly, FDI asset flows increased by €1.531,3 million in 2014, following a reduction of €8.253,9 million in the previous year. There was considerable volatility in FDI flows during the period 2010-2013, with particularly large flows in years 2010 and 2011.

CHART 8 Flows of direct investment 2008 - 2014
(€ million)



Source: Central Bank of Cyprus.

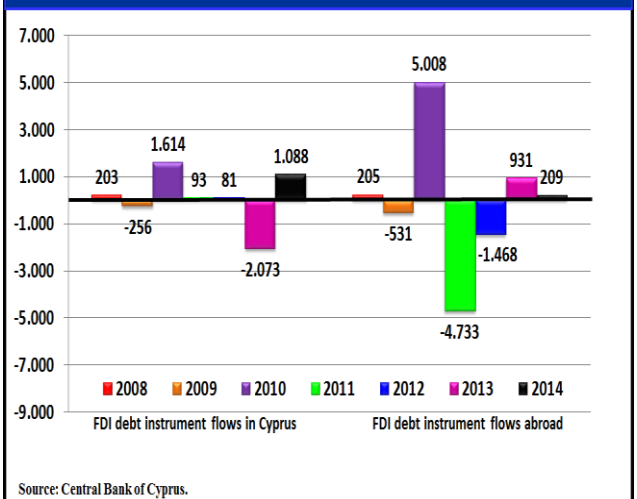
CHART 9 Direct investment equity and investment fund shares flows 2008 - 2014
(€ million)



Source: Central Bank of Cyprus.

Chart 9 provides more detailed information on the "equity and investment fund shares" flows component (including re-invested earnings) of FDI. "Equity and investment fund shares" liabilities flows decreased by €277,8 million in 2014 following a decrease by €7.387,9 million in 2013. Increases were recorded with regard to FDI asset flows. In the case of assets the increase concerned primarily "reinvestment of earnings", while in the case of liabilities the decrease concerned primarily "equity other than reinvestment of earnings".

CHART 10 Direct investment debt instruments flows 2008 - 2014
(€ million)



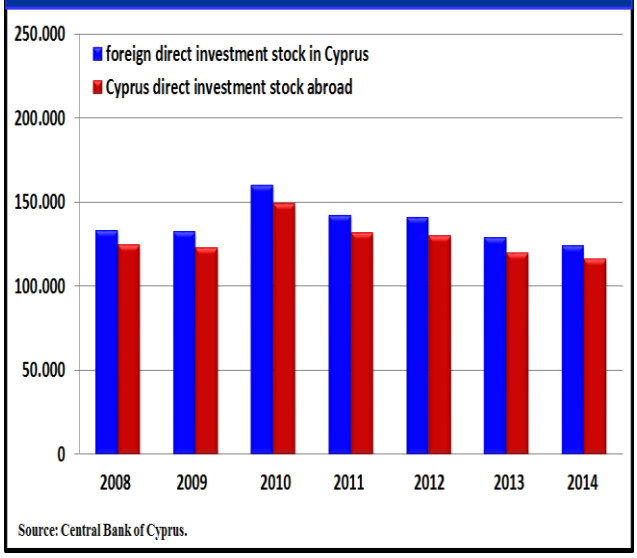
Source: Central Bank of Cyprus.

"Debt instruments" flows refer mainly to intercompany lending in direct investment enterprises, in a direct investor (reverse investment) or between fellow enterprises. There was considerable volatility in the recorded aggregated flows of assets of this category during the period 2010-2014 **(Chart 10)**, particularly during the years 2010-2011. "Debt instrument" liabilities increased by €1.087,9 million in 2014, despite the reduction observed during the previous year. Similarly, "Debt instrument" asset flows increased by €208,9 million in 2014.

Chart 11 presents the aggregated stocks of FDI liabilities recorded in Cyprus during the years 2008-2014. By the end of 2014, the total stock of FDI liabilities accumulated in Cyprus was €124.346,1

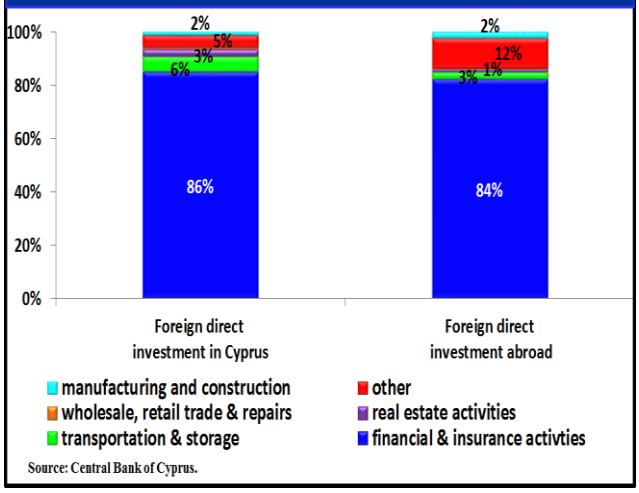
million, a 4% decrease compared with 2013. Similarly, the total stock of FDI assets decreased from €119.805,2 million in 2013 to €115.975,2 million in 2014 (a 3% decrease). In both cases the changes in positions resulted from price, exchange and "other changes" not related to transactions. Due to the higher amount of FDI liabilities, the spread between assets and liabilities in 2014 was €8.370,9 million.

CHART 11 Foreign direct investment stocks 2008 - 2014
(€ million)



Source: Central Bank of Cyprus.

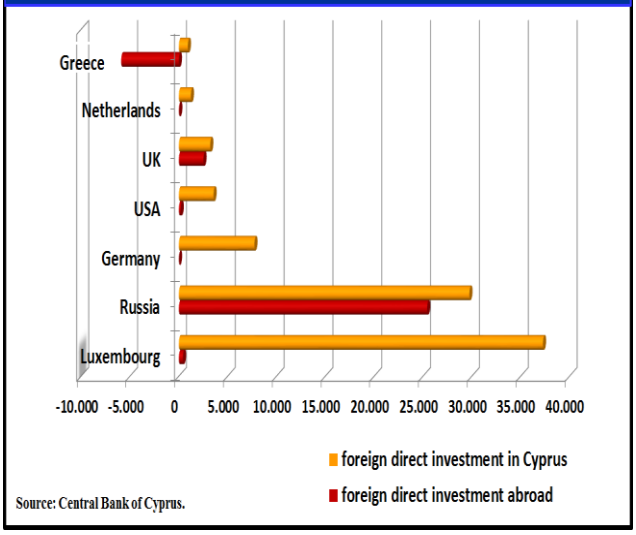
CHART 12 Direct investment net stock positions by economic activity 2014
(% of stocks)



Source: Central Bank of Cyprus.

An important aspect of FDI is its allocation by economic activity (based on the economic sector into which the direct investment takes place). The main sectors for 2014 are presented in **Chart 12**. The most profound insight in both assets and liabilities is that most of the invested amounts concerned investments in "financial & insurance activities". In the case of assets, the contribution of this sector in 2014 was 84% and in the case of liabilities it was 86%.

CHART 13 Direct investment stocks by country 2014
(€ million)



Source: Central Bank of Cyprus.

In **Chart 13,** FDI stocks are decomposed by country. It presents the main countries whose residents are investing in Cyprus (liabilities), as well as some of the main target countries for Cypriot investors abroad (assets). Only six countries are presented from each category. Most direct investors in Cyprus come from Luxembourg, Russia and Germany. For Cypriot entities, the main direct investment destination is Russia.

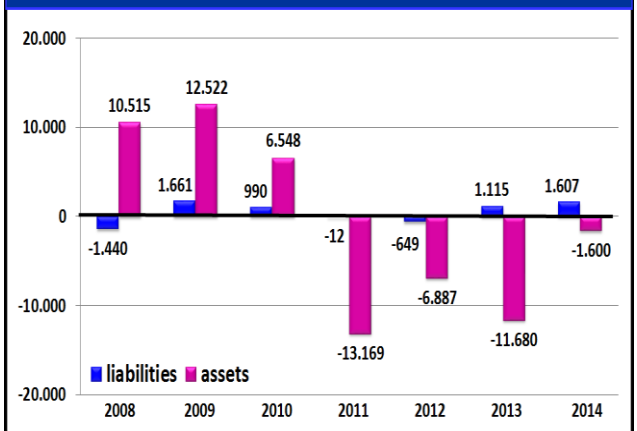
2.2.2 Portfolio investment

- **Portfolio investment stocks remained relatively stable in 2014. These investment positions comprised primarily long-term debt securities.**

- **The most important category of investors in debt securities issued by non-residents (assets), were "monetary and financial institutions" and "other sectors".**
- **On the liabilities side, debt securities were predominantly issued by "general government" and "other sectors".**
- **Most of the investment positions undertaken by residents abroad were placed in Russia.**

The portfolio investment (PI) flows for 2014 are presented in **Chart 14**. PI assets held by residents abroad decreased by €1.600,1 million in 2014, representing mainly net sales of long-term debt securities. Foreign asset holdings declined significantly during the previous three years, most notably in 2011. PI liability flows increased by €1.114,7 million in 2013 and €1.606,8 million in 2014, representing a net inflow of funds from securities issued by residents and held by non-residents. In both years, the additional investments were directed to long-term debt and equity securities.

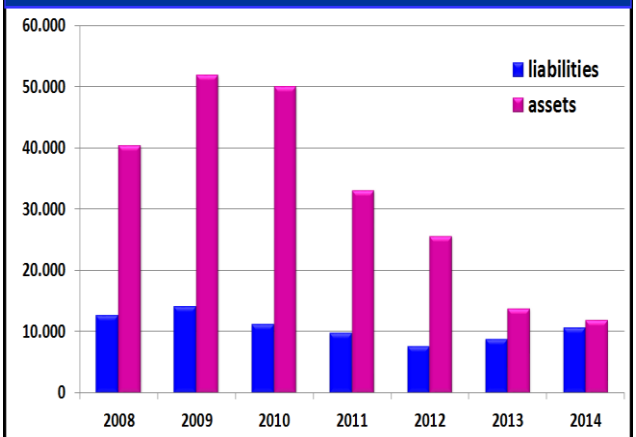
CHART 14 Portfolio investment flows 2008 - 2014
(€ million)



Source: Central Bank of Cyprus.

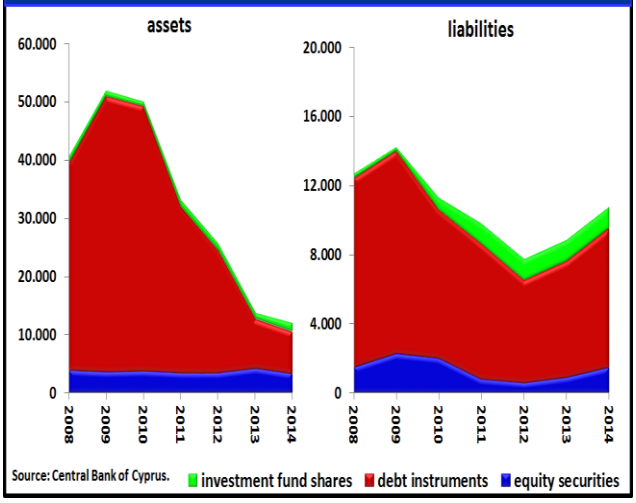
PI stocks remained relatively stable in both assets and liabilities in 2014 (**Chart 15**), in line with the previous year. Assets decreased from €13.832,1 million in 2013 to €11.967,4 million in 2014, following reductions in equity and debt security investments abroad. The stock of liabilities is smaller but nevertheless increased from €8.860 million in 2013 to €10.754,6 million in 2014. This increase in liabilities concerned mostly long-term debt securities issued by MFIs and "other sectors" in Cyprus. In 2014 the liabilities to assets ratio closed at 0,90%.

CHART 15 Portfolio investment stocks 2008 - 2014
(€ million)



Source: Central Bank of Cyprus.

CHART 16 Portfolio investment assets and liabilities 2008 - 2014
(€ million)

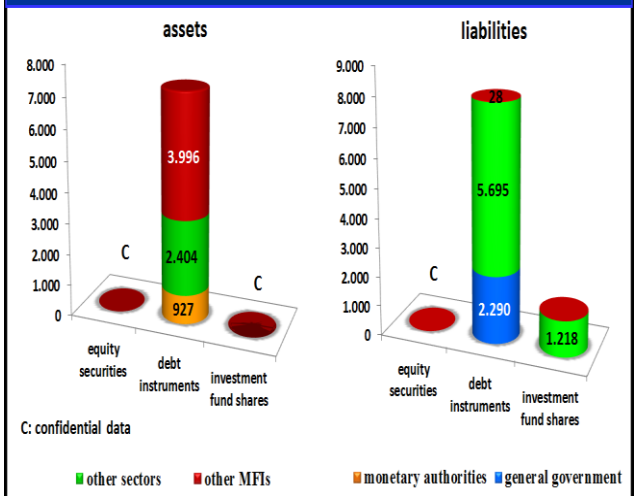


Source: Central Bank of Cyprus.

In **Chart 16** PI asset and liability stocks are decomposed by instrument. Debt securities constitute the main component for both assets and

liabilities, amounting to €7.326,4 and €8.012,5 million, respectively, as at end 2014. Equity investments and investment fund shares represent only a small fraction of both assets and liabilities. On average, for the period covered by the analysis, equity investments corresponded to 10% of total assets and 13% of total liabilities. Investment fund shares on the other hand corresponded to 5% of total assets and 9% of total liabilities.

CHART 17 Portfolio investment by sector 2014
(€ million)

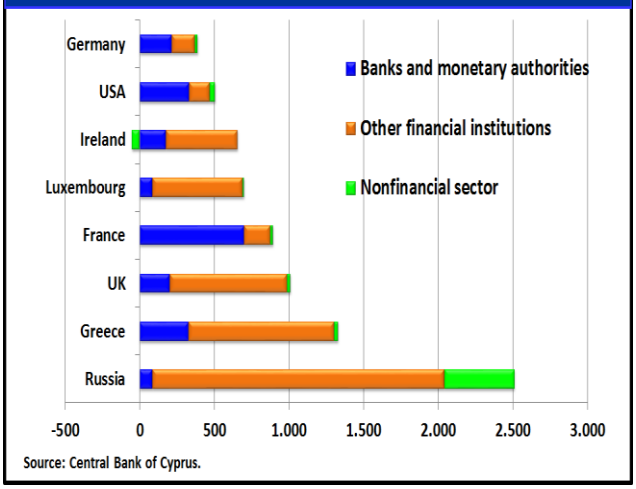


Source: Central Bank of Cyprus.

PI are most commonly analysed by sector and financial instrument (**Chart 17**). Out of the total amount of investments in debt securities abroad (assets), €3.995,5 million corresponded to investments by MFIs and €2.403,6 million to investments by "other sectors". To a smaller extent, there were also investments abroad by the "monetary authorities" (€927,3 million). In the case of liabilities, bonds and notes held by non-residents were mainly issued by "other sectors" (€5.695 million) and the "general government" (€2.289,8 million).

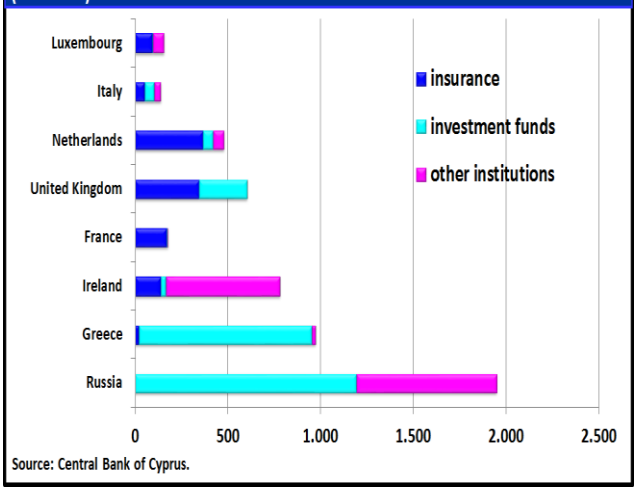
In **Chart 18,** securities held by residents in 2014 are distinguished by country and economic sector. Most of the investment positions undertaken by residents abroad were placed in Russia (€2.509,5 million) and Greece (€1.327,1 million). In both countries, most of the amounts concerned investments by financial institutions other than "banks and the monetary authorities". "Banks and the monetary authorities" were the main investors in France and the USA with €698,4 and €333,8 million, respectively.

CHART 18 Portfolio investment assets held by residents 2014
(€ million)



Source: Central Bank of Cyprus.

CHART 19 Portfolio investment assets held by "other" resident financial institutions and excluding banks and the monetary authorities 2014
(€ million)



Source: Central Bank of Cyprus.

The investment amounts placed by "other financial institutions" abroad are further decomposed into the

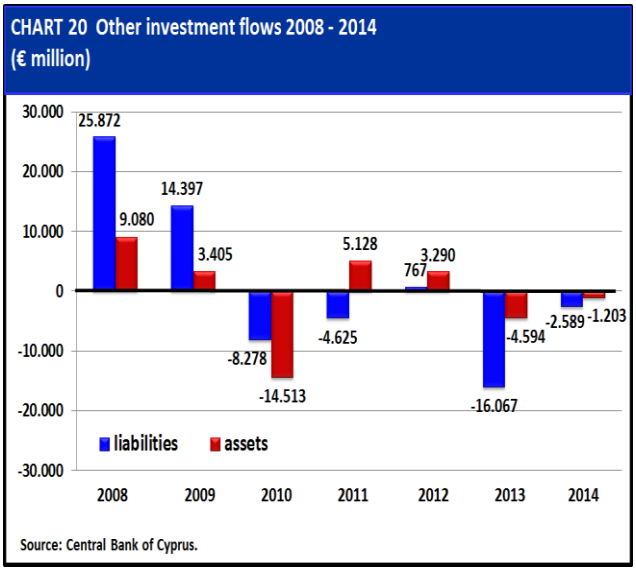
following segments: "insurance companies", "investment funds" and "other institutions" as demonstrated in **Chart 19**. Russia and Greece were again the main investment destinations. "Investment funds" invested €1.190,9 million in Russia and €930,8 million in Greece. "Insurance companies" invested mostly in the Netherlands and the UK and "other institutions" in Russia and Ireland.

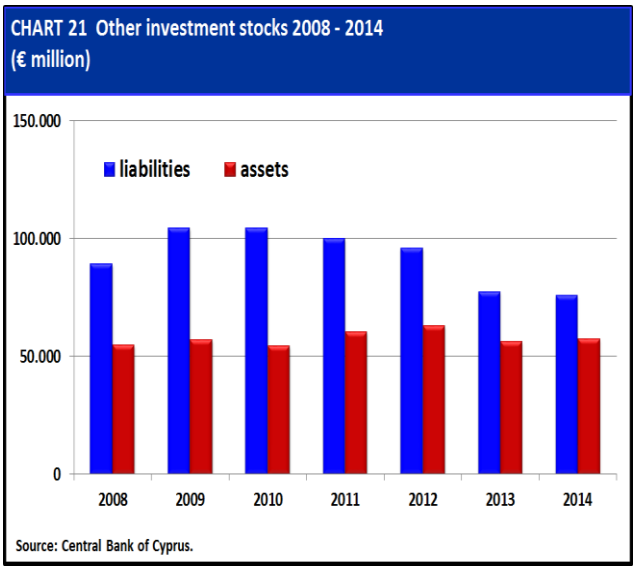
2.2.3 "Other" investment

- **"Other" investment liability flows were negative throughout the period 2013-2014.**
- **Liabilities stocks decreased in 2014, while assets increased marginally.**
- **In both assets and liabilities, "other" investment concerned mostly "loans/currency and deposits" and were primarily associated with "other sectors" entities and MFIs.**

Other investment (OI) liability flows were negative throughout 2013-2014. A €16.066,5 million decrease was recorded in 2013, and a smaller one in 2014 of €2.588,7 million as shown in **Chart 20**. Reductions in liabilities represent withdrawals of investments placed by foreign investors in Cyprus and concerned primarily reductions in "currency and deposits" held with MFIs. There were also reductions in OI assets, since negative flows were recorded in 2013 (€4.593,5 million) and 2014 (€1.202,7 million).

Chart 21 provides information on OI asset and liability stocks. Liabilities decreased in 2014 while assets increased marginally. By the end of 2014, liabilities were €75.901.8 million and assets €57.253,3 million. Liabilities represent mainly deposits by non-residents in Cyprus, as well as loans granted by foreign institutions to residents. Assets represent mainly deposits placed by residents abroad or loans granted by resident institutions to non-residents. For liabilities, the reduction observed in 2014 was due to decreases in "currency and deposits". In the case of assets, the small increase was mainly due to "loans" and "trade credit and advances".





The main financial instruments included in the OI category are reported in **Chart 22**. These include "loan/currency and deposits", "trade credits" and "other" assets and liabilities. As already noted, in both assets and liabilities, the great majority of OI concerned "loans/currency and deposits". Assets in this category increased to €53.288,0 million while liabilities decreased to €69.668,3 million by the end of 2014. In the case of liabilities the amounts are

mostly associated with loans provided by non-resident MFIs to "other sectors" entities in Cyprus.

CHART 22 Other investment assets and liabilities 2008 - 2014
(€ million)

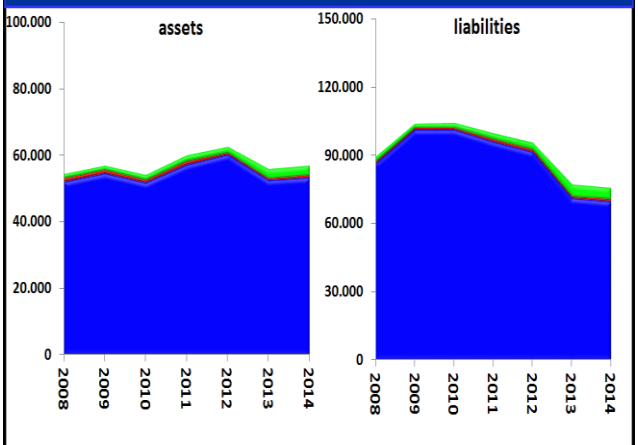
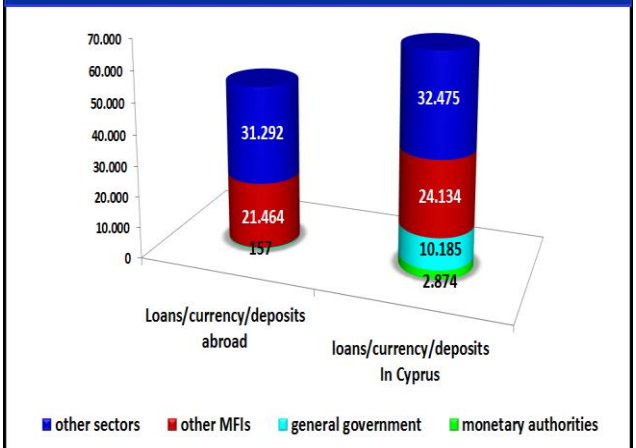


CHART 23 Loans, currency and deposits 2014
(€ million)



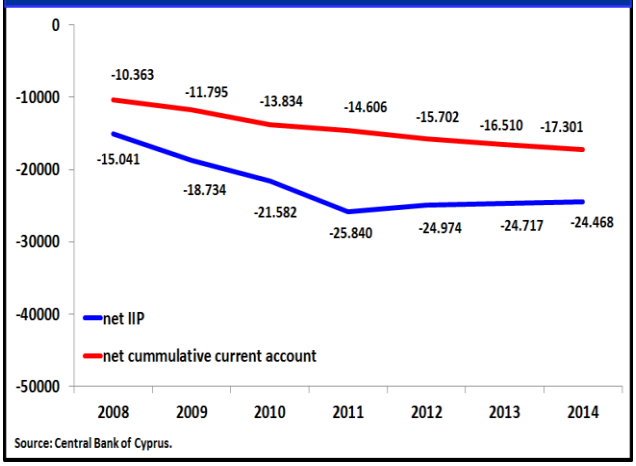
A sector level decomposition of "loans /currency and deposits" is illustrated in **Chart 23** using data for 2014. "Other sectors" owned most of the "loans/currency and deposit" assets abroad (€31.291,6 million which corresponds to 59% of the total amount). For "loans/currency and deposits" in Cyprus (liabilities), the respective amount (placed by non-residents with resident MFIs) was €32.475,4 million (47% of the total amount associated with this category). Furthermore, in the case of liabilities an amount equal to €24.133,8 million was attributed to "other MFIs".

3. INTERNATIONAL INVESTMENT POSITION (IIP)

- **The negative balance in the net IIP decreased to €24.468 million in 2014.**
- **In contrast, the cumulative net current account deficit increased slightly.**
- **The negative position in the net IIP is mainly driven by the liability positions in "other" and foreign direct investment.**
- **Foreign direct investment remains the most important component of the IIP, which however declined in 2014.**

Cyprus's liabilities towards the rest of the world remain significantly higher than foreign assets owned by its residents. This is primarily due to debt associated with ship-owning SPEs and obtained from non-domestic sources. The negative balance in the net IIP dropped to €24.468,1 million in 2014 (**Chart 24**), compared with €24.717,4 million in 2013. However, at the same time there was a worsening in the cumulative net current account deficit, which increased to €17.301,4 million in 2014 (it was €16.509,9 million in 2013).

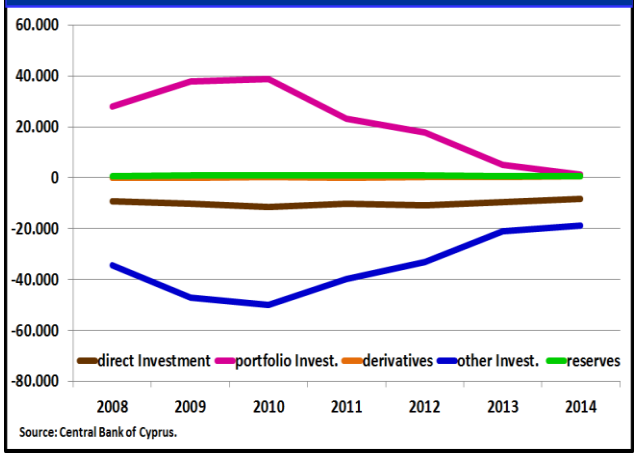
CHART 24 Cyprus's net cummulative current account and net IIP 2008 - 2014
(€ million)



The values of external assets and liabilities are influenced by changes in market prices, exchange rates, reclassifications and other volume changes. Therefore, developments in the IIP account may not reflect fully developments in the current account.

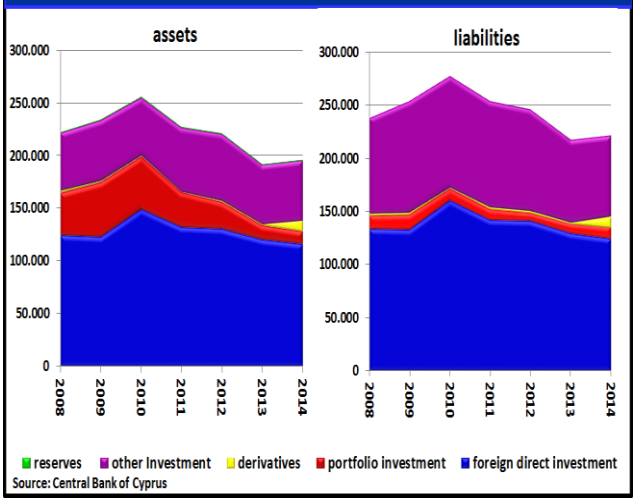
As shown in **Chart 25,** the negative net IIP position is almost exclusively due to the large net liability position in OI (there are also small negative values in the direct investment category). Most of the liabilities in this category concerned loans as well as currency and deposits placed by non-residents with resident MFIs. On average, for the period under consideration, the net stock balance for direct investment was -€9.988,0 million and for "other" investment -€34.885,0 million. The net IIP positions with respect to PI, derivatives and reserves were positive with average values for the period at €21.702,2 million, €159,3 million and €817,8 million, respectively.

CHART 25 Net IIP stocks by category 2008 - 2014 (€ million)



In order to gain more insights into the asset and liability positions, these are further analysed in **Chart 26** by investment component. Foreign direct investment provided the highest contribution in both assets and liabilities. However, foreign direct investment assets decreased from €119.805,2 million in 2013 to €115.975,2 million in 2014 and foreign direct investment liabilities from €129.321,8 million in 2013 to €124.346,1 million in 2014. During the same period OI increased by 2% in assets but decreased by 2% in liabilities (to €57.253,3 million and €75.901,8 million respectively). There was also a decrease in PI assets, but the stock levels associated with this investment category are small when compared with OI and FDI.

CHART 26 International investment position assets and liabilities 2008 - 2014 (€ million)



4. EXTERNAL DEBT

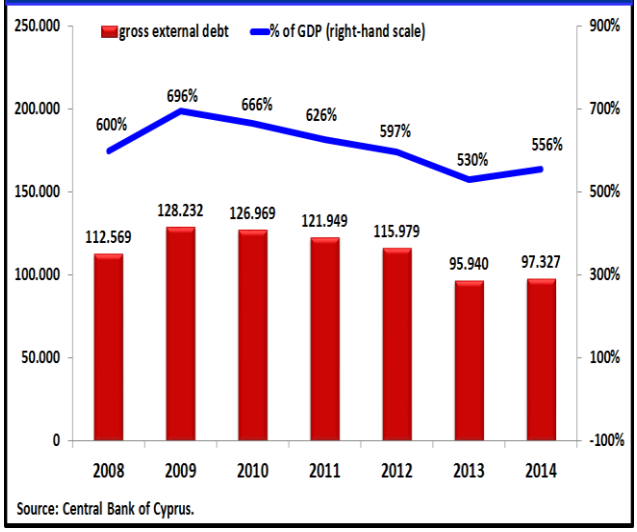
- **Cyprus's gross external debt increased to €97.327,3 million in 2014.**
- **"Deposit taking corporations" and "other sectors" continue to be the major holders of external debt.**
- **The holdings of these institutions consist primarily of currency, deposits and long-term debt.**

Cyprus's gross external debt[3] increased in 2014 (**Chart 27**). It was €95.940,3 million in 2013 but rose

[3] External debt includes, among other things, non-resident deposits, which are covered by strict prudential regulations issued by the Central Bank of Cyprus. The regulations require MFIs to maintain a substantial part of

to €97.327,3 million by the end of 2014, which corresponds to 556% of the country's GDP. As explained above, for the negative net IIP position, part of this debt is associated with ship-owning SPEs. "Deposit taking corporations" and "other sectors" were the major holders of external debt with €24.179,1 million and €44.271,7 million, respectively. There was also a €12.478,3 million holding by the "general government" in 2014, which represents an 18% increase compared to its holding in 2013 (€10.616,6 million).

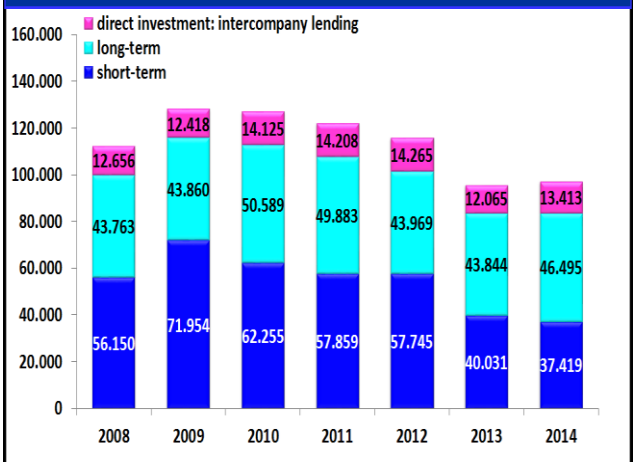
CHART 27 Cyprus's external debt 2008 - 2014
(€ million)



Source: Central Bank of Cyprus.

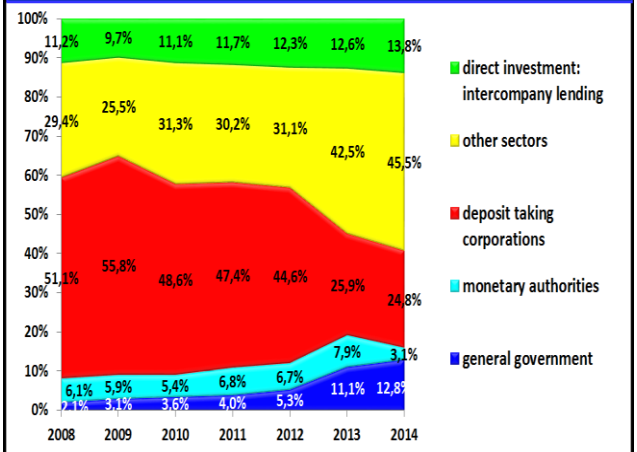
In general, gross external debt can be divided into the following three categories (**Chart 28**): (i) long-term debt; (ii) short-term debt; and (iii) direct investment intercompany lending. Cyprus's gross external debt during the last two years consists mostly of long-term debt. By the end of 2014, long-term debt amounted to €46.495,4 million and corresponded to 62% of the total amount of external debt in 2014. The decline in the total amount of external debt observed in 2013 was mainly driven by the reduction in short-term debt, which dropped by €17.714,5 million between 2012 and 2013.

CHART 28 Composition of external debt 2008 - 2014
(€ million)



Source: Central Bank of Cyprus.

CHART 29 External debt contributions by sector 2008 - 2014
(€ million)



Source: Central Bank of Cyprus.

Gross external debt is further decomposed in terms of sectors in **Chart 29**. With a share of 24,8% at the end of 2014, "deposit taking corporations" are no longer the major holders of external debt. The contribution by the "other sectors" entities increased

their non-resident deposits in liquid assets. Prudential regulations regarding foreign currency deposits are even stricter.

significantly during the last three years, reaching 45,5% of the total volume of external debt by the end of 2014. With regard to the financial instruments associated with each category, most of the holdings by “other sectors” entities concerned long-term loans, while in the case of “deposit taking corporations” most of the holdings concerned currency and deposits.

Appendix: BPM6 methodology

In 2014 the Central Bank of Cyprus (CBC) adopted the Balance of Payments and International Investment Position Manual, Sixth Edition (BPM6), published by the IMF. The aforementioned revision of the manual was deemed necessary in order to capture several important developments that have occurred in the years following the publication of BPM5.

In particular, BPM6 takes into account economic developments associated with globalisation, financial and technological innovations, and places increasing emphasis on the use of the balance sheet in examining vulnerabilities. Furthermore, it introduced the concept of economic ownership. In general, the new manual provides enhanced clarification, elaboration and level of detail to the balance of payments (BoP) / International Investment Position (IIP) statistical framework.

The BPM6 has been revised and updated in parallel with the United Nations’ System of National Accounts 2008 (2008 SNA) and the European System of Accounts (ESA 2010) This is in order to enhance consistency and ensure data comparability between international accounts and national accounts, strengthening the integration of all sets of macroeconomic statistics.

The implementation of the new manual provides the opportunity for further changes and benchmark revisions, aimed at the improvement of the coverage and quality of the data produced. The most important change concerns the incorporation and publication of data on "special purpose entities" (SPEs) registered in Cyprus. As a result of this change, all the statistics produced and published thereafter by the CBC, shall include data on SPEs which are registered / incorporated in Cyprus.