

Key messages:

- **Robust GDP growth:** 3.6% for 2017 and 3.0% for 2018.
- **Adequate primary surpluses** together with cash buffers built the last two years to reduce the public debt (average 3% within the SP period).
- **Debt fell below 100%** of GDP but remains high.
- Risk of **marginal deviation** of the 2018 MTO. Over performance over forecasts.
- **Lack of competitiveness, high debt and NPL's** highlight the **need for reforms**

Macroeconomic outlook

The economy of Cyprus is projected to expand by 3.6% and 3.0% in real terms for 2017 and 2018, respectively. These performances are primarily driven by consumption that will continue to provide a positive contribution to growth, mainly due to labour market developments, as well as the secondary effects from export oriented services sectors. Investment growth is estimated to continue contributing positively to growth. In particular the construction sector benefited from government incentives. Inflation, measured by HICP, is forecast to turn positive in 2017 rising to 1.1% and then to marginally decline to 1.0% in 2018.

Given the high level of public and private debt and of the high level on NPL's Cyprus is vulnerable to external shocks and will be negatively affected by a possible tightening in the Eurozone monetary policy. Most indicators highlight the lack of competitiveness of the Cyprus economy and the need to proceed with reforms for both the government and private sectors.

Short term fiscal outlook

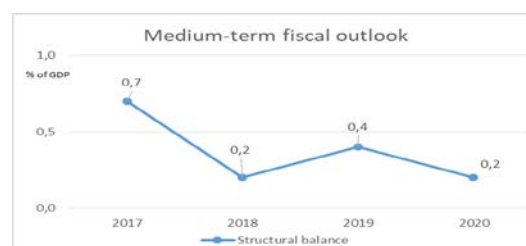
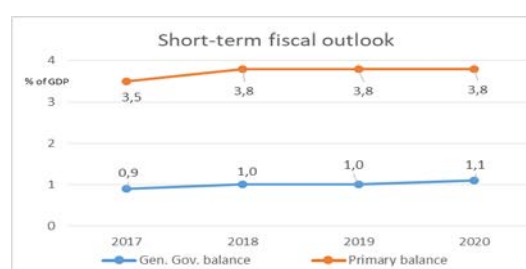
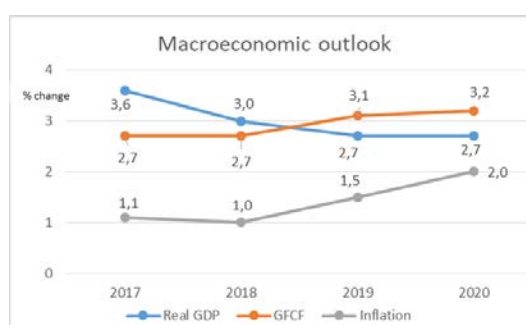
The more favourable than anticipated macroeconomic environment in conjunction with the measures taken during the MoU period, has contributed to the over performance of the fiscal targets that were set out, and the compliance with the national and the European fiscal frameworks. The general government balance in 2017 is estimated to be 0.9% and 3.5% primary balance of GDP compared to 0.4% and 3.0% primary balance in 2016, respectively. Pre-election period measures and commitments are expected to have a negative impact on public finances but still Cyprus is expected to comply with fiscal rules.

Medium-term fiscal outlook

During the latest Stability Program period, the MTO remains unchanged, i.e. a balanced position (0.0% of GDP) in structural terms. The government's fiscal policy stance is based on a macroeconomic scenario, which locks in the fiscal achievements and the respect of the national MTO over the medium-term. It is expected to safeguard the maintenance of a healthy primary balance position, with the aim to enhance credibility, thus facilitating access to the international markets. The structural balance in 2017 is estimated to be 0.7% of GDP fulfilling the MTO criterion (0%), whilst for 2018 is projected to decline to 0.2%.

Fiscal framework and national fiscal rules

Government debt fell last November below the 100% psychological barrier and is expected to decline further. It is projected that debt to GDP ratio will decline below the 60% mark by 2028. The government has accumulated substantial cash reserves and it is possible to reduce debt at a faster pace.



Key indicator forecast

| | | 2015 | 2016 | 2017f | 2018f | 2019f | 2020f | Source |
|----------------------------------|------------|-------|-------|-------|-------|-------|-------|---------------------------|
| Real GDP growth rate | [% y-to-y] | 1,7 | 2,8 | 3,6 | 3,0 | 2,7 | 2,7 | 1: Budget 2018 |
| Output Gap | [%] | -4,1 | -1,5 | 0,5 | 1,5 | 2,0 | 2,3 | 2: Stability Program 2017 |
| GG balance - MoF est. | [% of GDP] | -1,2 | 0,4 | 0,9 | 1,0 | 1,0 | 1,1 | 1 |
| GG debt - MoF est. | [% of GDP] | 107,5 | 107,8 | 102,7 | 97,9 | 93,3 | 88,4 | 1 |
| GG structural balance - MoF est. | [% of GDP] | 0,8 | 1,1 | 0,7 | 0,5 | 0,4 | 0,2 | 1 |
| GG revenue | [% of GDP] | 39,2 | 39,2 | 38,6 | 38,4 | 38,4 | 37,9 | 2 |
| GG expenditure | [% of GDP] | 39,3 | 38,9 | 38,4 | 38,0 | 38,0 | 37,4 | 2 |