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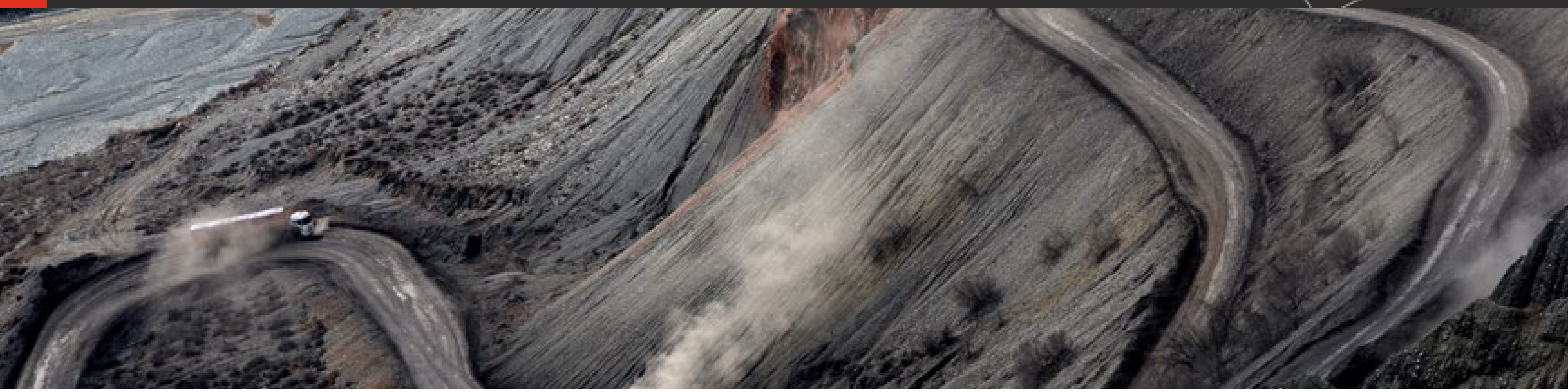
COVID-19

Impact of the pandemic on the Cyprus Economy

13 May 2020



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Foreword

The COVID-19 pandemic in addition to the upheaval it caused to peoples' lives, families and communities and its continued health threat, it also has a significant impact on businesses and the economy. At PwC, we are working closely with businesses to help them mobilise, stabilise and return to work. As businesses are working on their scenario planning it's important to have a sense of the potential economic impact.

The Cyprus specific results of our recent CFO Pulse Survey revealed that CFOs are greatly concerned about the effects of COVID-19 on their operations. Around 83% of Cypriot CFOs expect their revenues to decrease and at the same time 52% of Cyprus CFOs believe their company could get back to "business as usual" within 3 months if COVID-19 were to end today.

To better understand the potential economic impact from COVID-19 on Cyprus, we carried out a scenario based impact analysis in collaboration with the Economics Consulting team of PwC UK. We base this on two scenarios, in line with the latest thinking of epidemiologists and economic policymakers.

More importantly, we fill in a gap in the volume of analysis for the economy overall and also for sectors of the Cyprus economy. Our analysis is based on what businesses have been experiencing in Cyprus, with insights from our sector experts and wider stakeholders.

As the COVID-19 pandemic continues to evolve, appreciating the potential economic impact on the basis of various scenarios will go a long way to assist businesses shift focus to efforts that support a return to work, while addressing needed changes in the months ahead. In these challenging times we will stand by you and we will continue to focus on building trust in society and solving important problems leveraging the insights and expertise of our international network.

Constantinos Constantinou
Head of Advisory
PwC Cyprus

Executive Summary

2020 GDP impact (YoY*)

Scenario 1 (Shorter lockdown)	Scenario 2 (Longer lockdown)
-7.6%	-13.5%
+7.6%	+8.7%

2021 GDP impact (YoY)

* (YoY) – Year on Year

(1) Any references to GDP impacts made in this report relate to GDP in real terms

-8.5% GDP impact (2012 to 2014)

Expected GDP impact under Scenario 1 is broadly similar to the 2013 crisis, while under Scenario 2 impact is expected to be much greater.

ECONOMY-WIDE IMPACT[1]

In our report, we assess two scenarios as regards lockdown measures due to COVID-19. Scenario 1 relates to actual recent announcements regarding the lifting of restrictions, while Scenario 2 relates to a longer lockdown period in the event that there is another surge in virus cases.

Under both scenarios, GDP in real terms is expected to be significantly lower in 2020 as compared to 2019 (-7.6% for Scenario 1 and -13.5% for Scenario 2). As for 2021, under Scenario 1 GDP in real terms is expected to grow by 7.6% compared to 2020 and be marginally lower than in 2019 (-0.6%); under Scenario 2, GDP in real terms is expected to grow by 8.7% compared to 2020 and continue to be lower compared to 2019 (-5.9% lower).

It is noted that, under both scenarios, 2020 and 2021 GDP is expected to be well below the pre-pandemic expectations based on forecasts (i.e. IMF pre COVID-19 forecasts 2020:+ 2.9%, 2021:+ 2.7%). Specifically, when compared to the pre COVID-19 estimates, 2020 GDP is lower by 10.1% and 15.9% and for 2021 by 6.0% and 11.0% under Scenarios 1 and 2 respectively.

SECTOR IMPACTS

Most adversely impacted sectors	GVA % drop (2020 vs 2019)
Hotels & Restaurants	-60% to -93%
Real Estate[2]	-17% to -24%
Construction	-13% to -29%
Wholesale & Retail Trade	-18% to -30%

(2) The impact on the real estate sector is mitigated by the fact that c.60% of this sector's GVA relates to imputed rents of owner-occupied dwellings which is not affected by the COVID-19 crisis

Contents

1 Setting the scene

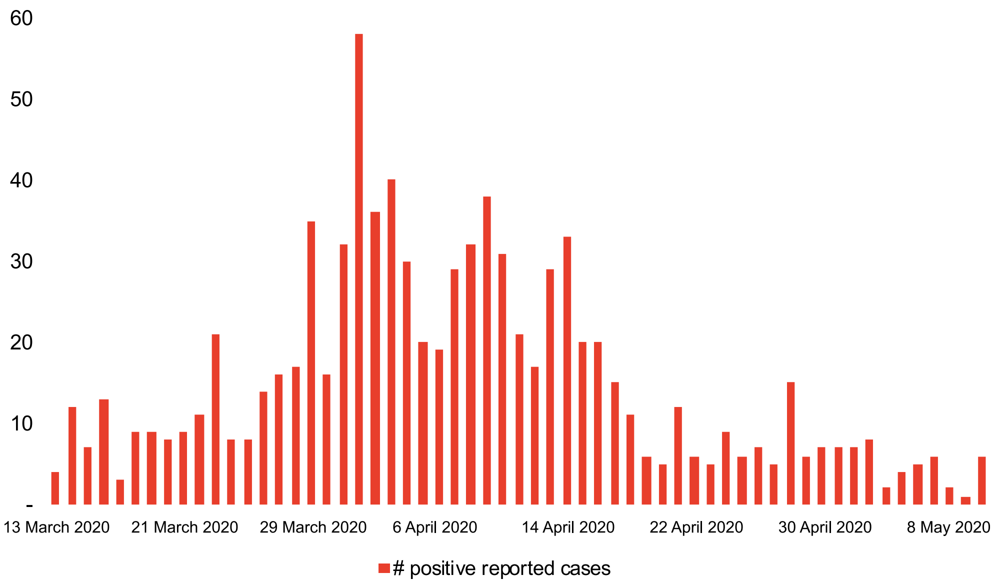
COVID 19 - Key facts & figures: Cyprus fared better compared to many European countries (1 of 2)

CY Covid-19 (as at 10 May 2020)

898	16	401	> 76k
Positive reported cases	Deaths [1]	Recoveries	# COVID-19 tests

(1) 16 reported deaths as per covid19.ucy.ac.cy; figure rises to 21, by adding deaths not directly attributed to COVID-19

Cyprus # positive reported cases as at 10 May 2020



Source: UCY (covid19.ucy.ac.cy), European Centre for Disease Prevention and Control

COVID 19 - Key facts & figures: Cyprus fared better compared to many European countries (2 of 2)

Covid-19 around the Globe

212

Affected countries

CY Ranking (as at 10 May 2020)

64th

In reported cases/ 1M pop

62nd

In deaths/ 1M pop

COVID-19 stats comparison as at 10 May 2020

Country	Cases / 1M pop	Deaths / 1M pop	Tests / 1M pop
World	**540**	**36.5**	**N/A**
Spain	5,735	572	52,781
Usa	4,133	244	28,536
Italy	3,623	505	42,439
Uk	3,229	469	26,829
Portugal	2,715	112	50,767
France	2,711	404	21,213
Germany	2,051	90	32,891
Israel	1,905	29	53,342
Turkey	1,644	45	16,251
Russia	1,517	14	38,625
Cyprus	744	13	63,062
Bulgaria	285	13	8,295
Greece	261	14	9,488
Egypt	92	5	879
China	58	3	N/A

Cyprus has undergone much more extensive COVID-19 testing by comparison to many other countries. This is significant to consider when comparing Cyprus to other countries as regards the number of positive reported cases/1M pop.

Source: Worldometers

- The numbers above are dependent on the level of testing performed by each country
- It is noted that there may be COVID-19 cases that have not been officially reported and/or may have been omitted for the purposes of the above table
- Data may also be subject to retrospective corrections

Timeline of Covid-19 outbreak: lockdown measures and government support packages in Cyprus

The first outbreak of COVID-19 in Cyprus on the 9th of March was followed by a series of Government measures including social distancing, sector lockdowns and travel bans.

March 2020

09 — **First COVID-19 Case**
First 2 positive reported cases of COVID-19 in Cyprus

10 — **Stay at home**
First set of social distancing guidance

15 — **Travel Restrictions**
Inward travel restrictions & 14-day quarantine for new arrivals

16 — **First set of government measures**
Sector lockdowns
Education
Hospitality & Leisure
Retail (non-food)
(exceptions apply)
Personal care services

21 — **First Death**
First COVID-19 related death

Travel Ban
Complete inward travel ban excluding cargo imports/exports

24 — **Stricter lockdown measures**
Restriction on movement (notification to Authorities via sms for going out)

Additional sector lockdowns
Public areas
(Churches, beaches, marinas, playrounds, parks, excursion areas, open sports areas, open markets)
Construction sites
(exceptions apply)

27 — **Fiscal support packages**
Parliament voted the first set of fiscal measures amounting to €823m, as presented in page 9

29 — **Monetary Response**
Parliament approval of suspension/deferral of loan instalments till Dec 2020

April 2020

1 — **Peak of COVID-19 cases**
#58 of positive reported cases

24 — **Extension of travel bans**
Announcement of Ministry of Transport extension of travel bans until 17 May

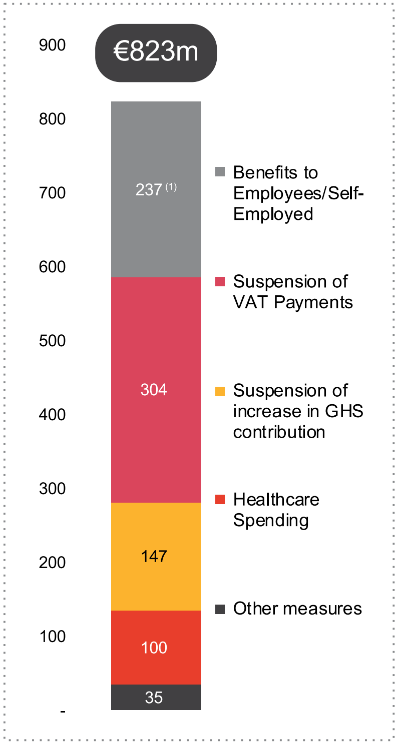
May 2020

10 — **Cases & deaths as of today**
898 positive reported cases
16 deaths
401 recoveries

Source: Government Decrees, Official announcements, press releases and media reports

Fiscal Response

The COVID-19 Fiscal Support Package announced by the Government mainly comprises the following:



(1) Covers the period 16 March -12 April 2020

Source: Ministry of Finance and official Government statements

Benefits to Employees/ Self-Employed
€237m

- Special Unemployment Benefit
- Special Leave Benefit for parental leave
- Special Sickness Benefit
- Special Benefit for the Self-Employed

For more information click **here**

- The figure of €237m for benefits to employees and the self-employed, relates to planned support until 12 April; the actual amount of the fiscal support package may increase, depending on the lockdown duration and the Government's fiscal capacity.

Suspension of VAT Payments
€304m

- Temporary suspension of the obligation to pay VAT until 10 Nov 2020, for the periods ending 29 Feb to 30 April 2020
- Applies to all taxable persons except taxable persons other than those whose activities fall within specific trading categories

For more information click **here**

Suspension of increase in GHS contribution
€147m

- Suspension of the increase in GHS (General Health System) contribution for 3 months (April - June 2020)
- The increased contribution rates will apply for March 2020

Healthcare Spending
€100m

- Employment of additional medical, nursing and support staff
- Investment in equipment and material infrastructure
- Reinforcement of the Institute of Neurology and Genetics in human resources and in material infrastructure
- Reinforcement of Ambulance Centre and Service 1420

Other measures
€35m

- Support for tourism recovery
- Support to students abroad
- Repatriation of citizens abroad
- Allowance for employees of the Ministry of Education working in afternoon programmes

Other measures - not quantified

- Deferral of annual company registration fee
- Support for recovery of agriculture, culture, fishing services etc
- Reduction of the electricity tariff by 10% for a period of 3 months

Monetary Response

Suspension/ Deferral of loan repayments

Date passed in Law:
29 Mar 2020

Period Effective:
30 Mar 2020 - 31 Dec 2020

- The suspension/deferral of loan repayments (capital and interest) is for a period of 9 months (up to 31 Dec 2020).
- Applies to borrowers whose delays as at 29 Feb 2020 do not exceed 30 days from the last date of payment of their instalments.
- The interest amount that is suspended/deferred, will be added to the loan balance at the termination of the measures (i.e. 31 Dec 2020) and the total capital and interest amount that has been suspended will not be immediately payable, unless agreed otherwise between the borrower and the financial institution.
- On April 3rd 2020, and following guidance by the Central Bank of Cyprus, the Association of Cyprus Banks announced that suspended/deferred interest instalments will not accrue interest during the period of suspension.
- As per the Minister of Finance, this measure could potentially affect €16bn loans. As at 24 April 2020, the Minister of Finance announced that requests for suspension of loan instalments reached 50k amounting to €10bn.

ECB/CBC relief measures

Date announced:
ECB (€1.2bn): 31 Mar 2020
CBC (€90m): 10 April 2020

Period Effective:
ECB (€1.2bn): 31 Mar - 31 Dec 2020,
CBC (€90m): Jan 2021

- The ECB and CBC Relief Measures result to a capital relief for Cyprus banks of c.€1.3bn and these enable the banks to provide much needed liquidity through the granting of new credit facilities. For more information click **here**.
- The purpose of such credit facilities is to meet current needs for liquidity, working capital, salaries, rents, payables to suppliers but excluding the repayment of existing loans. Facilities could also cover investment needs of businesses and individuals.
- At an ECB level, it is noted that the ECB has launched the Pandemic Emergency Purchase Programme (PEPP) which comprises a Quantitative Easing Programme in the region of €750bn.

Suspension of Foreclosures

Date announced:
18 March 2020

Period Effective:
18 March 2020 - 18 June 2020

- In line with the decision made by the Association of Cyprus Banks (ACB), temporary suspension of 3 months of the foreclosure process by banks, the State-owned management company KEDIPES and other credit acquiring companies until 18 June 2020.

Source: Media reports and official government statements, Association of Cyprus Banks (ACB)

PwC CFO Survey COVID-19 : A cause of considerable concern amongst Cypriot CFOs

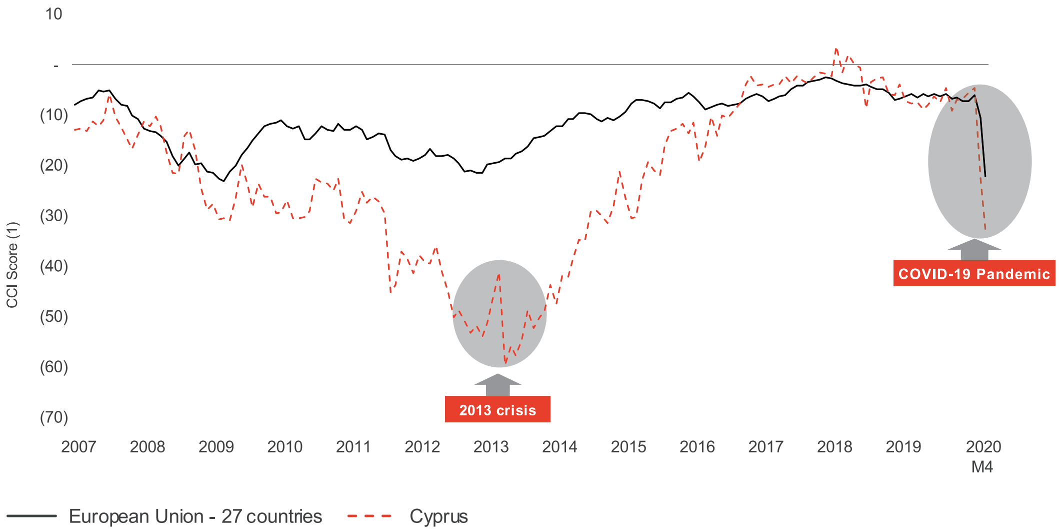
During this bi-weekly survey, conducted by PwC Cyprus as part of a global PwC effort / initiative, Cyprus participated with 45 CFOs who were surveyed for the round taking place between 20 and 22 of April. For the full report, click **here**.

Key Findings

- Nearly three-quarters (78%) of respondents are greatly concerned about the effects of COVID-19 on their operations, while only 9% view it as an isolated challenge.
- 69% of CFOs expect a decrease in their company revenues and/or profits as a result of COVID-19, while only 4% of them expect an increase in their revenues.
- The majority of the CFOs (around 69%) consider implementing cost containment, while only 11% are not considering any financial actions.
- 62% of the respondents believe that their company could return to 'business as usual' within three months if the crisis were to end today, while only 4% believe that it will take more than a year.
- 73% of CFOs are concerned about potential recession.
- 42% of the participants mostly expect their companies to have changes in staffing the following month.

Consumer Confidence Indicator has dropped sharply in Feb to April 2020

Consumer Confidence Indicator (CCI) 2007- 4M 2020



(1) Represents the degree of optimism that consumers have on the state of the economy, expressed through their activities of saving and spending

Commentary

- As result of the COVID-19 pandemic and the strict restrictive measures adopted, the Consumer Confidence Indicator (CCI) in Cyprus and the European Union, has experienced a sharp drop since Feb 2020. In Cyprus, the CCI dropped from -4.4 in February to -22.6 in March and subsequently to -32.5 in April 2020.
- The Cypriot CCI had also experienced a very sharp drop during the 2013 crisis. It is worth noting that it took about 3 years for this Indicator to reach 2007 pre-crisis levels.
- Following the sharp drop in Q1 2020, it is uncertain how quickly consumer confidence will return to pre COVID-19 levels. This depends greatly on whether the virus will continue to be under control, avoiding further restrictions on economic activity and performance of key sectors.

Distinct differences in economic landscape and policy response between 2020 and 2013 (1 of 2)

	2020 Crisis	2013 Crisis
Economic Fundamentals	• More robust economic fundamentals, with economy on a growth path up until the COVID-19 crisis; this is the key reason for a potential recovery in 2021, compared to 2013.	• Significant fundamental weaknesses meant that the economic recession continued also in 2014.
Fiscal Position	• State in a strong fiscal position, enabling it to support businesses and individuals in a number of ways, preventing also a significant rise in unemployment, unlike the 2013 - 2014 experience. • State has access to the international markets, and has recently raised €1.75bn (in April 2020) and €1.25bn from Cypriot banks.	• State had significant fiscal weaknesses, with budget deficit and public debt at high levels. • Access to international markets was severely limited. • The State could not support struggling businesses and individuals, leading to increased corporate distress and a significant rise in unemployment.
Banking Landscape	• Although NPLs are still a dominant challenge, banks are in a much stronger position than 2013. • Banks have ample liquidity and stronger capital position to fund the economy. In addition, significant consolidation has been observed, further strengthening the remaining banks and the sector overall. • Central Bank of Cyprus and relevant European authorities (EBA and ECB), reacted promptly by granting certain relaxations (i.e. reduction in capital requirements or definition of NPLs) to give banks the ability to deploy their liquidity in the economy. Specifically for the Cypriot banking sector, banks were provided with a capital relief of c.€1.3bn, enhancing further their ability to provide funding and/ or absorb losses in loan restructurings.	• Banking sector was weak and vulnerable, both in terms of capital and liquidity; in addition, the bail-in of uninsured depositors had caused a significant decline in the confidence to banks. • As a result, not only the banks could not support the economy, but a substantial part of the country's wealth in terms of deposits and its ability to repay existing debt was lost due to the bail-in.

Distinct differences in economic landscape and policy response between 2020 and 2013 (2 of 2)

	2020 Crisis	2013 Crisis
Local Vs Global Issue	• The COVID-19 pandemic is a global issue, affecting all economies in Europe and beyond. The EU Commission and ECB therefore are adopting more flexibility in terms of fiscal and monetary supervision, which is expected to foster economic recovery.	• In 2013, Cyprus was an isolated case (in addition to a few other southern Eurozone members, each to a different degree); Global/Eurozone institutions were stipulating stringent requirements for Cyprus to help its fiscal and monetary stability.
Speed of response	• Authorities reacted speedily to combat the 2020 crisis, both in terms of dealing with the health hazard (i.e. early adoption of lockdown measures), as well as with the adoption of an appropriate fiscal and monetary response. The former prevented the spread of the virus to an uncontrollable level, while the latter provided a much needed liquidity boost to the economy.	• The State and relevant Regulators did not react effectively before the fiscal and monetary situation became unsustainable; when the deep-rooted problems culminated in the March 2013 crisis, it was too late to reverse the trend, and the weak position of the State and the banks meant that none could support the real economy.

Macroeconomic Projections by various organisations

Ministry of Finance

Forecasted Macro Indicator	06 May 2020	03 April 2020	14 April 2020	16 April 2020	April 2020 (3)	28 April 2020 (4)
Real GDP Change % 2020	7.4% contraction	3.5% contraction	6.5% contraction (vs. 7.5% contraction for the Eurozone)	6.0% contraction	7.0% baseline contraction (5.0% / 13.0% contraction under different scenarios)	7.0%- 14.0% contraction
Real GDP Change % 2021	6.1% growth	3.8% growth	5.6% growth (vs. 4.7% growth for the Eurozone)	5.0% growth	6.0% growth	N/A
Unemployment rate 2020 / 2021	8.6% / 7.5%	8.0% / 7.0%	8.8% / 7.4%	N/A	N/A	N/A
Budget deficit as % of GDP 2020 / 2021	10.9% / 10.1% (Current Account Balance)	7.3% / 0.7%	8.3% / 5.6% (Current Account Balance)	6.7% / 3.6%	4.3%/ N/A	N/A
Public Debt as % of GDP 2020 / 2021	115.7% / 105.0%	GGGD (1) increase somewhat in 2020 and could decline below 65% of GDP by 2028 (2)	N/A	108.0% / 105.0%	116.8% / 103.2%	N/A
Inflation rate 2020 / 2021	-0.2% / 1.0% (Consumer Prices Projections)	0.1% / 0.7%	0.7% / 1.0% (Consumer Prices Projections)	0.6% / 1.5%	-0.3% / 1.0%	N/A

Source: Publicly available information

(1) Gross General Government Debt

(2) Based on the assumption of 2% medium-term growth and primary surpluses, combined with a subdued increase in the marginal effective interest rates

(3) As regards the MoF projections, data has been obtained from the Stability Programme document (dated April 2020)

(4) Study undertaken by Eleni Andreou and George Syrichas - The Economics Research Centre of the University of Cyprus

Lifting of restrictions that affect economic activity

As per the official announcement by the President of the Republic of Cyprus on 29 April and the Minister of Health on 30 April, the lifting of restrictions is expected to take place in four phases. The lifting of restrictions timeline depends on the strict adherence to the epidemiological protocols and instructions of the Ministry of Health and the satisfactory performance of epidemiological KPIs.

May 2020

Phase 1

04

Increase in the permitted movements of citizens (authorisation through sms - max 3)

Re-opening of:
- Construction sites
- Retail stores (non-food) exept malls and big department stores
- Flea markets, street vendors and bazaars
- Tourist offices and tourist agencies
- Dental centres

11

Re-opening of schools (only for final year high school students)

Phase 2

21

Lifting of all restrictions of movement

Re-opening of:
- Schools
- Hairdressing salons and beauty centres
- Restaurants and cafes (outdoors only)

June 2020

1

Re-opening of:
- Ports excluding cruise ships
- Public libraries, museums, archaeological and historical sites
- Betting shops

Phase 3

09

Re-opening of:
- Shopping malls and department stores
- Airports and ports (including cruise ships
- Hotels
- Restaurants and cafes (indoor as well)
- Gyms
- Summer programmes of private higher education schools
- Open air theatres and cinemas

July 2020

13

Phase 4

14 onwards

Re-opening of:
- Casinos
- Theatres and cinemas
- Concerts
- Playgrounds
- Stadiums and Sports centres (closed to the public)

2 Economy-wide Impact

Economic Impact Assessment Methodology

Our assessment is based on macroeconomic analysis of each of five economic transmission channels. We have used a combination of sector expert insights and Input-Output (IO) modelling and overlays in relation to policy responses, to estimate overall impacts.

A The **five transmission channels** (set out in page 20)

	Assessed by
Sector partial or full lockdowns	IO model
Labour supply impacts	Overlay
Consumer spending	IO model
Business investment	IO model
Policy response	Overlay

We consider the five main transmission channels through which COVID-19 could impact the Cypriot economy.

B Each sector of the economy

- Hotels and Restaurants
- Financial and Professional Services
- Construction
- Real Estate
- Wholesale and Retail Trade
- Transportation and Storage
- Health and Social care
- Info and Communication
- Utilities
- Education
- Public Administration
- Manufacturing

We consider the short-term economic impact to the Cyprus GDP based on sector-specific demand and supply shocks.

In deriving the impact, we have gathered data and insights from key industry leaders and players in relation to the potential impact of COVID-19, as well as their expectations going forward.

Short term economic impact on

GDP (%)
2020 and 2021

Sector GVA impacts
2020

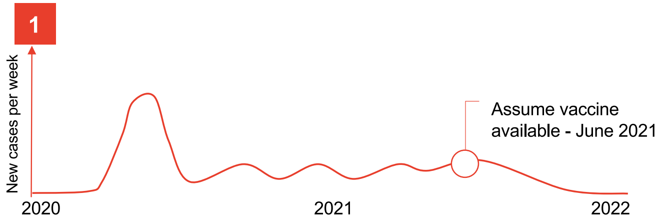
by considering the economic impact in **two different lockdown scenarios** and the relevant fiscal and monetary responses

Potential COVID-19 lockdown scenarios to inform economic impact analysis

We assess two scenarios that reflect a range of likely outcomes on the lifting of lockdown restrictions that are currently in place. The first scenario relates to actual recent announcements regarding the lifting of restrictions, while the second one relates to a longer lockdown period in the event that there is another surge in virus cases before the Summer. Both scenarios assume that the pandemic will not peak again in Autumn/ Winter season.

Shorter Lockdown - 2 months (Scenario 1)

NPIs introduced have a significant positive impact as regards the spread of the disease, which peaked in early April 2020.



Assumptions:

- Following an initial peak in early April 2020, successful implementation of Non-pharmaceutical interventions (NPIs) including testing, contact tracing, quarantine of cases and social distancing prevent an ongoing rapid increase.
- The Cyprus Government takes the steps towards relaxation of its measures/out of lockdown with reopening of sectors as follows (as per Government announcements on 29 and 30 April):

04 May: Construction sites, non-food retail stores re-open (excluding shopping centres)

21 May: Restaurants and cafes re-open (outdoor only), hairdressing and beauty salons

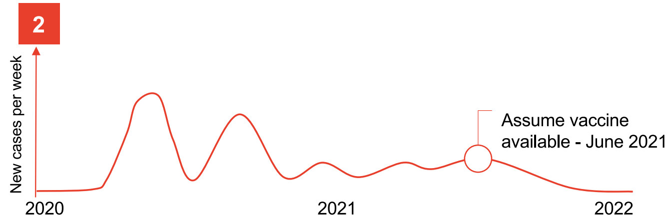
09 June -13 July Accommodation, cafes, bars and restaurants re-open in full, shopping centres, airports for tourist purposes (travel restrictions apply)

14 July +: Sports and entertainment centres re-open, casino re-opens

It is noted that despite the re-opening of airports, tourism flows are still expected to be significantly lower compared to 2019, as discussed later in the report.

Longer Lockdown - possibly 4 months (Scenario 2)

The implementation of NPIs is less successful, leading to a second peak and a more prolonged lockdown of an additional 1.5-2 months.



Assumptions:

- Weaker adoption of NPIs (for example, new surge of cases post early-May lifting of lockdown) leads to a second peak and a prolonged lockdown of an additional 1.5-2 months.
- As the virus peaks again, the Cyprus Government re-instates the lockdown, for a further period of an additional 1.5-2 months, compared to Scenario 1.

COVID-19 economic impact transmission channels

For the two scenarios presented, we modelled five main transmission channels through which COVID-19 could impact the Cypriot economy (the first four are negative, with an offsetting positive effect from monetary and fiscal policy responses). Other reinforcing and mitigating impacts are possible, so this is not an exhaustive list.

1. Sector partial or full lockdowns

- Significant periods of mandatory closures of construction sites, most retail outlets (except supermarkets and pharmacies), leisure, hospitality, sports and entertainment venues.
- The reduction in business activity due to lockdown leads to lower demand for outputs.

2. Labour supply impacts

- Social distancing measures, non-essential workers working from home for extended periods without adequate technological support, or workers staying at home to care for children or other dependents, which may have a negative impact on labour productivity.
- In addition, some workers may be sick and are unable to work, but these impacts are expected to be small given the low level of infection in Cyprus.

3. Consumer spending

- Consumers defer major purchase decisions and discretionary spend.
- Higher unemployment and lower earnings result in reduced levels of consumer confidence and lower consumer / retail spend overall.

4. Business investment

- Significantly reduced levels of business and consumer confidence result in a sharp and sustained downturn in business investment.
- Investment focuses on infrastructure and facilities to counter the pandemic and investment in digital ways of working (or new delivery models).

5. Policy response

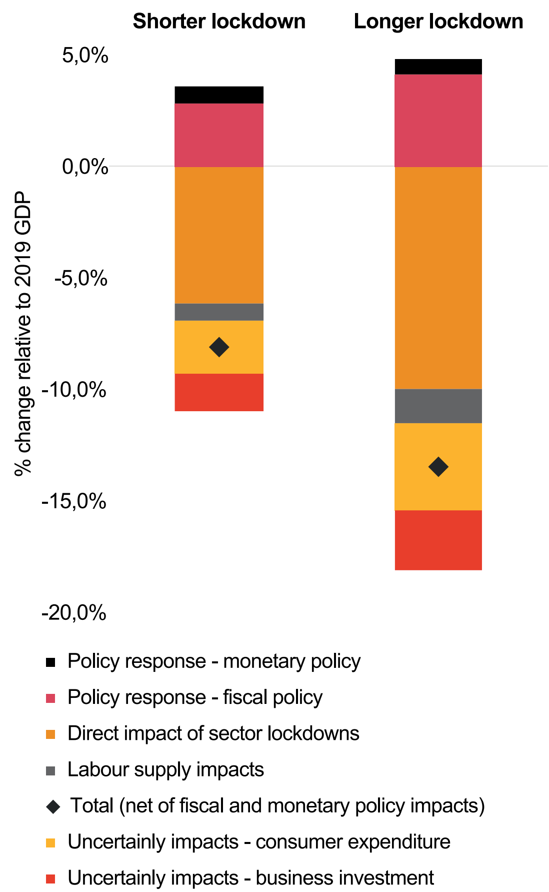
- Extensive working capital / cashflow support to businesses and individuals through the provision of unemployment benefits, deferral of loan instalments for certain borrowers and other relief measures (deferral of VAT payments has not been included in the fiscal response impact).
- Fiscal support for healthcare service.
- Looser monetary policy stance through additional quantitative easing, capital relief for Cypriot banks and other measures to boost credit flows to business / increase disposable income for individuals.

Illustrative scenarios for impact on Cyprus 2020 GDP

The combination of a full or partial lockdown in some sectors, labour supply impacts and uncertainty effects, offset partly by the injection stemming from policy responses, could reduce Cyprus GDP by 7.6% to 13.5% in 2020, relative to 2019 GDP.

Figures below are only illustrative of broad orders of magnitude and should not be taken as forecasts or predictions. Please see technical annex for more information on assumptions.

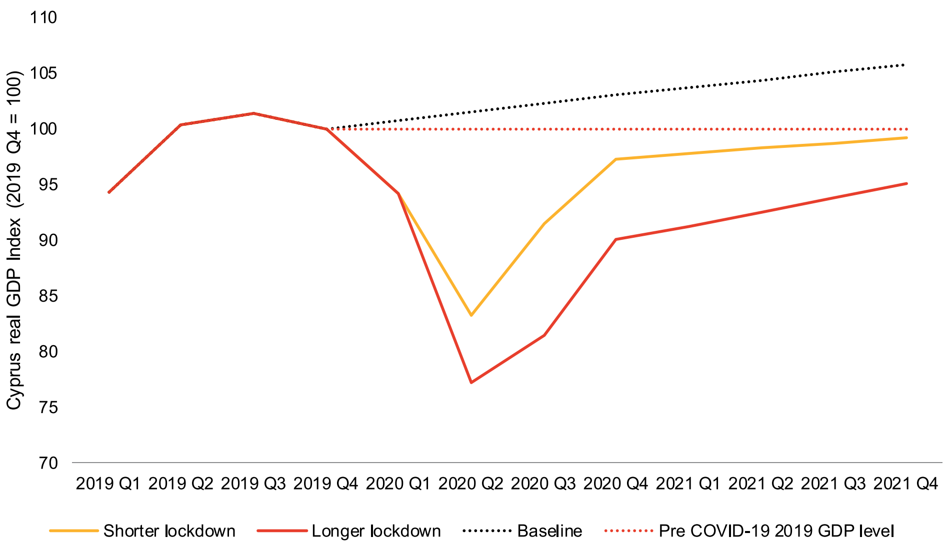
2020 impact (%) on Cyprus GDP relative to 2019 GDP	Scenarios	
	Shorter Lockdown	Longer Lockdown
1. Sector lockdowns	-6.1	-10.0
2. Labour supply impacts	-0.8	-1.5
3. Uncertainty-consumer expenditure	-2.4	-4.0
4. Uncertainty business investment	-1.6	-2.7
5. Policy response	Fiscal: 2.8 Monetary: 0.5	Fiscal: 4.2 Monetary: 0.5
Overall Cyprus economic impact	**-7.6**	**-13.5**



GDP will drop very sharply in Q2 2020… but is likely to recover in later periods

It is expected that the COVID-19 crisis will lead to a very sharp fall in GDP in Q2 2020, mainly driven by sector-based lockdowns, as well as lower consumer spending and business investment. Output is then expected to recover in Q3 and Q4 2020 on a quarter on quarter basis. In 2021, annual GDP growth could be around 7.6% and 8.7% in the shorter and longer lockdown scenarios respectively, although the pace of this remains highly uncertain.

Cyprus index GDP (Q4 2019: 100), quarterly levels in each scenario



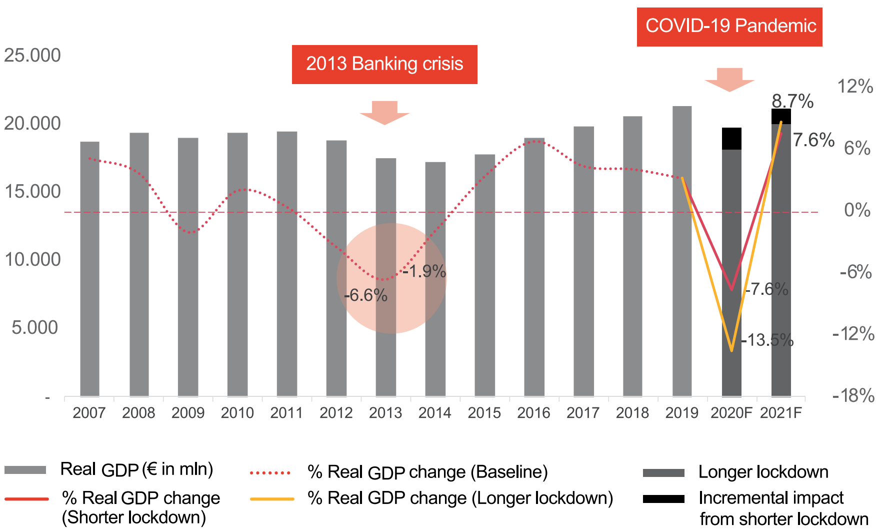
Source: National Accounts CyStat, PwC analysis

Commentary

- In the Shorter lockdown (Scenario 1) and Longer lockdown (Scenario 2), GDP could contract sharply in Q2 2020. We assume output would then recover quite fast at first as the lockdown is relaxed, followed by a more gradual pace of recovery later as economic life slowly returns to normal; 2021 growth % rate under the Longer lockdown scenario will be slightly higher than in the Shorter lockdown scenario, as GDP starts from a much lower base.
- Under both scenarios, GDP in real terms is expected to be significantly lower in 2020 as compared to 2019 (-7.6% for Scenario 1 and -13.5% for Scenario 2). As for 2021, under Scenario 1 GDP in real terms is expected to grow by 7.6% compared to 2020 and be marginally lower than in 2019 (-0.6%); under Scenario 2, GDP in real terms is expected to grow by 8.7% compared to 2020 and continue to be lower compared to 2019 (-5.9% lower).
- It is noted that, under both scenarios, 2020 and 2021 GDP is expected to be well below the pre-pandemic expectations based on forecasts (i.e. IMF pre COVID-19 forecasts 2020:+ 2.9%, 2021:+ 2.7%). Specifically, when compared to the pre COVID-19 estimates, 2020 GDP is lower by 10.1% and 15.9% and for 2021 by 6.0% and 11.0% under Scenarios 1 and 2 respectively.

Cyprus GDP contraction in 2020 is expected to be between 7.6% and 13.5% compared to GDP contraction of 8.5% during 2012 - 2014

Cyprus GDP and GDP % in real terms (2007-2021)



Source: National Accounts CyStat, PwC Estimates

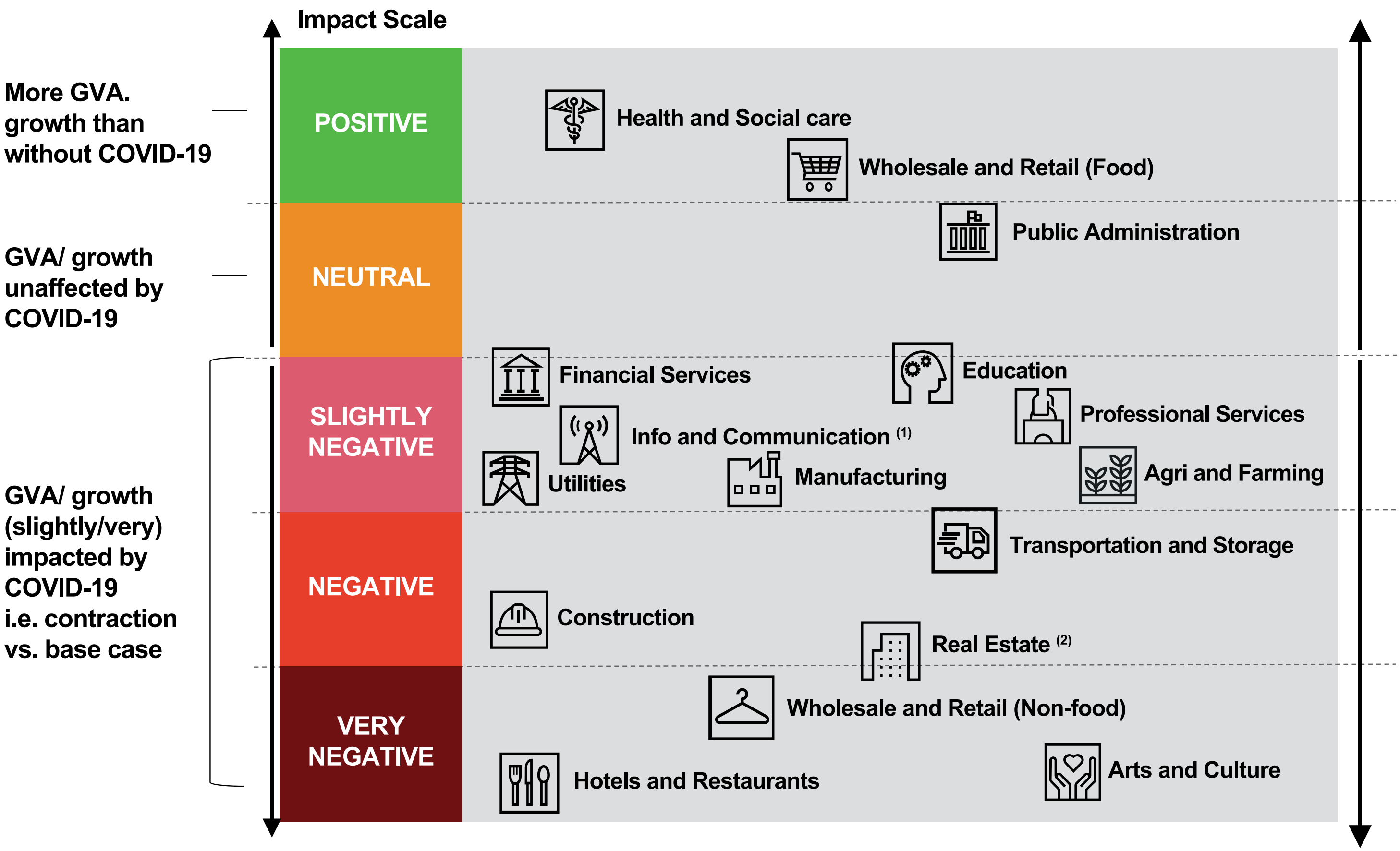
Cyprus GDP evolution

- The economic downturn in 2020 under the Shorter lockdown scenario is expected to be broadly similar to the 2013 economic recession, whereas the economic downturn is expected to be greater under the Longer lockdown scenario.
- According to these estimates, GDP is expected to drop by 7.6% and 13.5% under the two lockdown scenarios respectively, compared to the YoY fall of 8.5% experienced in 2013 and 2014 on a cumulative basis.
- This sharp decrease is after including the fiscal and monetary response in the current COVID-19 crisis, whereas in 2013 there was limited ability by the State and the banking sector to respond in the same way; had the State not been able to react, the disparity between the 2020 COVID-19 crisis and the 2013 crisis, in terms of GDP drop, would have been even higher.
- There are interesting sector impact comparisons between the two crises, which are shown on page 33 of this report.
- The economic growth in 2021 is expected to be higher compared to pre COVID-19 expectations, as there will be a significantly lower 2020 GDP base. However, and as mentioned on the previous page, the level of GDP in real terms will fall short of 2021 pre COVID-19 expectations in both lockdown scenarios.

3

Cyprus sector impacts

Expected impact on sectors in Cyprus



(1) includes telecommunications, TV & publishing activities, computer programming and other IT related activities
(2) c.60% of this sector's GVA relates to imputed rents of owner-occupied dwellings which is not affected by the COVID-19 crisis

Industry expectations and insights - Tourism

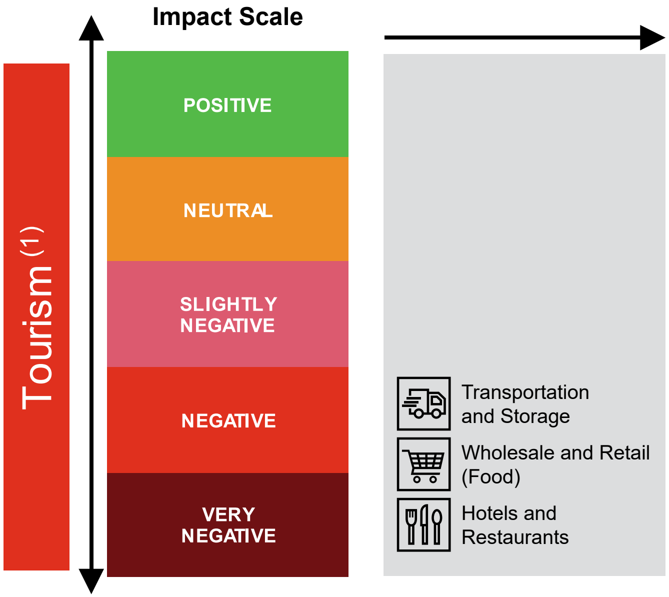
Tourism

c.6%

2019 Direct Contribution to GVA

Hotels and Restaurants

Key affected sectors by COVID-19

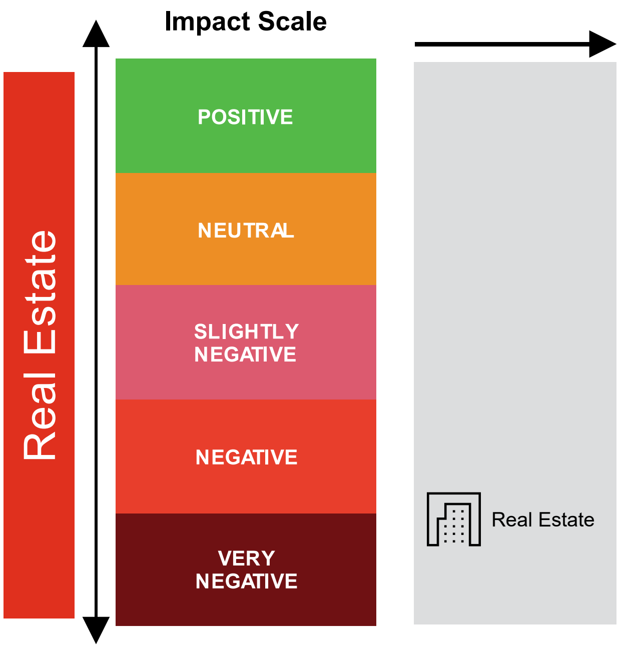


[1] Tourism predominantly affects the Hotels and Restaurants sectors with a smaller impact on Transportation and Storage and Wholesale and Retail sectors.

Key Industry Insights/ expectations

- Possibly the worst hit industry, with Cyprus facing the added drawback of being accessible primarily by air and, less so, by sea.
- Tourism predominantly affects the Hotels and Restaurants sectors with a smaller impact on Transportation and Storage and Wholesale and Retail sectors. There are of course significant indirect spill-over effects to other sectors of the economy such as Food Manufacturing, Financial Services, Professional Services etc that are accounted for in the sector specific GVA.
- Significant uncertainty as regards timing of lifting of travel restrictions, how airlines will perform this year and the appetite of tourists from key markets (in particular, there seems to be little clarity from our biggest markets namely the UK and Russia).
- Local hoteliers are still considering whether or not they will operate their hotels this year, as there needs to be a minimum occupancy level to render operations profitable while there are significant reputation and other risk considerations; perhaps hotel operators who have a number of hotels may choose to operate some of their hotels.
- The nature of the tourist experience will be different, as measures need to be taken to protect public health; we understand that the sector stakeholders are currently considering these issues.
- A positive message seems to be that in the eyes of European tour operators, Cyprus together with Greece, Malta and Bulgaria are perceived more favourably, due to the way COVID-19 was handled and the much lower number of cases, compared to countries with much higher tourism flows such as Italy, Spain, France and Turkey.
- The domestic market may be a positive factor without of course being able to replace foreign tourism; Cypriots made up 7% of guest nights in 2019, while there have been c.500k packages of Cypriots who travelled abroad in 2019.

Industry expectations and insights - Real Estate



Real Estate

c.5%

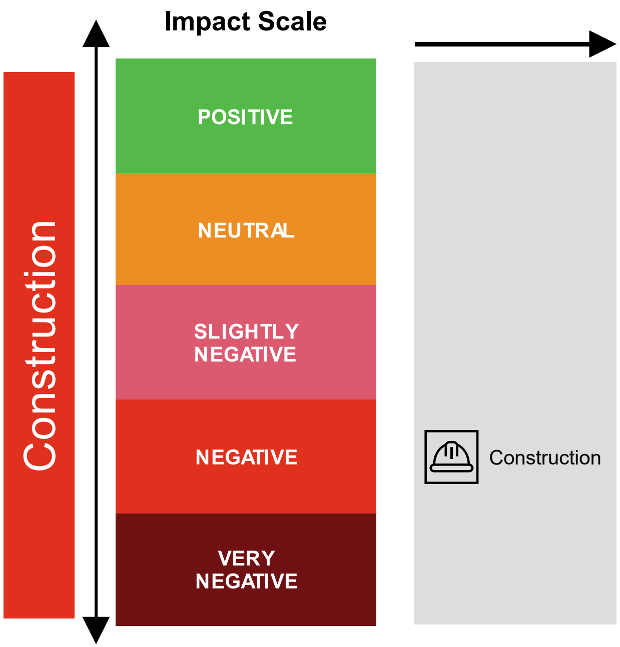
2019 Direct Contribution to GVA

Total real estate accounts for 11% of total 2019 GVA, out of which 6% relates to imputed rents of owner-occupied dwellings not affected by the COVID-19 crisis.

Key Industry Insights/ expectations

- Real estate transactions are expected to be reduced both in number and value, as both businesses and individuals may choose to defer significant investments in the face of increased economic uncertainty. It is noted that the number of transactions in Q1 2020 was already much lower compared to Q1 2019 (as Q1 and part of Q2 2019 had very strong performance) and COVID-19 has of course exacerbated this trend.
- In addition, industry experts expect that issues with licensing / permits of projects, delay in lending approvals due to practical reasons and impact on buyers' ability to complete acquisitions will also adversely affect the sector. Concerns also arise in relation to the risk of recovery of collections from buyers and pre-sale commitments (prepayment of reservation fees) subject to issuance of permits and that such buyers may back-off.
- The Cyprus real estate sector has a significant reliance on foreign buyers, fuelled mainly by the Cyprus Investment Programme. With restrictions in air travel, coupled with rising economic uncertainty at a global level, this segment of the market is expected to be particularly hit.
- As a result, coastal areas - which had a higher reliance on foreign buyers-will be more severely impacted than Nicosia.
- Industry experts appear to be relatively optimistic, in terms of prices, as they expect prices to drop compared to last year but then to rebound.
- In the medium to long-term, the growth in online shopping and remote working is likely to cause a drop in retail real estate assets and to a lesser extent office space. Industrial assets, on the other hand, may stand to benefit.

Industry expectations and insights - Construction



Key Industry Insights/ expectations

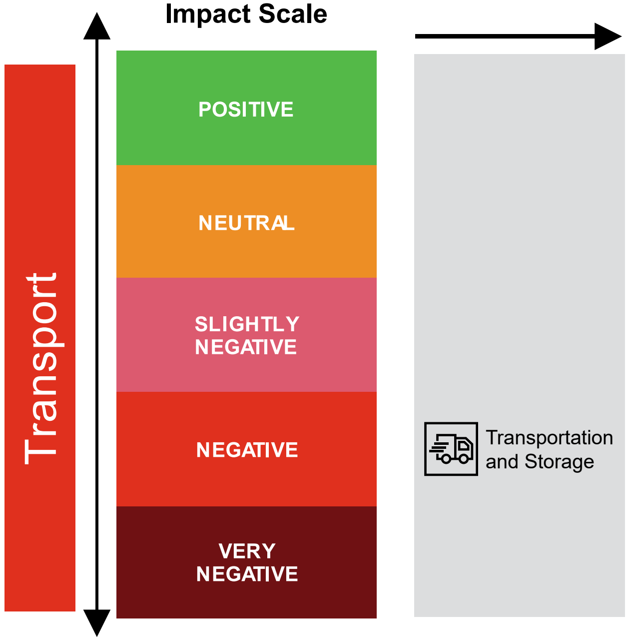
- Construction is of course closely correlated and relies on the appetite for real estate development - therefore the negative trends in real estate will inevitably affect construction activity.
- The sector has been under lockdown since 24 March - small sites (employing up to 3 workers) as well as some public sector projects allowed to operate.
- Upon the lifting of the lockdown in relation to construction sites on 4 May, activity fuelled by projects which are currently in progress has resumed.
- However, economic uncertainty and the reluctance of some companies or individuals to start new projects or even continue existing projects will impact the sector adversely.

Construction

8%

2019 Direct Contribution to GVA

Industry expectations and insights - Transport



Key Industry Insights/ expectations

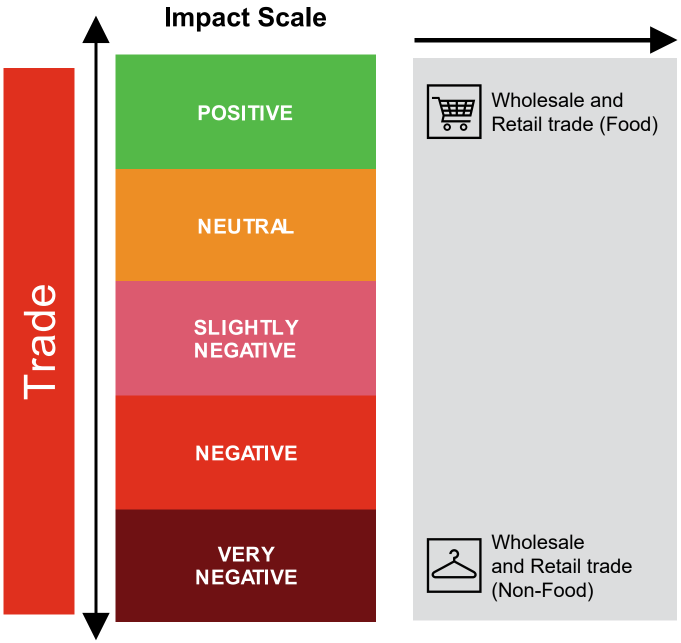
- Around 60% of the direct GVA of this sector is estimated to originate from shipping activities, driven by Cyprus' role as a ship-owning and ship management jurisdiction by many international players. The performance of this sector is therefore driven by market developments in the global shipping industry, and not on the specifics of the Cyprus lockdown, which in turn has been affected by the global trading environment in light of the pandemic.
- The local element of the transport sector relates to the distribution for the local supply chain, comprising forwarding, haulage, warehousing and other logistics activities. Such activities are therefore inevitably affected indirectly by the drop in the activity of their clientele, particularly in the non-food segment as well as materials in relation to construction.

Transportation and Storage

c.7%

2019 Direct Contribution to GVA

Industry expectations and insights - Trade



Wholesale and Retail

c.11%

2019 Direct Contribution to GVA

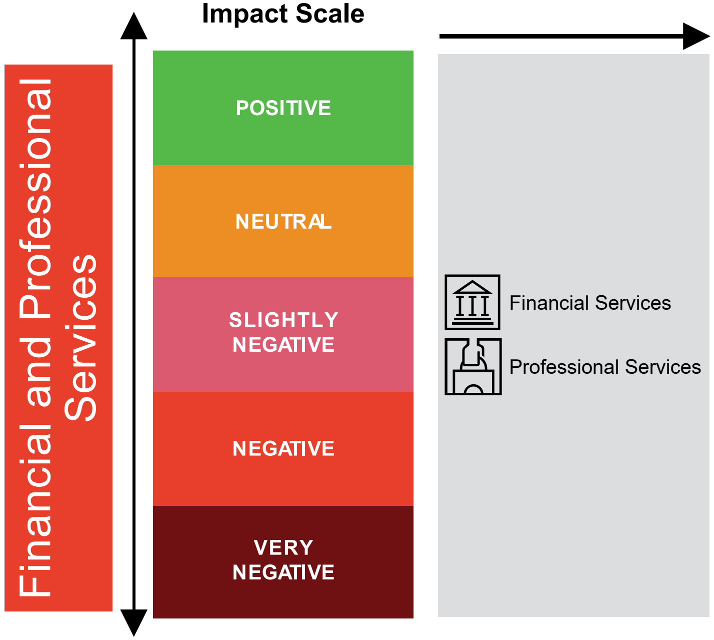
Food 3.7%

Non- Food 7.3%

Key Industry Insights/ expectations

- In line with global trends, retail trade of foodstuffs/ FMCG items has been positively impacted by the lockdown. There have not been significant supply chain disruptions in this sector, and Cyprus has not witnessed goods shortage in supermarket shelves.
- However, the sector will be negatively impacted by the significant drop in tourist arrivals this year, which will particularly affect the wholesale food chain (HORECA business).
- Non-food retail has of course been severely affected as it has been under lockdown. Industry players expect this year to be significantly impacted, especially in areas involving high-value items like cars and furniture, as consumers may choose to defer non-discretionary material spending. Other segments such as apparel, toys etc. may not be equally affected.
- Consumer behaviour will be adversely impacted by the fact that the disposable income of many employees across Cyprus may be negatively affected (see also Consumer Confidence Index on page 12). Consumer confidence, once tarnished, sometimes displays elements of stickiness despite improvement in fundamentals. On the other hand, loan instalment deferrals till the end of the year may affect consumption positively.
- The sector has been and will be witnessing acceleration of trends such as online shopping and players will be called to radically adjust their business and operating models.

Industry expectations and insights - Financial and Professional Services



Financial and Professional Services

c.14%

2019 Direct Contribution to GVA

Comprises mainly banks, insurance companies, accounting and legal firms.

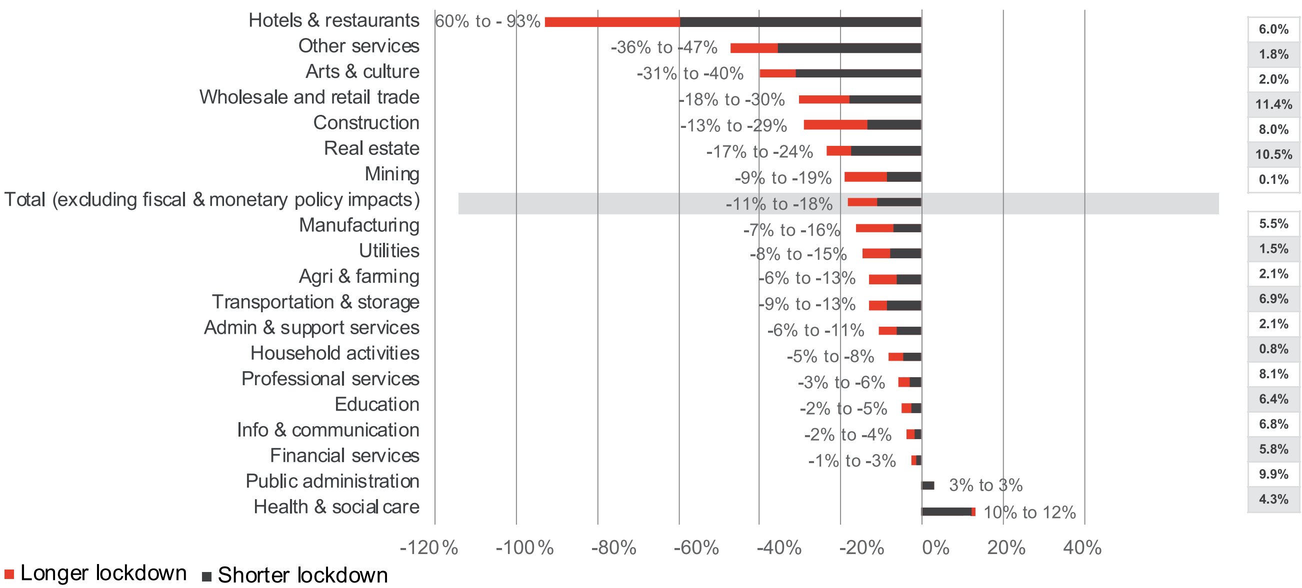
Key Industry Insights/ expectations

- Cyprus, being predominantly a services economy, has a significant reliance on banking, other financial services as well as professional services such as accounting, legal and consultancy services.
- Similar to other countries, the direct impact of COVID-19 on such sectors has not been significant, as this sector has not been under complete lockdown and/or majority of workers can work effectively from home.
- A possible direct impact of COVID-19 on professional services may relate to the drop in transaction activity both globally and in Cyprus, which has resulted in a respective drop in business activity for professional services.
- Despite the small direct impact, there will be indirect impacts from the reliance of such services on other sectors of the economy such as tourism, real estate and trade.
- In terms of the role of banks to provide much needed liquidity to the economy, banks in Cyprus have excess liquidity which could help fund the real economy. In addition, capital relief of c.€1.3bn will enable banks to grant loans and/or absorb losses on loans restructuring.
- A potential approval of the law for Government-backed guarantees may further stimulate lending; we understand that this is still the subject of debate between the Government and the political parties.
- On the other hand, banks remain vulnerable due to high NPLs which are expected to increase given the economic conditions. The period following the suspension/deferral of the loan payments is expected to expose the banks to a new wave of NPLs that will impose an additional burden to their financial performance. Ongoing transactions of banks to sell significant portions of their NPLs have been temporarily halted due to unfavourable timing. If the banks are able to recommence the loan disposal process and to sell the NPLs, de-risking of their balance sheets could further enhance their ability to support the economy. However, the rising unemployment and corporate distress as a result of COVID-19, may worsen the economic environment in which they operate and, as a result, the number of borrowers that can be considered viable and to which credit can be extended, will be limited.

Our estimates show biggest impacts for hospitality, trade, construction and real estate

Our sectoral analysis shows that some of the industries which have a substantial share in GVA and are likely to experience the greatest economic impact in 2020 are Hospitality (Hotels and Restaurants), Trade, Construction and Real Estate. Hospitality is particularly hit due to the dominant reliance on tourism from countries hit by COVID-19, such as the UK and Russia. Other sectors like Manufacturing, Transport and Utilities have limited direct impacts but are impacted through indirect shocks from other sectors. Similar to trends in other countries, Education, Financial Services and Professional Services have lower negative impacts but again they are also expected to have indirect impact from other sectors. Finally, there is also marginal offsetting from Public Administration and Healthcare. The total impact of -11% to -18% is before the positive impact from fiscal and monetary response.

% impact on 2020 GVA relative to 2019 by Sector - Shorter vs longer lockdown



Source: PwC analysis, Cystat

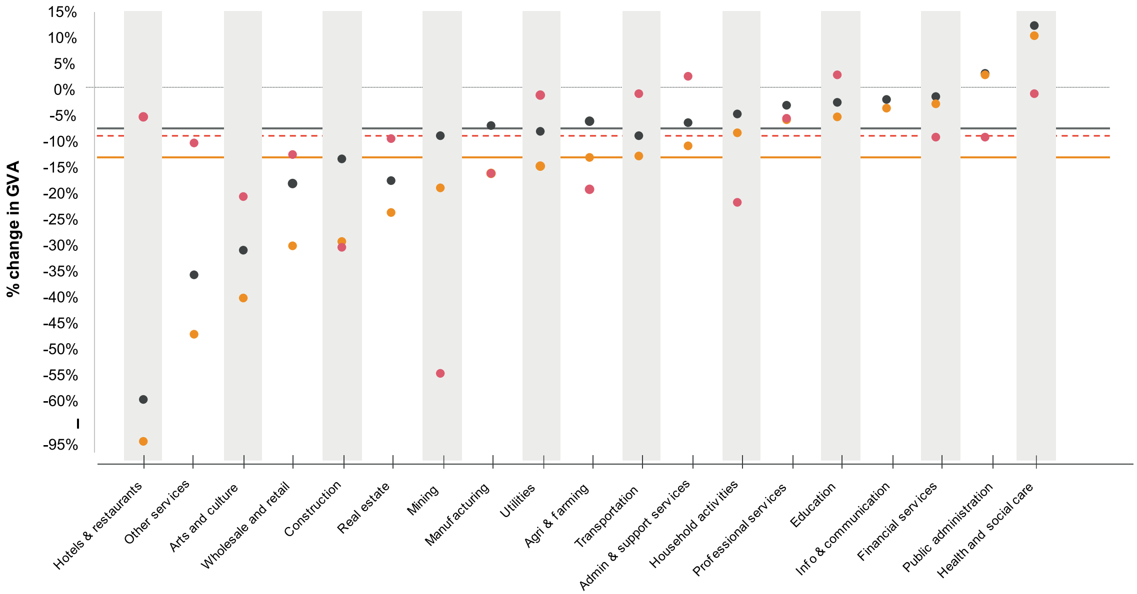
Commentary

- The I-0 approach helps identify points of most negative impact, including supply chain effects. Refer to Annex.
- These impacts stem largely from demand-side effects, and we assume that the economy re-allocates labour to where it is needed.
- Our analysis also implicitly assumes that policy action is sufficient to prevent a very large wave of corporate insolvencies (though there are bound to be some in practice).

COVID-19 sector impacts vs 2013 crisis

Sectoral GDP impacts in the shorter and longer lockdown scenarios in 2020 vs actual 2012-2014 impacts

	Hotels & restaurants	Other services	Arts and culture	Wholesale and retail	Construction	Real estate	Mining	Manufacturing	Utilities	Agri & farming	Transportation	Admin & support services	Household activities	Professional services	Education	Info & communication	Financial services	Public administration	Health and social care
% of 2012 GVA (real terms)	5.7%	1.7%	2.0%	11.0%	6.8%	10.7%	0.1%	4.9%	1.9%	2.4%	6.9%	1.5%	1.2%	7.6%	6.3%	3.7%	9.5%	12.0%	4.1%
% of 2019 GVA (real terms)	6.0%	1.8%	2.0%	11.4%	8.0%	10.5%	0.1%	5.5%	1.5%	2.1%	6.9%	2.1%	0.8%	8.1%	6.4%	6.8%	5.8%	9.9%	4.3%



Source: PwC analysis, Cystat

● COVID-19 Shorter lock down ● COVID-19 Longer lock down ● 2012-2014

—— GDP impact (COVID-19 shorter lock down drop) —— GDP impact (COVID-19 longer lock down drop) ---- GDP impact (2012-2014)

Commentary

- While the potential scale of the annual GDP impact under the shorter lockdown scenario of -7.6% could be broadly similar in magnitude to the experience of 2013 crisis of -8.5% (cumulative fall in GDP between 2012 and 2014), there are significant differences in sector impact. As expected, this is primarily due to the very different nature of the two crises.
- The key sectors expected to be impacted by COVID-19, for which 2013/2014 performance was significantly better, mainly include Hotels and Restaurants and Other service activities.
- In 2013/2014, Financial Services had a higher impact as banks were at the epicentre of the crisis and Public Administration was also hit due to public sector employee pay cuts in an effort to handle the fiscal crisis.
- Sectors negatively affected in both crises but to a different degree include Construction, Real estate and Wholesale and Retail trade, which tend to suffer in a general economic downturn.

4

Annex - methodological details

Methodology for assessing impacts by channel (1 of 2)

- **Annual vs quarterly:**
  This report focuses on estimated impacts on annual GDP/GVA in 2020, but these are based on a quarterly model where output falls sharply in Q2 2020 and then recovers at varying rates in different scenarios later in the year.

- **Sector lockdown:**
  We first use a bottom-up, sector-by-sector approach, leveraging the knowledge of our sector experts to build a view on how lockdown will directly impact the key sectors (hospitality, arts and entertainment, construction etc). We then use OECD Input-Output tables to model the knock-on effects through the supply chain, as reduced demand in these sectors has further impacts on the sectors which supply them.

- **Uncertainty - consumer expenditure:**
  This is modelled as a response to the reduction in labour income arising as the lockdown reduces GVA in each sector. This has a knock on effect on consumption, which is more acute for more labour-intensive sectors.

- **Uncertainty - business investment:**
  Based on our bottom-up view of the direct sector impacts, we translate this into an impact on investment – for example reduced turnover in the construction sector has reduced investment spending as a counterpart.

- **Labour supply impacts:**
  These are assessed in five categories covering workers that are: a) self isolating; b) infected and not ill; c) infected and ill; d) caring for dependants; e) not affected by the disease. We assume the first four segments of the workforce lose between 75-100% of their working hours during absence and calculate the total number of hours worked lost. For Cyprus, the impact comes mainly from d), as infection rates have been low. In this analysis, we don't take into account the productivity improvements that could potentially result from adjusting to lower staff levels, or the potential for continued home working by those with only mild symptoms.
- Further information on the Input-Output modelling approach is set out on pages 37-38.

Methodology for assessing impacts by channel (2 of 2)

- **Policy response - fiscal:**
  We categorised the fiscal support measures to combat COVID-19 into: a) additional day-to-day spending and b) tax relief measures. Each spending category is associated with a fiscal multiplier between 0.4 (tax relief) and 0.6 (expenditure) which we obtained from the University of Cyprus (**see Pashourtidou, Savva and Syrichas, 2014**). The fiscal impacts from the direct support provided to the health sector is calculated as a direct injection into the health sector, and as such is captured through the sector IO impacts. We have excluded from our analysis any tax measures (such as VAT payment deferrals), as the net impact of these measures are likely to be negligible as consumption will be impacted when the deferred payments become due. We have, however, included the impact of the loan deferrals scheme, but used a smaller multiplier to account for the fact that repayments are deferred, rather than forgiven. We do not explicitly model the impact of Government loan guarantees, in the event relevant laws are approved by the House of Representatives, though these will help to limit downside risks to the economy relative to our two scenarios.

- **Policy response - monetary:**
  Monetary policy support is mainly driven by: (1) ECB capital relief measures, estimated to be worth €1.2bn in Cyprus, and (2) the delay in the implementation of the G-SIFI buffer by the Central Bank of Cyprus (CBC), worth €90m. The effect of the capital relief measures is captured as a reduction in bank capital requirements (CET1 / RWA ratio), and multiplied by an estimate of the output elasticity taken from a study by the Bank of International Settlements.

Type of fiscal support	Examples (non-exhaustive)	Multiplier
Additional day-to-day spending	• SME and corporate allowance for the full or partial suspension of operations • Special allowance for leave due to child care • Special sickness benefit • Self-employed allowance • Support for tourism, students, education and other spend	• A 1 percentage point decrease in the government expenditure-to-GDP ratio leads to a 0.6% reduction in output in the first year
Tax relief	• 3-month suspension of an increase in contribution to the General Health System	• A 1 percentage point increase in tax revenue-to-GDP ratio leads to a 0.4% reduction in output in the first year

We use an input - output approach to assess sector impacts…

The Input-Output model is a “snapshot” of the economy for a given year, which shows what each sector must consume (intermediate consumption) from every other sector in order to produce a €’s worth of goods or services (production output).

Input-Output Models

- are powerful tools used to assess economic impacts and are well established in modern research as well as commonly used in professional practice.
- allow for the estimation of direct, indirect and induced economic impacts along the entire supply chain.

Input-Output Models

- describe how primary inputs and products are used to produce further products and satisfy demand.
- use Input-Output-Tables, which illustrate the inter-industry transactions and have the ability to trace the effects of how the change in final demand for one sector impacts other sectors and the economy as a whole.

Impact Assessments, based on Input-Output Models

- can estimate the short-term economic impacts consequential from the sector lockdowns and labour supply disruptions.
- help assess the economic impact that policy interventions may have by incorporating a number of policy measures in the I-O model.

Exemplary Input - Output Table

From To		Intermediate demand			Final demand				Total demand
		Primary sector	Secondary sector	Tertiary sector	Public Consumption	Private Consumption	Investments	Exports	
Intemediate Inputs	Primary Sector								
	Seconday Sector		Q1				Q2		
	Tertiary Sector								
Intemediate Inputs	Wages & Salaries								
	Gross operating surplus		Q3						
	Taxes - subsidies								
	Imports								
Total Supply									

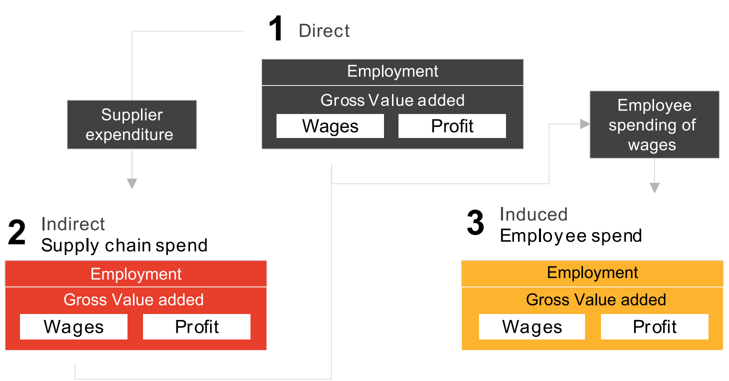
The use of the Input-Output approach facilitates the estimation of the short-term economic impacts of sector specific demand and supply shocks.

…through three main channels - direct, indirect and induced

We use Cyprus input-output (I-O) tables extracted from the OECD to model the economic impact of COVID-19 in the following three tiers:

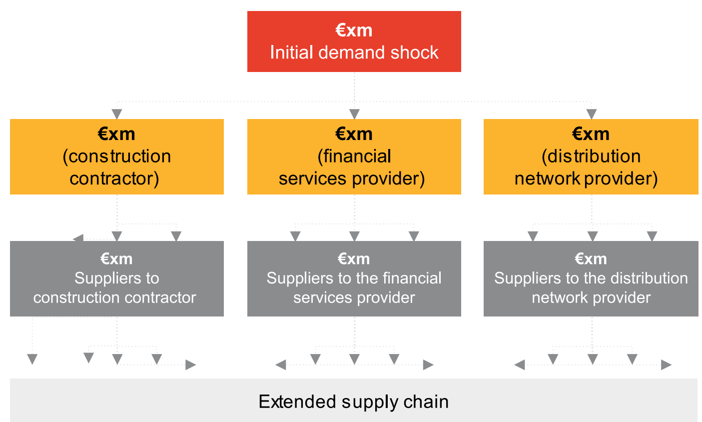
1. **Direct impact:** The impact in GVA (*) as a result of disruption brought about by COVID-19.
2. **Supply chain spend impact (indirect):** The impact in GVA through the supply chain - suppliers, their suppliers, etc.
3. **Employee spend impact (induced):** The impact in GVA in the wider economy as a result of lower wages and salaries that could be spent by employees.

The relationship between the three levels of economic contribution



*Note: GVA = Gross Valued Added (a sectoral version of GDP) i.e. an industry's contribution to GDP

A simplified representation of the relation between COVID-19's direct impact and its impacts through the supply chain



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Contact us:

Constantinos Constantinou
Partner
Head of Advisory
constantinos.constantinou@pwc.com
Tel: +357 22 555 700

Michalis Stephanou
Partner
Deals
michalis.stephanou@pwc.com
Tel: +357 22 555 770

Dr Jonathan Gillham
Director
Economics Consulting (PwC UK)
jonathan.gillham@pwc.com
Tel: +44 (0) 771 456 7297

Socrates Paschalis
Director
Deals
socrates.paschalis@pwc.com
Tel: +357 22 555 769

Barret Kupelian
Senior Consultant Economist
Economics Consulting (PwC UK)
barret.g.kupelian@pwc.com
Tel: +44 (0) 771 156 2331

Christina Christodoulou
Manager
Deals
christina.christodoulou@pwc.com
Tel: +357 22 555 096

For more information on the wider business impact of COVID-19, please see our website at:

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