Investment and Investment Finance: The Cypriot Case

Conference Report

The conference "Investment and Investment Finance: The Cypriot Case" held in Nicosia, Cyprus, on 26 September 2019 was organized jointly by the Nicosia Chamber of Commerce and Industry and the European Investment Bank. This report summarizes the content of the presentations and discussions.

Main interventions

In his opening address, **Stelios Anastasiades**, President of the Nicosia Chamber of Commerce and Industry, underlined the EIB role in promoting investment and economic prosperity. The EIB's long engagement in Cyprus led to EIB financing of 50 projects in the public sector and 350 in the private sector over 25 years. The EIB's country event contributed to increasing awareness of barriers to investments and obstacles to economic growth in Cyprus.

Marjut Falkstedt, Secretary General of the European Investment Bank, emphasized the long-term challenges for Cyprus. In its 60 years of existence the EIB has funded 12000 projects and mobilized about EUR 3tr of investment in 60 countries. With a balance sheet of EUR 300bn, a lending volume of EUR 64bn and 800 projects per year, the EIB is having a long lasting economic and social impact. The investment realized in 2018 alone will create 1.2mn new jobs by 2021 and increase GDP by 1.1%. As a testament to its commitment to sustaining the environment, the EIB intends to change its lending mix by 2020 and raise lending to projects towards climate change mitigation and adaptation to 50% from 30% currently. All EIB operations will comply with the Paris Agreement by 2020. While barriers to investment in Cyprus are higher than in the EU, the economy is benefiting from a constructive business environment. As a trusted partner of Cyprus, the EIB has a significant pipeline of innovation and infrastructure transport projects.

Yiorgos Lakkotrypis, Minister of Energy, Commerce and Industry, acknowledged the EIB Investment Survey (EIBIS) as the most valuable source of information available to both the private and the public sector to identify barriers to investment. To address barriers to investment relating to the high cost of energy, the government was aiming to introduce a competitive electricity market to support large scale projects in renewable energy and specialized schemes for self-generating energy for companies. Minister Lakkotrypis also referred to the government investment of EUR 300mn in transporting LNG; the use of the newly founded natural gas in order to produce electricity and the change in the energy mix with the objective of 20% of renewable energy by 2022. Reference was made to EUR 100mn in private sector supporting schemes between 2014-2020 from the ministry of energy, tax exemptions for companies investing in intangibles and innovative technologies. In order to support innovation, the government recently appointed a Chief Scientist, a National Board on innovation and a deputy minister on innovation.

Debora Revoltella, Director of the Economics Department, European Investment Bank, underlined that investment is recovering but is still below the pre-crisis level. Firms in Cyprus are as concerned with investment dynamics as elsewhere in the EU. Political environment and economic dynamics are turning negative in firms' perceptions, but to a lower extent that in the EU as a whole. While firms in Cyprus are still lagging behind in active innovation, they are apace with their EU peers in adopting digital technologies. Debora Revoltella pointed out that, in the survey, there are firms reporting no investment plans in the forthcoming three years, probably because they are at the restructuring phase and confronted with legacy issues. Some firms, however, report that they have invested too much. Long-term barriers to investment include uncertainty related to trade issues and Brexit and high cost of energy. Availability of skilled workers and the regulatory environment are also important barriers to investment. Access to finance is improving over time and remains at levels comparable to those in the rest of the EU. Collateral requirement and cost of credit are the most important financing constraints, with manufacturing and small firms being mostly affected.

Panel I moderated by **Haritini Tsangari**, Professor and Associate Head of the Department of Economics and Finance, School of Business, University of Nicosia, focused on Investment in Cyprus - Corporate Perspective.

Christodoulos E. Angastiniotis, President of the Cyprus Chamber of Commerce and Industry, emphasized that Cyprus is an attractive investment destination due to its quality of life, EU/EUR membership, education, and tax system. It is an important regional financial and investment hub for energy, services, funds, tourism and shipping. It has potentials for further investment in theme parks and marinas. The country's investment profile further improved following the sovereign rating upgrades. In his view, there was no lack of access to capital, but a lack of good projects in the market or businesses to demand funding. He highlighted the need to discourage strategic defaults and encourage banks to lend.

Anita Fürstenberg, Director, Operations Directorate, European Investment Bank, underlined that Cyprus is EIB's largest client in the region with an exposure of 13% of Cyprus's GDP. Recently, EIB-funded projects include the University of Cyprus, Institute of Neurology extension, wind farm in Cyprus and several other infrastructure projects. EIB's support to Cyprus intensified immediately after the crisis with credit lines to SMEs guaranteed by the Cypriot government to which all banks have access. Of the EUR 1bn available, commitments of EUR 750mn have been signed, and EUR 650mn have been disbursed to SMEs providing them with funding at interest rates lower than otherwise available. To support investment in climate change mitigation and adaptation, the climate efficient fund maintained by the Cypriot government is complemented with an EIB credit line. There is still a lack of good projects in climate change mitigation and adaptation in Cyprus as in many EU countries and the Advisory Hub is helping in that regard.

Charis Pouangare, Deputy CEO of the Bank of Cyprus, underlined that the Bank of Cyprus has half a billion euros in European programs of which 48% is to firms up to nine employees and 33% to firms with 10 to 49 employees. These programs cover investment, working capital and even overdrafts. The Bank of Cyprus intends to give EUR 2bn in new loans to firms in Cyprus in 2019. Charis Pouangare explained that, while banks have excess liquidity and are willing to lend, there is an insufficient number of good projects ready for finance.

In the discussion, **Anita Fürstenberg** stressed that the EIB funding will be aligned with the Paris agreement by 2020. **Christodoulos E. Angastiniotis** argued that bureaucracy is a problem for an investor. A new investment law is in the parliament according to which eligible investments that qualify as strategic and comply with specific requirements would be licensed in 3 months. An investment officer would be assigned by the competent ministry for each such investment in order to overcome bureaucracy.

Maria Heracleous, Executive Member of the Board of Directors, Central Bank of Cyprus, in her keynote speech reiterated that the Cypriot economy staged an impressive come back with GDP currently exceeding its pre-crisis level. The government budget is registering sizeable fiscal surpluses and the sovereign regained its investment grade credit rating resulting into lower yields. Yet, there are still challenges. Non-performing loans are high at 32% of total loans and remain higher than elsewhere in the euro area. Productivity is low, digitalization is hampered by low investment in Research and Development and there is a lack of skilled labour, while bureaucracy reduces the attractiveness of the economy. Targeted investment is needed in order to remove the barriers and have a virtuous cycle in innovation, technology and developing skills that would improve productivity.

Panel II which was moderated by **Savia Orphanidou**, Economic Officer, Ministry of Finance, focused on Investment and Investment Finance in Cyprus.

George Kyriacou, Director of Economic Analysis and Research, Central Bank of Cyprus, emphasized that economic activity in Cyprus recorded a successful catching up to the euro area after 2016. Economic growth was mostly attributable to consumption as investment was low, but investment is now catching up with that in the euro area. Recovery in non residential private investment is particularly strong. He noted foreclosed private properties transferred to the government resulting result in a drop in other private investment in the later part of each calendar year. He finally stressed a number of challenges, including the need to diversify sources of financing investment, to reduce lengthy judicial process, to improve public efficiency, innovation, and contract enforcement.

George Nishiotis, Associate Professor of Finance, University of Cyprus, focused on two issues namely, cash flow uncertainty and ease of doing business. First, cash-flow uncertainty is determined by the institutional environment, macro and business-related risks that result into a higher cost of funding. Second, Cyprus is ranked 126th in dealing with construction permits and 138th in enforcing contracts in the Ease of Doing Business 2019 among 190 countries, illustrating the country's bureaucratic burden.

Marios Tannousis, Deputy Director General, Cyprus Investment Promotion Agency (CIPA), emphasized the importance of the growing fund industry in Cyprus. In 2018 EUR 6.7bn of assets were under management, an increase by 14% since 2016. About 1/3 of that investment goes to investments in Cyprus. There are more than 150 investment funds authorized in Cyprus, of which 31 EU fund management companies. The way forward includes increasing the number of funds. A private equity fund of EUR 20mn capitalization, for example, has been set by the government in collaboration with the private sector in order to finance SME projects.

Christos Paschalides, European Commission, European Semester Officer in Cyprus, underlined that digitalization serves as a channel of innovation across all sectors of the economy. EU strategies recognize the potential for Artificial Intelligence and develop the necessary regulatory framework. The country is ranked 22nd in the EU in terms of digital skills. Main issues include the limited interaction between academia and businesses; low Research and Development spending; the high administrative burden; access to finance and limited digital skills. Nevertheless, the appointment of the Chief scientist and the National Board on Innovation are steps in the right direction.

In the discussion, while **Marios Tannousis** and **George Kyriacou** pointed to an insufficient number of good projects ready for finance, **Christos Paschalides** stressed the need for alternative sources of funding. In that regard the government support fund for SMEs could help. **George Kyriacou** acknowledged that there are payment issues like money laundering as it takes 5 months to complete a Know Your Client (KYC) process. **Christos Paschalides** suggested that digitalization could help speeding up the KYC process. M**arios Tannousis** underlined that funding is available for small projects but for large projects a syndication or the participation from an international financial institution is needed. **George Nishiotis** added that it is necessary to provide affordable sources of financing, stressing the important role of the EIB. On the interaction between academia and businesses, **George Nishiotis** added that universities have been producing good quality research, but academics were so far not allowed to participate in start ups. Looking forward a new law would allow the participation of researchers in start ups.